COMPETITION POLICY IN ASIA

Essays on Recent Development

Edited by Vanessa Yanhua Zhang

This book is dedicated to Professor Jean-Jacque Laffont and Professor Jean Tirole
– who taught us competition and regulation.

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Douglas H. Ginsburg

Competition Policy International has been publishing articles by antitrust scholars, lawyers, and regulators since its inception in 2004. In 2011 it first dedicated a portion of each issue to the Asia Column, edited by Vanessa Yanhua Zhang, and thereby created what is now the premier forum chronicling antitrust developments in the region, which abound.

The national antitrust agencies in Asia are, with two exceptions, relatively recent in origin. The newest agency, the Competition Commission of Hong Kong, began to operate in 2013; the Competition Commission of India became fully operational in 2009. And the Chinese Anti-Monopoly Law went into effect in 2008. Even the more mature agencies in the region, the Fair Trade Commissions of Japan and of Korea, have undergone substantial changes in direction in recent years. In sum, antitrust in Asia is in a state of rapid change and development at a time when Asian nations have become increasingly important to the global economy, both as major exporters and, more recently, as importers of goods and of foreign direct investment. It is no wonder the attention of the worldwide competition community is newly focused upon antitrust in Asia, and therefore upon the reports and analyses that appear in CPI's Asia Column.

The authors whose reflections make up these pages are participants in a collective intellectual effort to develop legal competition frameworks and competition cultures in the many Asian nations now making a serious effort to establish an enduring, predictable, and successful competition policy. In the United States, the effort to fashion a body of coherent economically based competition law took nearly a century, from passage of the Sherman Act of 1890 to the incorporation of rigorous economic analyses into the policies of the enforcement agencies and into the decisions of the courts. By contrast, the pace of competition law development in Asia, as reflected in published agency policies and increasingly in court decisions, is quite remarkable.

Across the region, competition agencies are not only working to develop and refine their application of the law; they are also expanding and defining the bounds of their enforcement by applying their national competition laws more aggressively to foreign participants in their markets and to those undertakings' overseas parent corporations. The essays in this book, in recounting that work, paint the picture of a dynamic Asia in which competition regimes are doing in a few years what the United States and the European Commission took decades to accomplish.

The process of maturation is neither consistent nor without difficulties, however, as documented in several of the essays that follow. During its own long period of maturation, the United States' competition policy suffered growing pains. Similarly, each Asian nation's unique legal, governmental, and business regimes are testing the flexibility and transferability of competition law, the central tenets of which typically were borrowed from the older regimes of the United States and Europe. K K Sharma, for example, recounts the enormous political as well as technical exertion required to bring the enforcement provisions of India's Competition Act into force. Evans, Zhang, and Zhang, in their contribution, show how the National Development and Reform Commission and Chinese courts are harmonizing the unfair pricing provisions of the Anti-Monopoly Law with the approach to unfair pricing taken by the European Commission and the United States.

The essays in this book also highlight the shared global circumstances that have shaped Asian antitrust policies. Just as it is hardly possible to contextualize global economic policy without reference to the pandemic economic crisis of 2008, so it is impossible to ignore the incentive that crisis created for Asian policy makers to find new ways to advance their countries' economic recoveries, including the use of antitrust policy to promote new — and new kinds of — growth. Hwang Lee illuminates the Korean government's emphasis upon protecting small- and medium-sized enterprises — viewed as potential drivers in a new Korean economy — from unfair trade practices. Michael Han and Kexin Li point to the statements made by a High Court judge suggesting that Chinese companies use antitrust litigation to surmount the technological challenges presented by multinational patent-holders and to advance home-grown development.

At the same time, this collection underscores the increasingly interconnected world in which both private companies and national competition agencies must operate. Indeed, as reflected in several articles, Asian competition authorities have begun to challenge more aggressively what they see as the anticompetitive conduct of international actors. Chester Toh, for example, highlights a recent enforcement action by the Competition Commission of Singapore that resulted in the imposition of fines not only against Singaporean companies but also against their Japanese parents.

The development of an economically-based competition policy, which is the express goal of most Asian antitrust authorities, may be described, to borrow a phrase from Deng Xiaoping, as an effort to "seek truth from facts," that is, to determine by trial and error, whilst relying upon the best available empirical evidence, what works to promote market efficiency and to enhance consumer welfare. That project may be more rapidly advanced, however, when we also seek truth from each other. As can be seen from the essays in this volume, East and West are doing so more consistently and more enthusiastically than ever before. This book enhances their exchange as it welcomes readers to join the authors in that ongoing dialogue.

ABOUT THE EDITOR

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Dr. Vanessa Yanhua Zhang is a Director at Global Economics Group and Senior Researcher at Market & Regulation Law Center (MRLC) of Renmin University. She serves as the chief editor of Asia Column at Competition Policy International (CPI).

Dr. Zhang is the author of several academic articles on the Anti-Monopoly Law (AML), economic analysis of mergers, conspiracies, and industry restructuring and has published in peer-reviewed journals such as Journal of Competition Law and Economics, Review of Industrial Organization, Annals of Economics and Statistics (Annales d'Economie et Statistique), Competition Policy International, etc., and contributed to several books on competition policy and regulation. She is recognized by Euromoney's "2010-2014 Expert Guide to the World's Leading Competition and Antitrust Lawyers/Economists: China."

Dr. Zhang specializes in economics analysis in competition policy. She has worked a wide range of competition matters involving allegations of monopolization, foreclosure practices, vertical restraints, merger analysis and intellectual property. She has consulted on projects across various industries, such as payment card, banking, pharmaceutical, high tech, electricity, telecommunication, internet and consumer products. She has submitted expert reports before the Supreme People's Court of China, the Guangdong High People's Court, National Development and Reform Commission (NDRC) and the Anti-Monopoly Bureau of Ministry of Commerce (MOFCOM).

Dr. Zhang has taught at Renmin University of China and worked as a visiting researcher at CPB Netherlands Bureau for Economic Policy Analysis. She holds a Ph.D. in economics from Toulouse School of Economics in France and a B.A. in economics from Peking University in China.

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2014

The First Antitrust Decicion By The Chinese Supreme People's Court Qihoo 360 Vs. Tencent

The Chinese Supreme People's Court issued its first antitrust judgment in Qihoo 360 v. Tencent on October 16, 2014. In affirming a lower court ruling in favor of defendant Tencent, the Court addressed the question of market definition and market power in the context of dynamic platform-based businesses in which products are provided for "free". It is one of the most influential cases in the 65-year history of the Supreme Court according to the People's Court Daily.

CPI gathered leading antitrust lawyers and economists to discuss the implications of the Tencent judgment for antitrust in China and for Internet-based cases in other jurisdictions. The webinar was held on 16 December 2014.

Professor D. Daniel Sokol moderated a discussion with Antonio Bavasso, Dr. David S. Evans, Willard Tom, and Dr. Vanessa Yanhua Zhang. Evans and Zhang, with Global Economics Group, advised Tencent and submitted testimony to the Chinese Supreme People's Court. Bavasso is a partner at Allen & Overy in London and Will Tom is a partner at Morgan Lewis in Washington D.C. and former General Counsel of the US Federal Trade Commission. Danny Sokol teaches at University of Florida Law School and is Senior Of Counsel to Wilson Sonsini Goodrich & Rosati.

The following is a transcript of the webinar.

Daniel Sokol: Welcome to the CPI webinar, "The First Antitrust Decision by the Chinese Supreme People's Court, Qihoo 360 versus Tencent." I am Professor Daniel Sokol. With me are a number of excellent panelists who are going to provide analytical insights into this historic decision.

First we have David Evans, Chairman of the Global Economics Group. David has provided economic advice on a wide range of industries but has special expertise on platform based businesses, which some of us know of as two-sided markets. David currently teaches economics and antitrust at the University of Chicago Law School where he is a lecturer and at University College London where he is a visiting professor and is co-founder and co-director of the Jevons Institute.

Let me also add, David contributed a brilliant chapter to the Oxford Handbook of International Antitrust Economics, Volume 1 which is out as of this month which I edited. I encourage people to take a look at it for what was really a wonderful piece of scholarship and background.

Dr. Vanessa Yanhua Zhang specializes in economic analysis and competition policy at Global Economics Group, where she heads the China practice. Dr. Zhang has taught regulation and antitrust economics to graduate students at Renmin University of China. She also serves as the editor of the Asia Antitrust Column at Competition Policy International. Together, David and Vanessa worked as the economic consultants in this case for Tencent. Their insights as a result are highly appreciated.

Also joining us on the law side are two distinguished lawyers. The first is Antonio Bavasso. Antonio is co-head of the Global Antitrust Practice in Allen & Overy. He advises clients on all aspects of competition law, practicing primarily in London and Brussels. In addition to his work at the law firm, Antonio also teaches the EU competition law course at UCL, and along with David, is the co-founder and co-director of the Jevons Institute.

Joining us from the United States is Will Tom. Will is a partner in Morgan Lewis' antitrust practice in Washington, DC, and former General Counsel of the Federal Trade Commission. This is one of a number of senior positions that Will has held at both the Federal Trade Commission and the Department of Justice Antitrust Division. Over his career, Will has been very active on antitrust IP matters. Specific to China, Will was very active in the development of outreach efforts to China while at the FTC.

With those introductions, let me just note we have a historic case. There are a number of issues that we're going to discuss about abuse of dominance in China. We'll discuss platforms, high tech industries, economic analysis and reasoning by the court.

I think that maybe what we could do is start with Vanessa. Who are these companies?

00:03:46

Vanessa Zhang: Thank you, Danny. So let me give you a brief introduction of those two companies in this case. Tencent is the largest instant messaging software producer or provider and offers various free services. Those free services include the instant messaging platform, which also called QQ, Weibo, which is a micro-blogging platform, online games, online security software, social network services, search engine and e-commerce.

Tencent makes profits from selling advertising to companies that want to reach Tencent users, selling virtual products or items for its online gaming services, charging its users for the bundled SMS packages, providing mobile games and charging for other mobile value-added service such as the mobile books.

As its main product, QQ has 340 million monthly users in November 2010 and 452 million monthly users as of April 2013 according to iRresearch.

Let's turn to the other company, Qihoo 360. Qihoo is the largest Internet security software provider. And it also provides free services such as online and mobile security software, a web browser and a game platform with the games developed by third-party game developers.

Qihoo 360 makes profit from selling advertising and providing web game services. Its main product is called 360 Safeguard. It had 275 million monthly users in November 2010 and 444 million monthly users as of April 2013. So that's the basic background of the two companies. Danny.

Daniel Sokol: Thank you. Well, ultimately in order to have a decision we need to have a legal claim. Will, I wonder if you might walk us through what is the legal issue here? What's the allegation?

Will Tom: Put very simply, the war started when Qihoo publicly claimed that Tencent QQ instant messenger invaded users' privacy and configured its security software to block QQ. In response, Tencent called on users to make an either/or choice between QQ and Qihoo's 360 software, and announced that it would block users who have installed 360 from using QQ. It also bundled the default installation of its own security software with QQ upgrades.

Through governmental intervention, compatibility was quickly restored, but Qihoo sued Tencent under Article 17 of the Anti-Monopoly Law, claiming that the either/or choice made to users was an abuse of a dominant market position.

Daniel Sokol: We're going to get into the details in just a little bit. The question for those listening is as follows - what are the key ramifications for the decision for Chinese antitrust? David, I wonder if you could take a first stab at this?

David Evans: Thanks, Danny and thanks Will and Vanessa for that introduction. I think there are three important ramifications. None of them really have to do with the abuse of dominance claim, which I don't think anyone really took very seriously. The court probably could have just bounced the case based on just looking at some of the details of the claim and the effects.

So the importance of the decision is really on market definition and market power analysis and how the courts are approaching that. There are really three things.

First, the court adopted what I think is a very modern approach to market definition and the analysis of market power. It said that market definition, and I'm using my own words here, but I think it characterizes it pretty well, that the market definition is really a guide and that it isn't necessary to establish rigid boundaries in doing a market definition analysis. So it didn't get stuck in the rigid market definition approach that is still used in the European Union and it used to be pretty common in the US as well.

It also found related to that that market share is really just one metric for assessing monopoly power and a metric that actually ought to be used with considerable care. So the Chinese Supreme Court isn't going to obsess about market share statistics. And that makes the Chinese approach similar to the approach that many economists and antitrust scholars have advocated and that got incorporated into the 2010 DOJ/FTC merger guidelines. So that's the first point.

A second point is that the Chinese Supreme Court and the intermediate court recognized the importance of two-sided platforms, two-sided markets, in conducting a sound antitrust analysis. Interestingly they followed the approach that the ECJ more or less took in the recent Cartes Bancaires decision, and that's really that the two-sided platform issues should be dealt with in the analysis of market power and effects rather than in market definition. But nonetheless, they took two-sided platforms seriously and made it clear that that needed to be part of the analysis.

Here's third thing. You know you always like decisions where you won better than those where you didn't win and I obviously come from that bias. But if you read the decision, it's clear that in their very first case the Chinese Supreme Court is very comfortable dealing with advanced topics in antitrust. You know you can quibble with various things that they do, but I think overall the decision reflects a highly nuanced understanding of antitrust concepts. They were able to get into SSNIP test and hypothetical monopoly tests and all sorts of relatively advanced topics in antitrust. And, again, whether you agree with them or not, it does seem to be an impressive first showing for the court.

Daniel Sokol: Thank you, David. First of all, let me start by saying I agree with you entirely that this is not an easy first case. I think the Supreme People's Court really did a fine job. But we have legal experts from two other important jurisdictions and I thought maybe to get their thoughts. Antonio, you haven't had a chance to chime in yet. And I thought especially since David did bring up Commission cases and EC law more broadly, and given that you teach exactly these things in addition to practice it, I thought we would start with you.

Antonio Bavasso: Thanks, Danny. Yes. I think this judgment is extremely interesting. First of all, my high level reaction is that the Supreme Court went very deep, as David said, into the facts. I don't know if this is a function of the legal test of the Supreme Court is applying. Perhaps they have more leeway to do so under the standard that is applied in China. But it is impressive how detailed their analysis is about the economic evidence and how comfortable they seem to be to analyze and come to a view on advanced topics of antitrust economics.

Four high-level points that jump off at me about this judgment.

The first one is when you read the judgment and compare to the intermediate decision, they do appear to do market definition analysis which is fairly focused on a functional distinction between the products. And they explicitly say that the markets that business people refer to may provide clues, but cannot replace a rigorous relevant market analysis. I'm obviously looking at an English translation of the judgment.

But then, and this is my second point, having defined the market rather narrowly, they don't get stuck in that narrow market definition. Rather they do look at the question of dominance in a much more economically-minded way than what we are used to in many other jurisdictions. Therefore, as David said, they don't attribute an excessive importance to market shares, notwithstanding what appear to be some fairly constraining limits coming from the Chinese legislation about market shares. Effectively even though they look at dominance starting from a fairly narrow market definition they look also at the effect of the behavior and, most interestingly, they infer from the lack of effect that there is probably not a dominant position at play here. So the effects analysis loops back into whether there is a dominant position in the first place.

The third that struck me is that The Supreme Court venture quite confidently into an analysis of entry and consider what are the effects of entry onto the behavior in question. Perhaps we can explore that later on during this seminar.

Fourthly, the last interesting point here, which differs from the practice that is developing (particularly in Europe), is that they stress very clearly that the burden of proving an abuse of dominance rests with the party alleging the abuse of dominance and not with the party that is alleged to have breached the relevant legislation through an abuse of dominance. And that is, again, procedurally very important point.

Daniel Sokol: Thank you, Antonio. So to recap, there are three major findings that David brought up. Number one, market definition is a guide but is not necessary to establish rigid boundaries. Number two, market share is just one metric for assessing monopoly power and should be used with care. And number three, while two-sided platform issues might not be relevant at the market definition stage, they can be considered in analysis of dominance.

Antonio then added a number of additional points to add clarity to the decision from a European perspective. Will, we would turn to you. It's been a while since a high-tech issue has come before the US Supreme Court. Since Actavis last year. What are your thoughts from the US perspective on this case?

Will Tom: Well, like the other speakers on this panel, I was really quite impressed. I did think that the opinion displayed quite a lot of sophistication both about the purpose and the techniques of the market definition. It understood that a hypothetical monopolist test was not a mechanical exercise but rather a means to assess the ability of the defendant to exercise market power. And it really, as Antonio said, delved pretty deeply into the facts specific to each proposed substitute in the course of its market definition, and went beyond market share to consider factors such as ease of entry and the impact of innovation.

I'm not sure it would be quite right to call its approach a functional analysis in the sense that if you delved into the old US Supreme Court law, it had talked about whether to define markets on the basis of what products are functionally substitutable, and rejected that approach because the mere fact of offering the same function doesn't really tell you very much about what would happen in the event that a party or parties actually tried to exercise market power. And I think this opinion really did focus on the right issue, which is the thought experiment that the hypothetical monopolist test is supposed to offer. If a hypothetical monopolist in the proposed market tried to exercise market power, what would happen? And so the court went beyond functional substitutes and looked at, for example, whether single function IM services would actually constrain the behavior of suppliers of comprehensive services. And I'm not sure it would have included those companies as participants in the market had it not been for its conclusion that such companies were rapid entrants into providing full function services.

Similarly, in looking at whether mobile instant messaging services should be included in the market, it really looked not just at the functional characteristics or whether they were functional substitutes, but it also to what barriers, such as equipment acquisition costs, would inhibit rapid substitution in the event of an exercise of market power. So from a US perspective, this is very close to how we would think about market definition and market power. Maybe for the same reason that David being on the winning side of the case says, boy, this is great, being an American lawyer and having an American approach to what market definition and market power is all about it strikes me that this is a really good decision because it's so close to the way we think about things.

Daniel Sokol: Will, that's incredibly helpful and particularly if you talk about different frameworks for thinking this through as an American. I'm actually going to try a different framework here. David and Vanessa, you were the economic experts for Tencent. How did that work in a Chinese context? You've had significant experience as experts in Europe, in the United States, in Latin America. What's it like working as economic experts in the Chinese context?

David Evans: Well, let me start, Danny, by taking that and then turn it over to Vanessa, who obviously was closer to the Chinese teams we were working just because the language of the case was obviously Chinese. Let me answer that just to give a flavor of this for both the US and European audience. While the Supreme Court and the Intermediate Court were willing to take oral testimony, my involvement in this was on the paper. So the submission of expert evidence in this by both parties and the interplay was really by the submission of reports. And if you looked at the English version of those reports, they would look very much like a US expert report or a white paper that you would submit to the European Commission laying out arguments and evidence. In that sense what we did was very similar to what we do in the US and Europe with the exception that unlike the US there wasn't necessarily the kind of cross examination that you have here.

For an American, for an English speaker, it was obviously an interesting experience because eventually everything needed to be done in Chinese. Just in terms of how we ended up doing the case, we initially worked in English, but then as things got far enough along and I was kind of comfortable with the arguments from my perspective, we switched to Chinese and I relied on Vanessa to tell me where changes were being made and so forth.

So that's the perspective from my standpoint. I think Vanessa can give you probably a closer perspective from the standpoint of Chinese national acting as an expert in China before the courts there.

00:24:08

Vanessa Zhang: Yes. Working on the antitrust litigation case in China has been very challenging. And it demands seamless integration of the international experts and a global team with the local counsels. Often time we have to work closely with the litigation team on the ground and with full understanding of the specificities of internet industry in China, market characteristics and modern industrial organization theory as well as the litigation strategy. So it doesn't just demand the interpretation of culture and language differences, but also demands full experience of products and services involved and the related theory that has been applied in the case.

So if we take a bigger picture of the court system in China, academic credentials have been highly regarded. And academic publications are one of the most important criteria for economic experts in antitrust cases in China. Chinese judges, especially the judges from the Supreme Court and the provincial courts such as high courts in Beijing, Shanghai and Guangdong, have various training programs throughout the year. And they have the opportunity to interact with international scholars and the practitioners on the development of modern economic theory and anti-trust practice. Therefore they dare to take further steps into the analysis and carry out rigorous reasoning before making a decision. Yeah, that's basically our understanding on how the case has been worked out in China.

00:25:58

David Evans: The other thing I would just add to that, Danny, and the thing that may surprise some people, is the Chinese Supreme Court, unlike – well, some would argue our Supreme Court and certainly unlike the European Court of Justice, the Supreme Court is interested in basically rehearing or hearing additional factual evidence. So at the Supreme Court level it was possible to submit not only new reports but also new arguments. And that's a feature of the Chinese system that's certainly unlike my experience in the US and Europe.

Daniel Sokol: Thank you both. Just as an aside, Vanessa, I've participated in one of those training programs for Chinese judges. I thought that the judges were incredibly sophisticated, asked great questions and really cared about getting things right. I wish in other jurisdictions, including my own home jurisdiction, judges were nearly that eager to learn.

I do want to move on to a substantive question, Vanessa, maybe that you could answer. The security software was free. This is sometimes a very difficult concept for judges to understand. The fact that the software was free, did that pose any complication for the court and how did the Court handle it?

00:27:27

Vanessa Zhang: Yeah, you are right, Danny. It indeed posed complication for the court. First of all, the court acknowledged the "free" nature of the two companies' business models. They found that Internet service providers use free basic services to attract mass users, then leverage those users in value-added services and advertising to make profits. In turn, Internet companies promote their free services by those profits. That's a prevailing business model of the Internet industry. That's also why Internet service providers compete on quality, services and innovation, etc.

Therefore, when defining the relevant market, the court realized there is a limit of using the traditional Hypothetical Monopoly Test (HMT) into the Internet-based instant messaging (IM) service. So the court didn't fully take into account the price increase, but suggested a modified version by accepting a significant change over quality. In other words, it didn't use SSNIP test (small but significant and non-transitory increase in price) but accepted the test with small but significant and non-transitory decrease in quality. It is also called SSNDQ test by the court. Being aware that quality decrease could not be easily assessed and the quality data is not available, the court suggested qualitative but not quantitative hypothetical monopoly test with decrease of quality.

In the analysis the Court actually relied on product characteristics, function, quality, how difficult to acquire such a product, and other relevant factors to assess the demands substitution. And they also realized that, when it is necessary, supply substitution should also be applied. Therefore, the Court analyzed substitution between instant messaging and Weibo, SNS, mobile text messaging and email. At the end, the Court made a conclusion that relevant market is IM service market in China.

Daniel Sokol: Thank you. I guess now that we've heard about how things worked in China, Will, any reactions that you might have based on your experiences?

Will Tom: Well, I guess the first reaction is looking at the difference between generalist courts and specialist courts. It is interesting to see how much in tune this court and this decision was with standard international antitrust thinking which in some sense shouldn't be surprising because unlike our judges, by and large, these judges go to training programs at which Professor Sokol will teach them how to think about these issues. And he's obviously a very good teacher.

So that's –

Daniel Sokol: Let me add, by the way, that Will, and for that matter David, have both been gets lecturers in my class. So I outsource the teaching to the more effective teachers.

David Evans: Thanks, Danny.

Will Tom: Yeah. And unlike in the Internet market, the advertising is free and the service is expensive. So you've had your free advertising, Danny. So that's reaction number one. And, you know we all know that there are advantages and disadvantages to specialist courts. But here I think it was a clear advantage. Secondly, I think the point about dealing with the fact that the services were free; it was interesting to see how seamlessly the court handled that. Again, by focusing on what is the purpose of this exercise. The SSNIP test isn't some set of commandments handed down on stone tablets, but rather it is a tool to understand whether this defendant could really do something bad in the marketplace. Is there really a capability to illegitimately exercise power? And so it didn't get hung up on, you know what are the mechanics of modeling a 5 percent increase in price when 5 percent of 0 is still 0? But rather it did the kind of thought experiment that a hypothetical monopolist test was invented to do. Namely if this defendant, which was accused of handing consumers an all-or-nothing choice or if you will, exclusive dealing or tying, however you want to characterize it, is it really capable of implementing a harm to the marketplace by so going? And if you think about the required bundling or tie-out if you want to call it that, as a kind of decrease in quality, the court asked itself whether the facts made it plausible for market power to be exercised that way. And when it went through the possible constraints on that behavior, it pretty readily concluded that market power could not be exercised despite high market share. So, again, I thought it handled the issues pretty well.

00:34:30

Daniel Sokol: Thank you Will. Antonio, does this look similar or different based on your European perspective?

Antonio Bavasso: A bit of both: in the sense that on the one hand the Court had to grapple with the question on market definition and the analysis of impact of decreases in quality. Interested in David and Vanessa's view, but I thought that analytically the Court got a little stuck in not following what the intermediate court had done, i.e. drawing an analogy between the decrease in quality and the potential increase in price (given that conceptually the way to estimate the decrease in quality could be done by assuming increase in price).

On the other hand – and so in common with many courts - they had to come to terms with market definition. Where the approach is very different is that The Supreme Court then goes to the effects analysis and uses its findings on the effects to conclude that the behavior in question does not constitute an abuse of dominant position. And in fact is on that basis, to conclude that they alleged infringer does not hold a dominant position in the first place.

That is a very different from analysis that would typically be carried out by – a European Court. A European Court would not typically call into question the finding of a dominant position based on the effects of the behavior of the allegedly dominant firm. In Europe there is much more of a two-stage approach. We define the market to determine where is the dominant position; we then look at the alleged abuses. We never go back to call into question the dominant position, which is probably one of the reasons why some judgments – not all of them do not make an awful lot of economic sense.

Daniel Sokol: Thank you for your honesty about your perceptions of some of the decisions. I actually want to take a step back, because I think it would be helpful for those in the audience to understand. Vanessa, what was Tencent's share in what the court defined as the relevant market?

Vanessa Zhang: Yes. It depends on the calibration of the market share. And the Court has noticed in the decision that it would be effective usage time, effective usage frequency and active users. The data that has been used in the case is from iResearch. But iResearch only provides the PC-based data, which does not include the mobile-based data. So if we take monthly effective usage time as an example, Tencent's share exceeds 80 percent among the PC-based instant messaging service providers. That's also shown in the decision.

Daniel Sokol: I'm glad you raised that. Because then it leads to a much more important question. If the answer is around 80 percent, maybe, David, I could throw this in your direction. The court agreed that Tencent was not dominant. So why is it that the court dismisses this market share evidence that looks quite significant on its face at least?

00:38:58

David Evans: Yeah. No, it's very interesting. So they – part of it is what Antonio described, which is sort of the backward looking from the effects. But there's also what I would characterize as kind of a forward-looking analysis as to whether Tencent was capable of doing bad stuff. And there it really came down to their view of dynamic competition in this sector in China. So they recognized what we would call leapfrog competition--not their term—but essentially leapfrog competition where firms are constantly introducing new features to create products that are better than the other guy's products. And where are firms that are basically forced to do that if they want to keep their position. And that Tencent in fact is forced to do that if it wants to keep anything like the share that it has. My recollection is they gave the example of Microsoft's instant messaging service, which, of course, is very successful out of China, collapsing in China because of the perception that its quality was not only not that good but also that it had declined.

The court also, as Antonio and Will pointed out, placed a lot of weight on the fact of entry and the possibility that entry could discipline the large players. Then finally, they recognized this the broad competition between the platforms, the internet platforms in China, and that what these companies are really trying to do is to acquire people's attention in order to monetize it in some other way. That was kind of a driving force between the competition that was taking place. So it was that kind of analysis of the realities of market competition, at least in my reading, that led them to not place a lot of weight on the static share statistic.

00:41:30

Daniel Sokol: So this leads to a broader question. How much of the analysis is really dependent on the fact that this was an internet industry? And maybe with this question I'll return to Antonio and Will. Antonio, do you want to maybe walk us through whether or not this is highly dependent on the particular industry?

Antonio Bavasso: Well, I don't know if it's dependent on the internet industry. I think it is generally dependent on what the court perceives to be the characteristics of this industry. And the importance that innovation plays in this sector and in these markets generally. But I wouldn't infer from that that the impact of this precedent is limited. I think that a similar analysis is equally applicable as a matter of principle in all sectors where innovation can lead to what David called leapfrog entry and development. It seems to me that the court thinks that that type of analysis is central to any finding of dominance and rightly so. So that approach is rooted in the characteristics of the particular market, but is equally applicable to those markets which display similar characteristics.

Daniel Sokol: Will? Any additional thoughts?

Will Tom: I very much agree with Antonio that this is not unique to internet industries but rather is a function of the specific market being analyzed and that the broad principles would apply to any markets. You can imagine lots of internet markets in which there really is the kind of degree of lock-in and barriers to entry that would make it possible to exercise market power. Just as you can imagine lots of brick and mortar industries in which rapid entry is possible. And we've had lots of cases in highly traditional markets in which high market shares were not deemed to confer market power because entry was easy.

So I think it is very fact-specific at the level of the individual market. But principles are broadly applicable. I guess the other thing I would add here is I do think that the court was reasonably disciplined in treating the issues of market definition, market power, and anticompetitive effect or abuse separately. And so I may disagree slightly with Antonio on this point. The emphasis on lack of market power despite the high market share was really based more on the ease of entry I think than on the lack of effect. And while there was certainly a section of the opinion that dealt with whether one could infer market power from the ability of defendant to engage in this conduct, and the court rejected that possibility, it was focused on whether one could make that inference and not the other direction of rebutting the existence of market power simply from the fact that this particular conduct didn't have an effect.

00:46:30

Daniel Sokol: Thank you, Will. You raise a number of important points that there have potentially broader implications. So I thought as the last question, in fact, I'd focus on that. What is the relevance of this decision in cases in other jurisdictions? If, in fact, there is any relevance. I don't know. David, why don't I start with you?

David Evans: Yeah. I think there are three things. Obviously I don't know all the decisions out there, but at least from what I've seen, this appears to me to be one of the most important decisions concerning the analysis of fast moving internet markets. You know the other one that comes to mind is the European Commissions decision approving Microsoft's acquisition of Skype. So even though the precedential value isn't necessarily just about the internet industries, I think it is a particularly good analysis of those kinds of markets.

Second, it confirms the importance to the analysis of multi-sided platforms in antitrust. And it really is one of the two high court decisions now that recognized the concept and uses it in the analysis. The other one, of course, is the European Court of Justices decision, in September 2014, in Cartes Baincaires. That's two high courts now – one in Europe and one interestingly in China-- that has adopted the multi-sided platform approach explicitly in a decision.

And third, since we're all doing advertising here, my personal favorite, it recognizes the importance of the work I've done on attention markets--where firms compete in a variety of ways to capture scarce attention from consumers and then monetize that attention through advertising or other means. And that's the framework that I brought to the expert opinion in the case. They seemed to have picked up on that in the analysis.

Those are the three things that I would mention. The one other point that I guess I'll make if I have some liberty on this, Danny, just to respond to – maybe to respond to Will and to Antonio and to raise a question. It does occur to me that, you know one of the interesting aspects of what happens to courts is sort of a path dependence issue. The fact that the Chinese courts are beginning their development of cases by having two cases that focus on Internet industries is interesting. You wonder whether the dynamics of antitrust law would be different if like the Europeans had started with a dynamic industry rather than bananas. I think it is interesting that the Chinese are starting their analysis of antitrust with these dynamic industries. That may itself have some impact on how antitrust evolves over there. Anyway, just kind of a random thought.

Daniel Sokol: That's all very helpful. Vanessa, you've spent a lot of time working in China, but you were trained at Toulouse. You live in the United States primarily. You also are truly a world citizen and understand a number of different jurisdictions. What do you think the impact might have on any of these other jurisdictions?

00:50:38

Vanessa Zhang: Yeah. We have seen, and probably the other panelists have already raised this comment, this is the first antitrust case ruled by the Supreme Court of China. And it's also the most significant antitrust case which has set up the standard for analyzing the abuse of dominant cases in China.

Given the fast growing Chinese internet market, there might be more and more competition issues which might not have taken place in the other jurisdictions. So it would be a good example for a national supreme court to take into account rigorous economic analysis and to apply the modern industrial organization concepts into the decision. On one hand, China is trying to learn experience and lessons from its peers and trying to get in line with the international best practice in antitrust enforcement. On the other hand, China is also contributing to the international antitrust community with its own experience and dares to adopt the cutting-edge economic theory such as two-sided market theory into the antitrust analysis, which also improves our understanding of competition issues in innovation-driven industries. That's a couple of my thoughts.

Daniel Sokol: Will?

00:52:16

Will Tom: I guess I'm going to step away from the importance of this decision in terms of the economics of it and the antitrust analysis and step back to the question of institutions and the interplay of different voices on the international stage. I think one of the most significant impacts is that China will have to be taken seriously as a major contributor and thinker in this area. It is assuming a place among equals. So I think that's one thing to think about and the implications of that.

A second point is that, of course the courts in China, at least so far, have spoken only in the context of private disputes. So it will be interesting to watch the other governmental institutions in China and see whether you see a similar degree of care and sophistication. Because the executive branch, if you will, is also assuming a place among equals in the international enforcement community, and because you do not, at least as yet, see the kind of unification of those institutions that flow from the fact that in the US, for example, the agencies have to prove their cases in court. I think the dynamic in China may be somewhat more complex.

But I think that, regardless, you're seeing a tremendous globalization of antitrust and it really underscores the importance of dialogue among both the enforcers and the courts to achieve some degree of consensus about how to approach these issues.

Daniel Sokol: Antonio, I leave the last word with you.

Antonio Bavasso: I think the point that David made about what he calls path dependency, which lawyers would probably call the value of precedents, is one of the most interesting ones to my mind. It's true that we perhaps need to distinguish the judicial setting, the judgment which represents a fine example of decision making from the administrative enforcement.

The point that I find fascinating is that when China adopted an antitrust regime, it looked at European rules. Inevitably, as a result, it inherited a certain degree of "path dependency" is the presumption relating to market shares that found their root in cases such as United Brands and so on. So they've inherited a little bit of that baggage.

But with this judgment the Supreme Court makes the most of being as a new kid on the block of judicial enforcement, the Supreme Court raises the stakes by adopting a very interesting judgment which does away and doesn't absorb into their judicial system all the fallacies and rigidities that have developed over the years; the rigidities coming from precedents that judges in Europe need to deal with. This is a new start with a very interesting and in many respect I would say innovative approach to those issues. So I think that the Judgment it's to be saluted as a great achievement judicially.

Daniel Sokol: Excellent. Again, this is Daniel Sokol, Professor of Law at the University of Florida and Senior Of Counsel at Wilson Sonsini. I want to thank all of our participants: David Evans of Global Economics Group, University of Chicago and University College London; Vanessa Yanhua Zhang of Global Economic Group and Renmin University; Antonio Bavasso of Allen & Overy and University College London; and Will Tom of Morgan Lewis. Thank you all very much for your participation.

Qihoo 360 v Tencent: First Antitrust Decision by The Supreme Court

David S. Evans

Vanessa Yanhua Zhang[1*]

On October 16, 2014, the Supreme People Court (hereinafter "the Supreme Court") of the People's Republic of China issued the decision on the dispute between Qihoo 360 and Tencent.[2] It is the first antitrust case decided by the Supreme Court in China and ends one of the most significant antitrust cases brought under the Anti-Monopoly Law ("AML").

The Supreme Court dismissed Qihoo 360's claims on exclusionary practices and anticompetitive bundling against Tencent and upheld the decision made by the court of first instance, the Guangdong High People's Court (Guangdong High Court). In the decision, the Supreme Court carried out a sophisticated antitrust analysis. It re-examined major issues such as market definition, market power and whether Tencent had abused its market power. The decision emphasized the importance of competitive constraints and dynamic competition. It also took into account the characteristics of multi-sided platforms (i.e. two-sided markets) in the assessment of market power.

It is a landmark decision for China and will likely influence how the Chinese courts approach these issues generally and for Internet industries particularly. It is also a significant decision by international standards. Released three days after the Nobel Prize was awarded to a French professor Jean Tirole of Toulouse School of Economics,[3] in part for his work on two-sided markets, it is one of the first decisions to consider the role of multi-sided platforms in antirust analysis. It is also one of the most detailed antitrust analyses of competition in modern Internet businesses.

1 * Evans is Chairman, Global Economics Group and teaches part time at the University of Chicago Law School and the University College London. Zhang is a Director, Global Economics Group and has taught at Renmin University of China. The authors, together with Howard Chang, a Principal of Global Economics Group, consulted for Tencent and prepared evidence and economic analysis on this matter, in particular multiple expert reports to the Supreme People's Court.

2 See the Supreme People Court of P.R. China Civil Judgment No. Minsanzhongzi 4/2013. The Chinese version is available at http://www.court.gov.cn/xwzx/yw/201410/t20141016_198470.htm.

3 See Scientific Background on the Sveriges Riksbank Prize in Economic Sciences in Memory of Alfred Nobel 2014, "Jean Tirole: Market Power and Regulation," October 13, 2014, available at http://www.nobelprize.org/nobel_prizes/economic-sciences/laureates/2014/advanced-economicsciences2014.pdf.

In this article, we will summarize the Supreme Court's approach to assess the issues of market definition, market power and abuse of dominance.

The Internet industry in China expanded rapidly beginning in the late 1990's. Overtime, many thousands of companies entered the Internet-based business. By the end of December 2013, the number of Internet users had increased to 618 million and 45.8 percent of the population. Mobile Internet users had reached 500 million by the end of December 2013, up 80 million from the end of 2012.[4]

The case involved a dispute between two internet companies in China. Tencent attracts users by providing a variety of free services including QQ (its IM platform), Weibo (its micro-blogging platform), online gaming, online security, SNS, search and e-commerce. The company makes money from selling virtual products/items for its online gaming services; charging its users for SMS packages, mobile games, and other mobile value-added services such as mobile books and mobile games; and selling advertising to companies that want to reach Tencent's users.[5]

Qihoo360 attracts users by providing a variety of free services including online and mobile security through anti-virus software, a web browser, a game platform with games developed by third-party game developers, and a search engine.[6] Qihoo 360's Safety Guard, which is an Internet security product, had 456 million monthly active users in April 2013.[7] Qihoo 360 profits through selling advertising, and providing web game services.

On November 3, 2010, Tencent required the users of its IM services to choose between Tencent's QQ or Qihoo 360 software. Tencent's users therefore had to use security software made by providers other than Qihoo 360, including Tencent's own security software. Tencent and Qihoo 360 both restored interoperation on November 4, 2010, the next day. This is the famous "choose-one-from-the-two" incident, also known as "non-interoperability" conduct.

The case was initially heard at the Guangdong High Court. The Guangdong High Court dismissed Qihoo 360's allegations in March 2013. Qihoo 360 appealed to the Supreme Court.

The Supreme Court carried out in-depth analysis of the dispute and focused on five major issues. We will just discuss the first three, which applied economic analysis: market definition, market power and abuse of dominance.

4 China Internet Network Information Center (CNNIC), Statistical Survey Report on the Internet Development in China, January 2014.

5 *See* Tencent 2011 annual report, p. 107.

6 See Qihoo's Prospectus 2011. See also Paul Mozur, "Qihoo 360's Zhou Hongyi: Taking Aim at China's Internet," Wall Street Journal, November 30, 2012, available at http://online.wsj.com/article/SB10001424052970204707104578094460340552442.html.

7 Qihoo 360 2012 annual report, p. 27.

1) MARKET DEFINITION

The Supreme Court acknowledged that it is not necessary to define a clear relevant market in every abuse of dominance case. It would focus more on the market power and the anti-competitive impact of the alleged conduct than market definition itself. As market definition is "just a tool to evaluate the undertaking's market power and the competitive impact of alleged monopolistic conducts but not the goal,"[8] as the Supreme Court stated, it confirmed that the court of first instance, Guangdong High Court, just analyzed the possibility of market boundary, but did not give a clear conclusion on the boundary of the relevant market.

When defining the relevant market, the Supreme Court acknowledged the general application of the SSNIP test (also known as the "Hypothetical Monopoly Test"—HMT) as a method of analysis. The Supreme Court, however, realized the application of the traditional SSNIP test to internet-based instant messaging (IM) services that features a "free" business model is limited. Instead, the Supreme Court relied on product characteristics to assess demand and supply substitution. They analyzed the substitution relationship between IM and Weibo, SNS, mobile text messaging and email. The court defined the relevant market as the IM service market in mainland China.

In particular, the Supreme Court highlighted the importance of dynamic competition when assessing the competition in Internet market:

"The Court finds that competition, especially internet competition, has dynamic characteristics. When defining relevant market, one should take into account of predictable and possible market reaction and changes in the future, in order to correctly decide whether there is any competitive constraint coming from other undertakings."[9]

Compared to the decision of the court of first instance, the Supreme Court excluded Weibo and SNS from the relevant market. It, however, supported the analysis method of the court of first instance which emphasized the importance of dynamic competition instead of just focusing on the static competition.

"In this case, the court of first instance takes into account of the current growth and future trend of Weibo and SNS when analyzing whether Weibo and SNS belong to the relevant product market. Such a way of reasoning isn't improper." [10]

Meanwhile, the Supreme Court acknowledged competition of Internet platforms and emphasized the assessment of competition should focus on the user's side. It would consider platform competition more in the assessment of market position and market power than in market definition.

8 See supra note 1.

9 See supra note 1.

10 See supra note 1.

2) MARKET POWER

The significance of the Supreme Court's decision in this case is to not simply rely on market share to assess whether Tencent has market dominant position. Given the defined relevant market, Tencent's shares all exceed 80 percent in both the PC and mobile IM market, which is also the main allegation of Qihoo 360. High market share does not necessarily mean market power, as Tencent claimed, which has been upheld by the Supreme Court. The Supreme Court moved further to evaluate other important factors.

First, the Supreme Court took into account the current competition in the IM market in mainland China. It found that "competition in such a relevant market is quite sufficient".[11] Evidence shows that at the time when the alleged conduct took place, there were over dozens of IMs on the market. These IM products and services have gotten more and more reliable and mature over time with a significant user base. Especially with the development of mobile communication, new mobile IM providers continuously enter into the market. The Supreme Court focused on the major characteristics of competition in IM market: innovation competition, dynamic competition and platform competition.

Second, the Supreme Court cared more about whether Tencent had the ability to control product price, quantity or other trading conditions. The court found that given the "free" nature of the IM market, users have no willingness to pay. Tencent therefore has no ability to control prices on users' side, let alone to decrease quality or control product quantity and other trading conditions.

The Supreme Court also analyzed financial power and technology conditions of Tencent, reliance of other undertakings on Tencent's QQ instant messaging software, and market entry. In particular, the Supreme Court emphasized the importance of market entry in assessing market power.

"When assessing whether there is market dominant position, it's important to evaluate the easiness of market entry and expansion of market share. Low market share doesn't necessarily mean weak market competitive constraint. If undertakings could quickly enter into the market and effectively expand market, they will provide effective competitive constraints to the incumbent."[12]

Based on the evidence, the Supreme Court found market entry in IM market to be relatively easy. It especially analyzed the "Choose One from The Two" incident. The court found:

"The appellee's "Choose-One-from-The-Two" conduct only lasted for one day. Such an incident caused Tencent's competitor MSN's users increase 23 million in the same month. Several competitors competed on IM market. This evidence strongly proves that Tencent doesn't have significant market dominant position."[13]

Therefore, the Supreme Court concluded that current evidence doesn't support the claim that Tencent possesses market dominant position.

11 See supra note 1.

12 See supra note 1.

13 See supra note 1.

3) ABUSE OF MARKET POWER

When assessing whether Tencent had abused market dominant position, the Supreme Court has weighed both negative and positive effects that such alleged conducts have brought to consumers and competition. It highlighted that "the focus of the AML is not an individual undertaking's interests, but whether the healthy market competition mechanism has been distorted or destroyed." [14]

The Court analyzed Tencent's two kinds of conducts that were alleged anti-competitive by Qihoo 360: (1) "choose-one–from-the-two" incident; (2) bundling of IM and security software.

Regarding (1), after detailed analysis, the Supreme Court found that Tencent had no significant incentive to take such "non-interoperability" conduct to exclude and restrict competition in the IM market. In addition, the court found that such a non-interoperability conduct actually brought vibrant competition to the IM service market although it only lasted for one day. The court also analyzed the impact of such a conduct on the security software market and found the impact was actually quite little. Such a result not only proved that Tencent's non-interoperability conduct was not abuse of dominance, but also proved that Tencent doesn't have a dominant position.

Regarding (2), the Supreme Court did not find reliable evidence to support the Qihoo 360's allegation that such bundling behavior leverages Tencent's leading position in the IM market into security software market. Meanwhile, the court found there were legitimate reasons for Tencent to bundle QQ IM with QQ Software Manager since such a bundle provided function integration and improvements to quality and security, which consequently promotes IM's features and value.

Therefore, the Supreme Court concluded that neither non-interoperability nor bundling conducts violates the AML.

As the first antitrust decision made by the Supreme Court, the Qihoo v. Tencent decision will have a significant influence in China's antitrust enforcement.

First, it sets up the standard for antitrust private litigation with detailed antitrust analysis of market definition in general, and in abuse of dominance cases in particular. Especially it lays out the road map for a proper and rigorous antitrust analysis in assessing market power and abuse of dominance issues.

Second, it demonstrates that the Chinese courts, barely six years after the AML went into effect, are already adept at rendering sophisticated antitrust opinions and applying modern economic concepts. It suggests that economic analysis, and economists, have played a significant role in private antitrust litigation in China as they have in US private antitrust litigation and in cases brought by the European Commission. Qihoo and Tencent both retained economists and introduced economic evidence before the Supreme Court.

Finally, it is one of the world's leading and most sophisticated antitrust decisions concerning competition in Internet-based industries. It contributes to a better understanding of the competition issues in such fast-growing industries by considering the role of dynamic competition and multi-sided platforms.

14 See supra note 1.

Antitrust Enforcement: China ups the ante

Michael Han

David Boyle[1]

INTRODUCTION

Over the past year China's antitrust authorities have come to the fore on the global antitrust stage with some notable decisions and investigations in the non-merger antirust area. Many of these investigations, involving large multinational companies (MNCs), have invoked criticism from some in the international business community with allegations of discrimination against foreign companies. While MNCs at the centre of recent antitrust probes may feel aggrieved, as many companies do when faced with an antitrust investigation, there may be more substance to these investigations than simply discriminating against foreign companies. In this article we will elaborate on this further and provide some possible alternative explanations as to why foreign MNCs have been investigated of late. We will also compare the recent enforcement actions with other enforcement actions taken by the Chinese antitrust authorities against domestic companies - cases which have not grasped international headlines in the same way as investigations against MNCs in China.

While the Chinese authorities have shown that competition law compliance is now a real consideration for global companies doing business in China and have made great strides in terms of improving enforcement, there is still room for improvement in the authorities' practices and procedures. In particular, the law needs to be clearer in certain areas, and transparency of the authorities' investigation process needs to be improved so businesses can have more certainty on when their activities may breach Chinese competition law.

BACKGROUND ON THE CHINESE ANTITRUST AGENCIES

Before delving deeper into the Chinese antitrust authorities' recent investigations, it is useful to provide a brief introduction to the Chinese authorities and their various competences. The PRC Anti-Monopoly Law ("AML") was introduced in 2007, therefore the enforcement of competition law in China is still quite new. This is worth noting when comparing China with other major jurisdictions such as the US and EU which have built up a vast body of case-law and best practices over decades of competition law enforcement.

1 Michael Han is an antitrust partner of Fangda Partners and David Boyle is an associate with the same firm.

Unlike other jurisdictions, China does not have an independent and unified antitrust enforcement agency. There are three regulatory authorities that enforce the AML at the national level: the National Development and Reform Commission ("NDRC"), the State Administration for Industry and Commerce ("SAIC") and the Ministry of Commerce ("MOFCOM").[2] This article will focus on the non-merger enforcement activities of the NDRC and the SAIC. The NDRC is mainly in charge of investigations involving price-related antitrust infringements (including both anticompetitive cartel or vertical agreements and abusive conduct) while the SAIC is responsible for the enforcement against non-price related antitrust infringements.[3] It is worth noting that these three ministries responsible for the enforcement of the AML each have numerous other responsibilities, not just competition enforcement. As well as the resource burden this places on the agencies, which already have limited resources,[4] the different mandates can lead to potential conflicts of interests which may not be the case with antitrust enforcement agencies in other jurisdictions.

SUMMARY OF HIGH PROFILE CASES INVOLVING MNCS

The investigations and fines imposed by the NDRC and the SAIC on MNCs have spanned a number of sectors and industries. MNCs such as Qualcomm, Tetra Pak, Danone (Dumex), Mead Johnson and Abbott have been investigated and/or fined by the NDRC and the SAIC since 2013. This year the list of companies under investigation has been extended to include other well-known brands such as Microsoft, FAW-Volkswagen's Audi and Chrysler.

The authorities' investigations to date against MNCs have focused on price fixing agreements, Resale Price Maintenance (RPM), and abuse of dominance;

Cartels: Companies subject to cartel investigations include major Japanese auto parts and bearing producers such as Sumitomo Electric Industries Ltd. and Mitsubishi Electric Corporation,[5] and major suppliers of liquid crystal displays (LCD) from Korea and Taiwan including Samsung Electronics and LG Display.

RPM: Automobile companies such as FAW-Volkswagen, Chrysler, and Daimler, and infant formula producers such as Danone (Dumex), Mead Johnson and Abbott have been investigated by the NDRC.

Abuse of dominance: Companies such as Qualcomm, IDC and Tetra Pak have been investigated this year.

2 Above these three agencies is a higher authority, the Anti-Monopoly Commission of the State Council. The Commission's role is mainly competition policy making and high level coordination, rather than daily regulatory work or specific enforcement activities.

3 MOFCOM is the agency responsible for merger review.

4 According to press reports, the NDRC has an enforcement team of about 20 people. It is said that the SAIC has a smaller team, but no verified number is available. Although there is no clear data regarding the size of enforcement teams, it is evident that relevant authorities are short of manpower considering the size of China, and this is particularly obvious when compared with their counterparts in other major jurisdictions.

5 Other Japanese producers at the centre of the auto parts and bearings cartel investigations include; Hitachi Automotive Systems Ltd., Nachi-Fujikoshi Corp., Denso Corporation Nsk Ltd., Yazaki Corporation, NTN Corporation, TEKT Corporation, Mitsuba Corporation, Furukawa Electric Co., Ltd and Asian Industry Co., Ltd.

The stepping-up of antitrust enforcement by the Chinese authorities this year was not only evidenced by the increasing number of investigations but also by the enforcement approach and unprecedented fines levied by the authorities. For example, while it was relatively rare for companies to be dawn raided in the past, the Chinese authorities recently raided companies like Daimler and Microsoft. Similarly the level of fines has increased over the past number of years. During the early years of the AML, the fines were relatively modest in most cases (less than US $200,000). Recently, we have seen fines of over US $200 million imposed in the auto parts and bearings cartel cases. With the Chinese antitrust authorities gaining expertise and confidence in initiating and conducting investigations, it looks like this trend is set to continue.

DISCRIMINATION AGAINST FOREIGN COMPANIES?

The increased enforcement by the Chinese authorities has provoked criticism from some commentators claiming the recent investigations are politically motivated and are being used as a way to protect Chinese domestic companies at the expense of foreign competitors. AmCham China, the US business trade group in China, recently referred to foreign companies as being "singled out" in the Chinese investigations.[6] But there may be more to the story than the Chinese authorities simply singling out foreign MNCs. When one considers the industries in question, the previous antitrust investigations which some of those companies have faced in other jurisdictions, as well as the fact that many domestic firms have been investigated and fined by the authorities, the Chinese investigations may not seem so strange or one-sided. We will discuss each of those points in turn.

"SELECTIVE" IN THE INDUSTRIES INVESTIGATED

Being young antitrust agencies, the Chinese antitrust authorities have seemed to focus on industries which have major impacts on everyday lives of consumers so as to increase their profile as serious enforcers to consumers. This explains why we are seeing an increasing number of investigations involving products such as auto vehicles, infant formula, optical lens and gold jewelry. Unfortunately, in some of these sectors (such as auto vehicles and infant formula) many of the big players are foreign companies.

TARGET COMPANIES

The Chinese antitrust authorities have attracted criticism for being selective in the companies they investigate since many of the investigations concern MNCs. However, data from the NDRC's official website shows that only 10 percent of enforcement actions by the NDRC involves foreign companies and the number for SAIC is only 5 percent.[7] The impression that Chinese authorities are selectively pursuing MNCs may come from the fine levels imposed on these companies, which are themselves the focus of headlines. Given that the MNCs are global companies, these factors make the investigations involving MNCs more high-profile which catches a lot of attention from home and abroad. For example, in the Infant Formula case there were a total number of nine

6 See http://www.amchamchina.org/article/13239

7 See http://www.saic.gov.cn/gsld/llyj/xxb/201410/t20141015_149027.html. The number of enforcement actions taken by the NDRC which involved foreign companies was 33 out of a total 335 cases, and the number for the SAIC was only 2 out of 39 cases.

domestic and foreign infant formula companies investigated for alleged RPM and altogether fined approximately RMB 668 million (US $109 million). Biostime, a domestic infant formula producer was levied with the highest percentage fine amounting to RMB 163 million (US $26.54 million), 6 percent of its previous year's turnover;[8] while Wyeth and Meiji, two foreign producers, received full immunity for cooperation with the NDRC. Nevertheless the press seemed to focus only on the investigation of foreign producers; the fact that a domestic company attracted the highest percentage fine got little media attention.[9]

Therefore, while the investigations into foreign companies have grabbed the headlines, it should be noted that the Chinese authorities have been actively pursuing domestic companies in recent years. For example, the SAIC in one of its first few cases in 2011, investigated and fined domestic concrete companies and an industry association in Lianyungang, a city in the coastal Jiangsu Province.[10] Similarly, the NDRC fined a number of rice noodle producers in Nanning and Liuzhou (southern China's Guangxi Autonomous Region) for a price fixing cartel in March 2010.[11] Even state-owned companies have not escaped antitrust scrutiny in China; China Telecom and China Unicom were previously subject to antitrust probes for alleged abuse of dominance in the broadband access and inter-network settlement sector.[12]

During the same period (from the beginning of 2013 to now) when the NDRC seemed to increase its enforcement efforts against MNCs, there has also been quite a number of investigations against domestic Chinese firms by the Chinese authorities. In February 2013, state-owned distillers Kweichou Moutai and Wuliangye Yibin were fined 449 million RMB (US $72.5 million) for alleged RPM practices; in September 2014 the NDRC published 23 administrative penalty decisions made against the Insurance Association of Zhejiang Province (a trade association) and 22 insurance companies doing business in the same province, for a total of more than 110 million RMB (US$18 million).

In addition, it appears that most of the recent investigations have been initiated on the basis of whistleblowing rather than by the authorities' targeting specific companies. According to press reports, the Qualcomm and IDC investigations were both triggered by whistleblowers.[13] Therefore, both domestic and foreign companies face anti-trust risk equally since any company may be reported by a whistleblower.

WHY A SUDDEN PEAK OF ENFORCEMENT AGAINST FOREIGN COMPANIES?

During the earlier years of the implementation of the AML, enforcement focused mainly on domestic companies. Prior to 2013, foreign companies' names rarely appeared on the Chinese antitrust authorities' lists

8 Under the AML, the Chinese antitrust agencies may impose a fine up to 10 percent of the undertaking's previous year's turnover. Mead Johnson received the largest fine of RMB 203.76 million (USD 33.19 million), although the percentage of Mead Johnson's fine was 4 percent of its previous year's turnover.

9 See http://shipin.people.com.cn/n/2013/0808/c85914-22485692.html.

10 See http://finance.ifeng.com/roll/20110303/3553748.shtml

11 See http://www.chinanews.com/cj/cj-gncj/news/2010/03-30/2198963.shtml

12 The investigation was initiated in 2011. In February 2014, the NDRC claimed that it is still reviewing applications from both companies for a termination of the investigation based on commitments.

13 See the press report from Sina.com: http://finance.sina.com.cn/chanjing/gsnews/20140220/032018272422.shtml.

of reported investigations. However, for each type of anticompetitive conduct for which MNCs were recently investigated, the authorities first started with investigations into domestic companies. For example, the authorities had investigated numerous local cartels in various foodstuffs sectors before the NDRC initiated the first international cartel investigation - the LCD panels case in 2013. This indicates the Chinese authorities initially took a relatively cautious approach in terms of taking enforcement actions against MNCs. Why are we now seeing a sudden peak of enforcement against foreign companies? Rather than simply explaining this phenomenon as the selective and discriminatory enforcement against MNCs, an alternative explanation-at least plausible explanation-is that after a few years accumulating enforcement experience from investigations of small and local domestic companies, and internal training of their staff, the authorities are now becoming more confident in launching investigations against MNCs. If this is the case, it would be a big mistake for foreign companies to assume the lack of enforcement against them in the early years would stay forever. MNCs will have to adapt themselves to such a change in the enforcement climate in China.

SIMILAR ANTITRUST INVESTIGATIONS IN OTHER JURISDICTIONS

Large MNCs being the targets of antitrust investigations is not unique to China. These companies are often targets of competition authorities around the world. One of the purposes of antitrust law is to prohibit collusion or abuse of market power and maintain dynamic market competition; therefore, authorities are likely to pay more attention to the behaviour of companies with strong market positions.

Some of the recent investigations launched by Chinese authorities echo those in other jurisdictions. For example, some of the LCD panel producers fined by Chinese authorities had been previously fined by the EU in 2010, e.g., Samsung Electronics, LG Display and AU Optronics, amongst others. Also, Japanese auto parts and bearings producers which were fined by Chinese authorities this year, JTEKT, NSK and NTN, were fined by EU in March 2014 for their participation in the same international cartel. Qualcomm was previously investigated in other major jurisdictions, including Japan, South Korea and the EU for abuse of dominance and it was recently reported that the FTC, the US antitrust enforcement agency, has opened an investigation into Qualcomm.[14]

Taking these factors into account, the recent investigations may not seem so strange. China is not alone in conducting investigations in these sectors or investigating large MNCs for possible anticompetitive behaviour. Given the global nature of many cartels, it is not surprising the Chinese authorities have focused on the same MNCs which other jurisdictions have also investigated for their involvement in international cartels.

However, while the enforcement activity has increased over the past year, the Chinese authorities still have improvements to make in terms of transparency and due process in investigations and providing greater clarity on how certain types of behaviour are viewed by the authorities in China. Some of the issues in connection with transparency and due process may reinforce the perception of discriminatory enforcement against MNCs.

14 See https://sg.finance.yahoo.com/news/us-stocks-flat-qualcomm-sinks-153243892.html

ROOM FOR IMPROVEMENT

MORE FOCUS ON TRANSPARENCY AND DUE PROCESS IN INVESTIGATIONS

Under AML and relevant regulations, Chinese antitrust authorities are not obliged to publish every decision they make, which means disclosure is discretionary, rather than an obligation required by law.[15] Recently the NDRC has started to publish full texts of some of its decisions which is a welcome move.[16] While these developments are likely in response to criticisms on the lack of transparency of its actions, more is needed. For example, the decisions that have been published are very brief and lack the detailed antitrust analysis when compared with the decisions of the European Commission.

More focus on transparency and due process by the Chinese authorities is needed throughout the investigation process, for example, there are no 'state of play' meetings between the parties under investigation and the parties have no access to the authorities' case files at any stage of the investigation. This is quite different to the procedures in other jurisdictions where due process is adhered to in antitrust investigations. For example, in EU cartel investigations, the European Commission will issue a statement of objections to the parties which outlines the objections raised against them. At this stage the companies can examine the documents on the Commission's investigation file, reply in writing and request an oral hearing to present their comments on the case before representatives of the Commission.

Another area for improvement is to ensure companies being investigated (both foreign and domestic companies) can have adequate legal representation to protect their legitimate rights throughout the investigation. Recently, there had been so much speculation and concern about companies' outside counsels being excluded from defending them in investigations that a senior NDRC official had to clarify at an international conference organized by the ABA in China that the agencies would "welcome all companies efforts to defend themselves" in their investigations.[17] Interestingly, in the recent SAIC investigation of Microsoft, the SAIC made it clear in its public announcement that Microsoft's PRC counsels "witnessed the whole process of the dawn raid"[18] This suggests the authorities have been making conscious efforts to ensure a company's right to legal representation is respected. Nevertheless, unlike in western countries, legal representation in Chinese government investigation proceedings is still a relatively new concept. In practice, some officials may be under the wrong impression that the involvement of outside counsels means companies are choosing to be uncooperative and confrontational. Therefore, they may be hostile to outside counsels assisting their clients in an investigation. It will take time to get such officials to appreciate the role of outside counsels and change their misperceptions.

15 See Article 44 of AML, Article 12 of the NDRC Procedural Provisions and Article 25 of AIC Procedural Provisions.

16 From July 2013 to October 2014, the SAIC disclosed 18 penalty decisions in total on its official website: http://www.saic.gov.cn/zwgk/gggs/jzzf/
The NDRC disclosed 12 decisions relating to Japanese auto parts and bearing producers on 18 September 2014 and 23 decisions on domestic insurance companies on 2 September and 3 September 2014. http://jjs.ndrc.gov.cn/fjgld/index_1.html

17 PaRR report, "China's NDRC 'welcomes' companies to defend themselves in investigations" - ABA Antitrust in Asia, 26 May 2014.

18 See SAIC's public announcement at: http://www.saic.gov.cn/ywdt/gsyw/zjyw/xxb/201407/t20140729_147122.html.

MORE GUIDANCE ON PROVISIONS OF THE AML

Some legal rules need to be elaborated on, such as those with regard to the leniency policy. Although both the SAIC and the NDRC provide several provisions regarding exemption and reduction of the penalties, these provisions are still very general. It is not explicitly stated how companies can put down a marker, how much and what kind of evidence would help to get leniency, and the likelihood of getting leniency once the threshold for leniency is met. The implementation of the leniency mechanism largely depends on the discretion of enforcement authorities.

Greater clarity on how the authorities view certain agreements or behaviour would also be useful. RPM is subject to the rule of reason analysis in the US which requires balancing the benefit and harm of the relevant conduct, whilst it is presumably anti-competitive under TFEU Article 101(1) in EU. In China, although Article 15 of AML provides some justifications for RPM which is otherwise prohibited under Article 14 of AML, it had not been clear until recently what position the Chinese agencies would be taking in terms of enforcement against RPM.[19] Without familiarity with practices in China, investigated companies might unreasonably count on economic analysis for mitigated punishment or even exemption.

TIME FRAME FOR INVESTIGATIONS

Unlike antitrust investigations in other jurisdictions, the time frame for investigations in China is very short. This is largely to do with the constrained resources of the authorities who prefer to wrap up investigations quickly. For example, the investigation into the Japanese auto parts cartel lasted less than a year in China, whereas it lasted over a year in the US and more than two years in the EU. Similarly the investigation into Qualcomm which was announced in early 2014 is expected to be completed soon,[20] whereas the investigation into Qualcomm in the EU and Japan took more than two years. With such short time periods for investigations, the companies, their relevant employees and outside counsels are all under huge pressure which might restrict their abilities to effectively respond to inquiries by the authorities. Such quick time frames also raise due process concerns given that antitrust investigations are usually complex involving review of voluminous documentation and detailed market investigations.

These factors combined could explain in part why MNCs have felt they have been discriminated against by the Chinese authorities. During antitrust investigations in other jurisdictions, such as the EU or US, the MNCs would have had a different experience in terms of due process, transparency and treatment of their legal representation. Foreign companies and their advisors should understand that the rules and procedures in China are different from those in other parts of the world and the Chinese authorities apply these rules, however strange they may seem from a western point of view, to domestic and foreign companies alike.

19 Recently the NDRC took a series of enforcement actions against RPM, making it clear that in practice RPM almost always amounts to per se violation which can rarely be justified.

20 See http://tech.sina.com.cn/t/2014-11-14/doc-icczmvum9860121.shtml

IMPROVED ENFORCEMENT ACTIONS

While there is room for improvement, much progress has been made in legislation and procedures. More legal rules have been promulgated and draft rules published, especially in respect of procedural rules, e.g., the Several Provisions on Regulating the Price-Related Administrative Penalty Power promulgated by the NDRC. Furthermore, the enforcement teams of the relevant authorities are expanding steadily. More qualified staff are being hired by the NDRC and its local counterparts. Increasing resources again indicates that in the future enforcement actions will not diminish.

Despite shortcomings in relation to due process during the investigation, the Chinese antitrust agencies have recently shown a willingness to re-consider a decision and reduce a fine on hearing valid arguments from the parties. In August the NDRC sent a penalty decision of RMB 342.72 million (US $55 million) to Sumitomo Electric Industries Ltd., one of 12 Japanese car parts makers found to have engaged in price fixing under Chinese antitrust law. Subsequently, Sumitomo argued that the calculation of the fine should have been based on its stake in its China joint venture rather than the total sales of the joint venture for the previous year. The NDRC accepted Sumitomo's argument and reduced the fine by RMB 53.32 million (US $8.5 million).[21]

The agencies have also made use of the commitments provision in the AML under which an investigation will be suspended if the company makes commitments to take specific measures to eliminate the effects of its conducts within a certain time frame. If the company fulfills its commitments, the agency may terminate the investigation, otherwise it may decide to restart the investigation.[22] Recently the NDRC investigation of IDC was closed using this procedure.

CONCLUSION

The Chinese antirust agencies have made great strides over the past number of years. The agencies are still learning and are benefiting greatly from increased cooperation with other antirust agencies around the world. Chinese authorities now frequently interact with competition authorities in other jurisdictions. The NDRC and the SAIC have both signed memoranda of understanding with the DOJ and FTC in the United States, as well as the Fair Trade Commission of South Korea, and they often hold seminars with their U.S. and EU counterparts. International best practices on transparency in investigations should be an area where the Chinese antitrust authorities can learn from their peers. The Chinese antitrust agencies have recently started to publish some decisions, which is a good start.

However, foreign companies and their advisors should understand that the rules and procedures in China are different from those in other parts of the world. This not only relates to different interpretations of certain types of behaviour, for example RPM, but also to the way investigations are carried out. By improving transparen-

21 China News, "China's NDRC cuts antitrust fine after Sumitomo fights its corner", 21 August 2014.

22 See Article 45 of Anti-Monopoly Law, Articles 16, 17 and 18 of the NDRC Procedural Provisions and Articles 17, 18 and 19 of AIC Procedural Provisions.

cy in the investigations, companies will be better informed on how to comply with the AML. Greater transparency on the investigation process will also give investigated companies reassurance that they are being treated fairly.

In the early years of enforcing the AML, the NDRC and the SAIC focused their attention on domestic companies. Now, as the agencies gain confidence and learn from other jurisdictions, they are also tackling large MNCs doing business in China. Even though the recent enforcement activity against foreign companies has been much publicised, investigations into foreign companies still only accounts for a small percentage of the agencies' overall enforcement actions. The increased enforcement by the Chinese antitrust agencies against both foreign and domestic companies looks set to continue. As Professor Huang Yong, a leading Chinese antitrust academic and the deputy chairman of the advisory board to the Anti-monopoly Commission pointed out, "antitrust enforcement by Chinese authorities will become the new norm".[23] Foreign businesses will have to adjust themselves to the change of the regulatory environment in China and focus more on antitrust compliance to mitigate their exposure.

23 See http://www.ce.cn/xwzx/gnsz/gdxw/201409/24/t20140924_3586600.shtml.

Minority Participations and Merger Control Filing Requirements in East Asia

Maxime Vanhollebeke

Shan Hu

In July 2014, the European Commission published a White Paper with several proposals for changing the EU Merger Regulation.[1] Amongst those, the Commission is proposing to extend the scope of the EU merger control regime to also cover certain non-controlling minority participations. This proposal has led to criticism that the EU merger control regime could be overreaching. In this article we briefly contrast the current EU merger control regime applicable to minority investments with the rules applicable in a selection of East Asian jurisdictions. As will become apparent, non-controlling minority participations may already today be caught by merger control requirements in Asia.

THE NOTION OF CONCENTRATION: TWO CAMPS

With the notable exception of Hong Kong[2] and Malaysia, competition law jurisdictions across East Asia have adopted a merger control regime as part of their competition law framework.[3] Some jurisdictions like South Korea, Taiwan and Japan have had a merger control regime in place for many years. In other places (such as China, Indonesia, Vietnam or Singapore) the regime was introduced more recently.

Except for Singapore, most East Asian jurisdictions have opted for a mandatory merger control regime: a notification will be required (i) where a transaction qualifies as a "concentration"[4] and (ii) the transaction parties

1 European Commission White Paper "*Towards more effective EU merger control*" dated 9 July 2014. More recently, in October 2014 the European Commission published a competition policy brief on the acquisition of minority shareholdings (Minority Power – EU Merger Control and the acquisition of Minority Shareholdings).

2 Hong Kong's Competition Ordinance (Cap 619) only contains merger control provisions for concentrations in the telecommunications sector.

3 Thailand has a merger control regime but implementing regulations have yet to be adopted. In the Philippines, the Corporation Code requires mergers and consolidations of corporations to be approved by the Securities and Exchange Commission (SEC). The Department of Justice for Competition recently signed an MOU with the SEC which provides for a consultation process with respect to the competition law aspects of proposed mergers and consolidations.

4 The notion of "concentration" is a generic term used to refer to those transactions which may be subject to merger filing requirements. Please note that in some jurisdictions, "concentrations" are referred to as "business combinations" or "mergers".

meet relevant notification thresholds (usually expressed by reference to both domestic and worldwide turnover, market share or asset thresholds).

The notion of "concentration" varies from one jurisdiction to another. Broadly speaking it is possible to distinguish two camps. The first camp regroups countries such as China, Indonesia and Singapore, which rely on a "change of control" test to identify those transactions falling within the scope of their merger control regime. Non-controlling minority acquisitions will not be caught but, as we will see, the notion of control also varies from one jurisdiction to the next. The second camp regroups countries such as Japan, South Korea and Taiwan, which mostly rely on formalistic criteria to identify relevant concentrations. Minority share acquisitions exceeding certain equity thresholds will be caught irrespective of whether control is acquired.

JURISDICTIONS RELYING ON A CONTROL TEST

A number of emerging competition law jurisdictions have (sometimes) heavily borrowed from the EU model when establishing their domestic competition law regime. In East Asia, this is clearly the case for Singapore, as well as (albeit to a lesser extent) China and Indonesia. The merger control regime in these three jurisdictions uses concepts that are familiar in Europe. In particular, all three jurisdictions rely on a "change of control test" to identify relevant concentrations.[5]

Under the EU regime, the notion of control is broadly defined and refers to the possibility of exercising decisive influence on an undertaking. Such decisive influence can exist on the basis of rights, contracts or any other means. Control may be acquired on a legal or ***de facto*** basis and it may take the form of sole or joint control. A minority participation will usually be insufficient to confer control unless particular rights attach to it, allowing the minority shareholder to determine the strategic commercial conduct of the business (positive control) or to veto those decisions (such as the budget, the business plans, major investments or the appointment of senior personnel) which are essential for the strategic conduct of the business (negative control). In some instances, a minority shareholder can also enjoy control on a ***de facto*** basis, for instance where it is highly likely to achieve a majority of the votes cast at the shareholder meetings, given the dispersed nature of the remaining shares and the other shareholders' poor attendance in the past. Such ***de facto*** control scenarios are however relatively rare, and in most cases, minority investments with no particular rights attached (other than standard minority protection rights) will not give rise to a merger filing requirement. This could change in the future, as one of the proposals put forward by the European Commission is to expand the concept of "concentration" to also capture minority acquisitions which fall short of conferring control whilst still giving the minority investor a certain degree of influence over the business.

Whilst the notion of control in the East Asian jurisdictions is largely inspired by the EU concept, in some places the boundaries of this notion are not yet crystalized in detailed enforcement guidelines, and in practice the concept of control could possibly be broader than in the EU - as will be explained below.

5 The notion of control is also relevant under the Vietnamese merger control regime; see Article 17.3 of the Vietnamese Competition Act.

SINGAPORE

The notion of control under Singapore's merger control regime is aligned with the EU regime. According to Section 54(3) of the Competition Act, "control, in relation to an undertaking, shall be regarded as existing if, by reason of rights, contracts or any other means, or any combination of rights, contracts or other means, decisive influence is capable of being exercised with regard to the activities of the undertaking." The Competition Commission of Singapore (CCS) has issued detailed guidance on the notion of control, which heavily borrows from the EU guidance. Interestingly, the guidelines provide for a rebuttable presumption of control in the case of ownership of between 30 and 50 percent of the voting rights in an undertaking.[6] This presumption, which is absent from the EU regime, could have suggested a more stringent approach towards minority participations. In practice, however, the Singapore approach is aligned with the EU regime, except that because of the voluntary nature of the regime, very few minority acquisitions are notified to the CCS.[7]

INDONESIA

Indonesia also relies on a control test to identify those transactions which might need to be notified if the relevant thresholds are met. The Indonesian merger control regime captures mergers, consolidations and share acquisitions. Pursuant to Government Regulation 57 of 2010 (the "Regulation"), only those share acquisitions resulting in a change of control of the target are caught. The explanatory notes to the Regulation provide further clarifications on the notion of control in the context of identifying those group entities whose turnover and assets figures must be included to assess whether the notification thresholds are met. The notion of control is being defined as "the ability to influence or determine the management policies or the business and or to influence and determine management of the business". Unfortunately the merger control guidelines[8] issued by the Commission for the Supervision of Business Competition (KPPU) do not elaborate further on the concept and the merger control decisions published to date do not shed further light on the precise boundaries of this notion. Based on the KPPU enforcement practice to date, it would appear that the notion of control is broadly aligned with the EU concept.

CHINA

The notion of control is also at the heart of the Chinese merger control regime. According to Article 20 of the Antimonopoly Law, concentrations include (i) mergers, (ii) acquisitions of control by means of asset or equity purchase (iii) as well as acquisitions of control or decisive influence through contract or any other means.

6 See section 3.10 of the *CCS Guidelines on the substantive assessment of mergers*.

7 Since the entry into force of the Singapore Competition Act in 2008, there have been no reported notifications of minority participations and only a couple of notifications concerning the establishment of joint ventures. The public version of the clearance decisions relating to these joint venture transactions does not specify whether the relevant transaction involved minority participations.

8 See Commission Regulation No 2 of 2013 on the Third Amendment of the Commission Regulation No 13 of 2010 on the *Guidelines for Mergers or Consolidations of Business Entities and Acquisition of Shares of Other Companies*.

Up until recently, no formal guidance was available on what the notion of control or decisive influence might entail. In an early draft of China's Ministry of Commerce (MOFCOM)'s 2009 *Measures on the Notification of Proposed Concentrations*,[9] control was defined as the ability to make decisions regarding important management and operational issues such as the appointment of board members or key personnel, financial budgets, operation and sales, pricing, material investments, etc. Whilst such decisive influence could be achieved even absent 50 percent of the voting rights, there was an express recognition in the draft that standard minority protection rights would be insufficient to confer control. However this draft guidance was not retained in the final version of the 2009 Measures.

In June 2014, MOFCOM for the first time offered formal clarifications on the point. The guidance is set out in Article 3 of an updated version of MOFCOM's *Guiding Opinion on the Notification of Concentrations of Undertakings* (the "Guiding Opinion").[10] The Guiding Opinion expressly recognizes the concept of sole control, joint control and *de facto* control and lists a number of factors which are relevant for the control analysis. These factors include the shareholding structure and board composition of the target, voting rules at board and shareholder level, the appointment of senior personnel, structural links between shareholders and directors, the existence of substantial commercial relationships between parties, ***etc***. These factors echo those which are also considered in the EU to establish control. However, the guidance in China stops short of describing the particular circumstances in which a finding of control will be likely. In particular, unlike in earlier drafts, no guidance is provided on the treatment of minority acquisitions.

Based on MOFCOM's enforcement practice to date, minority acquisitions which would qualify as concentrations in the EU are also likely to qualify as such in China. However the Chinese regime could possibly capture a broader range of transactions. Unfortunately there are no published precedents which may be relied on or shed more light on the notification requirements of minority investments. Unlike in the EU, the unconditional merger control clearance decisions are not published and the public announcements relating to prohibition or conditional approval decisions do not provide much further guidance on the notion of control under Article 20 of the Antimonopoly Law.

The *Alpha V/Savio* conditional approval decision[11] however hints at a possible broad notion of control. In that case, MOFCOM conditioned its approval of the acquisition by Alpha Private Equity Fund V of Savio Macchine Tessili to the divestiture by Alpha V of its 27.9% interest in a Swiss competitor of Savio, Uster Technologies. Alpha V was Uster's largest shareholder and MOFCOM closely reviewed the voting patterns at shareholders' meetings, minutes of those shareholders meetings, and the composition and voting pattern of Uster's board of directors, before concluding that it could not rule out the possibility that Alpha V would influence Uster's operations and that the transaction could enable Alpha V to coordinate the operations of Savio and Uster. Whilst MOFCOM's analysis was part of the substantive assessment of the transaction (not unlike that which the European Commission would review in relation to "significant links" with competitors), it suggests a broad notion of control which could be of relevance not only at the substantive review stage but also at the jurisdictional assessment stage.

9 Draft *Provisional Measures on the Notification of Concentrations of Business Operators*, 13 March 2009.

10 MOFCOM *Guiding Opinion on the Notification of Concentrations of Undertakings* dated 6 June 2014.

11 Public Announcement No. 73 2011 of MOFCOM dated 21 October 2011.

Given the broad enforcement discretion of MOFCOM, where a transaction involves a minority investor which will be actively involved in the management or operation of the business - either on a ***de facto*** basis or through special rights extending beyond the usual minority protection rights - the parties are well advised to proactively engage with MOFCOM to inform their filing strategy.

JURISDICTIONS RELYING ON EQUITY THRESHOLDS

Other jurisdictions (including Japan, Korea and Taiwan) have opted for a more formalistic approach to identify relevant "concentrations". In those jurisdictions, minority share acquisitions exceeding certain equity thresholds qualify as "concentrations" irrespective of whether control is acquired:

In Japan,[12] share acquisitions resulting in the ownership of more than 20 percent of the voting shares in a target company will qualify as a concentration if the minority acquirer becomes the largest shareholder.

In South Korea,[13] share acquisitions resulting in the ownership of 20 percent or more of the voting shares in the target (15 percent in case the target is a KOSDAQ-listed company) will qualify as a concentration.

In Taiwan,[14] share acquisitions resulting in the ownership of more than one third of the voting shares or capital in the target will qualify as a concentration.

Such quantitative thresholds are easy to apply and promote legal certainty, but in practice they capture a broader range of transactions than in jurisdictions relying on a change of control test. Such formalistic approach can in part be explained by a different legal tradition, favoring a rules-based approach as opposed to a principles-based approach. Also, Japan, Taiwan and South Korea are established competition law jurisdictions whose rules are less influenced by the EU model centered around the "change of control" test.

While quantitative thresholds are used as a first filter to identify relevant "concentrations," even in those jurisdictions, the concept of control may nevertheless play a role in the jurisdictional merger control assessment.

First, the notion of control is sometimes used to identify the boundaries of the corporate group whose activity level must be considered to determine whether the relevant notification thresholds are met. In South Korea for instance, a corporate group includes all companies controlled by the same person and control is referred to amongst others as "the ability to exercise considerable influence"[15] – a notion which broadly corresponds to the EU notion of control except that it does not seem to capture negative control situations.

12 See *Japan Fair Trade Commission (JFTC) Guidelines from the application of the Monopoly Act concerning the review of Business Combinations,* dated 14 June 2011.

13 See Article 12 of the *Korea Fair Trade Act.*

14 See Article 6 of the *Taiwan Fair Trade Act.*

15 See Article 3 of the *Enforcement Decree of The Monopoly Regulation and Fair Trade Act.*

Second, the equity thresholds are often not the only criteria to establish merger control jurisdiction. In Taiwan, for instance, minority participations below 33 percent may still trigger a mandatory merger filing requirement in "joint control" situations. Indeed, the notion of concentration also covers transactions whereby "an enterprise directly or indirectly controls the business operation of another enterprise." Whilst the notion of control seems to be more limited than in the EU (in particular it does not seem to capture negative control situations),[16] this alternative test could capture certain minority share acquisitions below 33 percent in situations where the minority shareholder benefits from particular rights allowing it to exercise positive control over the business. In Japan, whilst minority participations below 20 percent usually do not give rise to a merger notification requirement, the JFTC guidance makes clear that minority participations below that threshold could still trigger a filing requirement in cases "where a joint relationship is formed, maintained or strengthened."[17] The relevant factors for assessing such joint relationship include a review of the shareholding structure, the existence of interlocking directorates as well as any other commercial, financial and business relationships or agreements between parties. These criteria appear to be broader than the EU concept of control and may capture minority participations which would likely not qualify as "concentrations" in the EU.

Third, even in South Korea, where the notion of control is not used to identify those transactions subject to a mandatory merger filing requirement, the control analysis still plays a role at the preliminary review stage. Indeed, transactions which are being notified because relevant equity thresholds are met but which do not involve a change of control will be cleared under a simplified review procedure without proceeding to a detailed substantive competitive assessment of the transaction.[18]

CONCLUSION

From this brief overview, it appears that non-controlling minority participations may already today trigger merger control filing requirements in East Asia. This has mainly been the case in jurisdictions such as Japan, Korea and Taiwan relying on equity thresholds to identify relevant concentrations. In jurisdictions relying on a change of control test (such as China, Singapore and Indonesia) non-controlling minority participations are in principle not caught, but in some jurisdictions (including China and Indonesia), the notion of control is not yet crystalized and could possibly be broader than in the EU. Any possible expansion of the EU merger control regime to capture non-controlling minority participations could provide these authorities with further comfort to adopt an expansive reading of their jurisdiction to review minority acquisitions which today escape merger control review in the EU.

16 One possible exception would be a scenario where the veto rights would be so extensive to cover not only the key commercial and strategic commercial decisions but also daily business operation and the appointment of personnel.

17 See Section 1.1. B of the 2011 JFTC *Guidelines on the application of the Antimonopoly Act concerning the review of business combinations* dated 14 June 2011.

18 See Korea Fair Trade Commission (KFTC) *Guidelines for the Combinations of Enterprises Review* dated 28 December 2011.

Implications of International Experience for Evaluating Unfair Pricing under China's Anti-Monopoly Law

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ABSTRACT

This article develops an economic framework for applying the unfair pricing provisions of China's Anti-Monopoly Law. It shows that virtually all jurisdictions around the world with such provisions have decided to consider unfair pricing claims only in exceptional circumstances, and rarely, if ever, in innovation-intensive industries. For those cases that pass this screen and receive consideration, the courts and competition authorities then, under the leading test, insist on substantial evidence that the price is significantly higher than cost and is unfair given the value provided to the buyer. The exceptional circumstances screen and the rigorous unfair pricing test are motivated by the recognition, supported by substantial empirical evidence, that successful firms must have the assurance of receiving significant rewards to induce them to invest time and capital in highly risky innovation that is the source of economic growth and welfare. The approach followed on unfair pricing by jurisdictions around the world is consistent with modern Chinese economic policy.

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SSRN: http://ssrn.com/abstract=2403159. Hereinafter Evans, Zhang and Zhang (2014).

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China's Anti-Monopoly Law contains an unfair pricing provision, Article 17(1), which has so far not been the subject of many enforcement actions or judicial decisions.[1] In the first decision to consider this part of the AML, the Shenzhen Intermediate Court in *Huawei vs. InterDigital* found that InterDigital charged Huawei unfair and discriminatory prices.[2] The NDRC—the competition authority responsible for enforcing this part of the AML—has adopted regulations on applying the unfair pricing law but has not issued any decisions.[3]

The experience of other countries and jurisdictions with unfair pricing laws provides a useful reference for Chinese courts and the NDRC in refining their analytical framework for implementing the unfair pricing law. This article summarizes how the courts and competition authorities in other countries have approached unfair pricing, explains the economic rationales behind their approach, and describes the economic issues that arise in assessing unfair pricing. It then discusses aspects of China's policies toward price regulation and the implications of these policies for how China may wish to adapt the experience of other jurisdictions.

We pay particular attention to the relationship between unfair pricing and innovation. Competition authorities and courts have taken an extremely cautious approach in their application of unfair pricing provisions precisely because of their concerns that imposing price caps would chill innovation and slow economic progress. They almost never use unfair pricing to restrict the returns on intellectual property rights.

I. INTERNATIONAL CONSENSUS ON UNFAIR PRICING

There are two schools of thought on unfair pricing.

One school says that antitrust should never limit how much any firm, including a monopolist, charges. The United States, Canada, and Australia belong to this school. The U.S. Department of Justice summarized the view: "This central tenet of U.S. antitrust law is well supported by court decisions that have held, for example, that '[a] pristine monopolist…may charge as high a rate as the market will bear' and that '[a] natural monopolist that acquired and maintained its monopoly without excluding competitors by improper means is not guilty of 'monopolizing' in violation of the Sherman Act…and can therefore charge any price that it wants….'"[4]

1 See Article 17 (1) of the Anti-Monopoly Law of the People's Republic of China, [2008] Presidential Order No. 68, August 30, 2007. The Chinese version is available at http://www.gov.cn/flfg/2007-08/30/content_732591.htm; an unofficial translation of the AML is available at http://www.americanbar.org/content/dam/aba/publishing/antitrust_source/Oct07_Bush10_18f.authcheckdam.pdf.

2 See Ye Ruosi, Zhu Jianjun & Chen Wenquan, "Determination of Whether Abuse of Dominance by SEP Owners Constitutes Monopoly: Comments on the Antitrust Lawsuit *Huawei v. InterDigital*," Electronics Intellectual Property, vol.3, 2013; see also Ye Ruosi, Zhu Jianjun & Chen Wenquan, "The Implementation of FRAND in the Litigations Involving SEP's Royalty Rates: Comments on SEP Royalty Lawsuit *Huawei v. InterDigital*," Electronics Intellectual Property, vol.4, 2013. The Guangdong High People's Court affirmed the decisions of the Shenzhen Intermediate Court. See Zhu Jianjun, "Determination of Whether Abuse of Dominance by SEP Owners Constitutes Monopoly: Comments on the Antitrust Infringement Case *Huawei v. InterDigital,*" China Intellectual Property News, December 5, 2013, available at http://www.cipnews.com.cn/showArticle.asp?Articleid=29779.

3 Article 11 of the NDRC Anti-Price Monopoly Regulations, NDRC Order No. 7, December 29, 2010, available at http://www.gov.cn/flfg/2011-01/04/content_1777969.htm. The Guangdong Price Bureau with guidance from the NDRC did apply the regulations to one case; see NDRC, "Guangdong Punished Sea Sand Price Monopoly Case to Guarantee the Smooth Proceeding of National Important Project Construction", October 26, 2012 available at http://jjs.ndrc.gov.cn/gzdt/t20121026_510834.htm

4 U.S. Federal Trade Commission and Antitrust Division of the U.S. Department of Justice, "Excessive Prices," in OECD Policy Roundtables: Excessive Prices (2011), 299-308, available at: http://www.oecd.org/competition/abuse/49604207.pdf, at 299.

The other school says that there are *exceptional circumstances* in which antitrust should limit how much a dominant firm can charge. According to a recent survey conducted by the OECD, while a number of countries have excessive pricing laws, "In general, excessive price cases are conducted infrequently even within those jurisdictions that prohibit and enforce excessive price provisions."[5]

For example, in 1994 the European Commission stated that, "in its decision-making practice [the Commission] does not normally control or condemn the high level of prices as such".[6] European Union cases typically are limited to situations in which (a) a firm controls a whole industry, such as the post office or the fixed-line telecommunications network, as a result of a government grant or regulation, or (b) in which excessive pricing is related to exclusionary strategies by the firm designed to limit the ability of other firms to compete. Excessive pricing cases are rare animals as a result. The European Commission has reached only six formal decisions concerning excessive pricing between 1957 and 2013—barely one a decade.[7]

Both schools of thought rarely or never use antitrust laws to regulate prices because of a shared concern: limiting the rewards that successful firms earn will dampen the very risk-taking and innovation that drives economic progress. The European Commission recently said: "It is nonetheless important to recognise that high profits may often be the result of superior innovation and risk taking, which should not be penalised as this would work as a disincentive to innovate and invest……"[8] The U.S. Supreme Court concluded that, "The opportunity to charge monopoly prices—at least for a short period—is what attracts 'business acumen' in the first place; it induces risk taking that produces innovation and economic growth."[9] Both jurisdictions view innovation broadly as the dynamic competitive process that is constantly refreshing industries with new challengers.[10]

The international consensus is therefore simple: *bring excessive pricing cases rarely if ever.* That high bar is higher still in innovation-intensive industries, where the risk of chilling economic progress is the greatest. As a result, excessive pricing cases in innovation-intensive industries cases are usually brought, if at all, only when the excessive pricing is alleged to be part of an exclusionary strategy.

II. THE UNFAIR PRICING TEST

Occasionally, courts are asked to consider excessive pricing cases and have had to sort out what constitutes an abuse. The European Court of Justice is the source of the most influential test of excessive pricing. In ***United Brands***—the famous case involving bananas—the Court concluded:[11]

5 OECD Policy Roundtables: Excessive Prices (2011), available at: http://www.oecd.org/competition/abuse/49604207.pdf

6 XXIVth Annual Report on Competition Policy 1994.

7 Id., and Massimo Motta and Alexandre de Streel (2007), "Excessive Pricing in Competition Law: Never say Never," in Arvid Fredenberg and Niklas Strand (eds), The Pros and Cons of High Prices, at 30.

8 European Commission, "Article 102 and Excessive Prices," in OECD Policy Roundtables: Excessive Prices (2011), 309-322, available at: http://www.oecd.org/competition/abuse/49604207.pdf, at 311.

9 Verizon Communications Inc. v. Law Offices of Curtis V Trinko, 540 U.S. 398, 407 (2004)

10 In addition, competition authorities and courts around the world recognize that the process of identifying whether a price is excessive or unfair is fraught with practical and theoretical challenges that heighten the risk of error. These difficulties increase the possibility of inefficient intervention, which would reduce consumer welfare.

11 Case 27/76, United Brands Company and United Brands Continental BV v. Commission of the European Communities, 1978 E.C.R. 207.

The questions therefore to be determined are whether the difference between the costs actually incurred and the price actually charged is excessive, and, if the answer to this question is in the affirmative, whether a price has been imposed which is either unfair in itself or when compared to competing products.

This test sets two successive hurdles for a competition authority or complainant claiming that a dominant firm engages in excessive pricing. The first hurdle is whether the price charged by the dominant firm is much higher than its cost. If it is, then a second hurdle presents itself before the court will find an unfair pricing abuse. The competition authority or complainant must show that the price is "unfair". The European Commission and other courts have concluded that this second hurdle requires, among other things, showing that the price is high relative to the value of the product to the buyer. Neither of these hurdles is easy to surmount, in part because, as courts have pointed out, it is difficult to develop sound evidence on these points.[12]

These tests are rarely if ever applicable to innovation-intensive and intellectual-property rich industries, as we show in the next section. The price-cost test is not useful in these situations because it makes no economic sense for innovation-intensive industries generally and for intellectual property rights in particular. In those industries, marginal costs are typically very low compared to the value of the product, and profits are the reward earned by the successful few to induce the innovative efforts of the many. In assessing the second prong of the *United Brands* test—the value to the buyer—antitrust enforcers need to recognize that the prospect of earning the profits that accrue to those who succeed is what generates the efforts to innovate, and that without those incentives the buyer would not receive *any* of the benefits of the innovation.

III. INNOVATION AND REWARDS

As discussed, competition authorities and courts rarely if ever consider unfair pricing claims and when they do they set a high bar for finding a dominant firm guilty of an abuse. They do so largely out of a concern for chilling innovation. There is considerable empirical economic support for this policy.

There is substantial empirical evidence that economic progress and long-term social welfare is driven by innovation that leads to the creation of new products and services, new technologies that facilitate the introduction of new products and services, and the creation of more efficient ways to produce goods and services.[13] The point is most clearly seen and best documented with new products. A pioneering study found that a seemingly trivial "new" product—the Apple Cinnamon version of the traditional Cheerios cereal—generated almost $67 million of additional value to consumers a year.[14] It is obvious that important innovations such as e-commerce sites generate value for consumers. New technologies such as mobile communication methods and platforms such as tablet computer operating systems create very large increases in social wealth because they support and spawn many new products, each of which may generate considerable value.

12 Case COMP/A.36.750/D3, Scandlines Sverige AB v. Port of Helsingborg [2006] 4 CMLR 23; Case 27/76, United Brands Company and United Brands Continentaal BV v. Commission of the European Communities, 1978 E.C.R. 207; Attheraces Ltd. v. British Horseracing Board Ltd., [2007] EWCA (Civ) 38, [2007] UKCLR (CA) 309.

13 For a general discussion of the evidence on innovation and economic growth see Robert J. Barro and Xavier Sala-i-Martin (2004), Economic Growth (2nd ed.) at chapters 6-7.

14 Jerry A. Hausman, "Valuation of New Goods Under Perfect and Imperfect Competition," in The Economics of New Goods, ed. Timothy F. Bresnahan and Robert J. Gordon (Chicago: University of Chicago Press, 1996).

This value creation results from dynamic competition in which most entrepreneurs, inventors and firms that try their hands at innovation fail. In fact, most new firms fail. Half of all new US firms, weighted by number of employees, fail in less than five years.[15] The same is true for other countries.[16] A study found that of the startups that secure venture capital funding in the United States (which is small fraction of the number of all startups), a third of those ventures exited with a value of zero within five years. Only 2 percent of the entrepreneurs made more than $100 million.[17] Similarly, few firms that are able to obtain patents realize any significant value from them. Most patents are worth little according to economic studies. A study for the United Kingdom found that the median patent was valued at just over US $1500.[18] Only a small percent end up being worth a lot.

Individuals and firms would be reluctant to assume these risks if they thought that the prices they could charge would be subject to uncertain and artificial caps. The process of innovation and dynamic competition that results in new products and technologies is driven by a highly skewed reward structure. A few that succeed get highly compensated, while the large majority of those who try wind up failing and getting little if anything for their efforts. That point is illustrated by the venture capital study mentioned above. A tiny fraction of the funded entrepreneurs got most of the returns.

This relationship between innovation, risk and reward is fundamental for understanding why competition authorities and courts have been reluctant to embrace unfair pricing restrictions.

Consider a competition to develop a new technology for gene splicing. There are 100 firms. Each invests 1 million Yuan a year over 10 years to develop the technology. Each firm therefore invests 10 million Yuan. Together, over 10 years, they have invested 1 billion Yuan. Only 1 firm succeeds. Thus, there is a 99 percent chance of failure and a 1 percent chance of success.

Let us suppose that to bear the risk—that there is a 99 percent chance of losing 10 million Yuan and a 1 percent chance of winning—each firm would need to expect at the beginning that they would earn 15 million Yuan or a 50 percent rate of return. In other words they would need to believe that they have a 1 percent chance of winning 15 million Yuan. The cost of capital is 50 percent since that is the minimum return that covers the risk. To participate in this technology contest each firm must believe that the winner will earn 1.5 billion Yuan. That is, in order to have a 1 percent chance of winning 15 million Yuan, the prize must be 100 times 15 million or 1.5 billion Yuan. That 1.5 billion Yuan is therefore the minimum prize necessary for inducing these 100 firms to try.

15 John Haltiwanger, Ron S. Jarmin, and Javier Miranda (2013), "Who Creates Jobs? Small Versus Large Versus Young," Review of Economics and Statistics, 95(2) 347-361, at 358.

16 David Audretsch, Patrick Houweling and Roy Thurik (2000), "Firm Survival in the Netherlands," Review of Industrial Organization, 16(1), at p. 5; Michael Fritsch, Udo Brixy and Oliver Falck (2006), "The Effect of Industry, Region, and Time on New Business Survival: A Multi-Dimensional Analysis," Review of Industrial Organization, 28(3), at pp. 292-295; Harald Strotmann (2007), "Entrepreneurial Survival," Small Business Economics, 28(1), at pp. 91-92.

17 Robert E. Hall and Susan E. Woodward (2010), "The Burden of the Nondiversifiable Risk of Entrepreneurship," American Economic Review, 100(3) 1163-1194.

18 Ariel Pakes (1986), "Patents as Options: Some Estimates of the Value of Holding European Patent Stocks," Econometrica, 54(4) 755-784.

Now consider the winner. Suppose the winner has earnings of exactly 1.5 billion Yuan. It incurred investment costs of 10 million Yuan. Its return is 150 times its investment and its rate of return is 15,000 percent. That is much higher than its cost of capital of 50 percent. Yet this is the competitive outcome. There is no excessive profit since if the winner earned less than 1.5 billion Yuan none of the firms, if acting rationally, would have entered the race in this example. Accordingly, if firms knew in advance that authorities would apply excessive pricing laws to cap their profits below that level, no technology would have been created. Moreover, even if firms believed there was a *possibility* of such a ruling, that risk and uncertainty would discourage investment.

This example encapsulates many of the issues that competition authorities and courts have had to confront in deciding whether to pursue unfair pricing cases. Limiting the rewards of successful firms squelches the effort that goes into the races to develop the very innovations that drive economic progress. The example above makes clear that comparisons of price and cost or even comparisons or the actual return to the risk adjusted cost of capital provide no evidence of excessive rewards. The rewards to the winners in these dynamic competitive races must be many times normal competitive profit, and greater than the risk-adjusted cost of capital for the individual firm, to induce the effort that goes into creating the occasional success.

IV. IPR-BASED INDUSTRIES

It has been argued that the importance of the innovation-effort-reward nexus may vary based on the industry at issue. Our own view is that it is a critical component of progress in almost all industries. In fact, human ingenuity can significantly transform even traditional industries such as farming and taxis. The considerations we have described, however, are indisputably important for industries based on intellectual property rights. Creating intellectual property to make money is a gamble. Out of all that are created, only a few books, songs, movies, video games, and patents are successful. Since most entries into this competition lose, the few that win must receive ample rewards.

Not surprisingly, competition authorities and courts have found excessive pricing involving individual holders of intellectual property rights rarely and under quite special circumstances. Indeed, leading experts have argued for putting intellectual property rights completely off limits for unfair pricing. Professor Massimo Motta, the current chief economist at the European Commission concluded that, "any good or service protected by Intellectual Property Rights should in principle not be subject to an excessive prices action."[19] Professor Amelia Fletcher, the former chief economist at the UK's Office of Fair Trading found that, "[t]here should be no intervention under Article 82 against the high prices of an innovative product within its patent period."[20] Professor Fletcher echoes the view of many observers in concluding that "[i]ntellectual property rights are specifically designed to provide innovating firms with a degree of market power, and to stimulate upfront R&D investment through the 'prize' of higher than normal future profits. Any reduction in future profits—or a greater risk of these profits being regulated—could clearly jeopardize such incentives."[21]

19 Massimo Motta and Alexandre de Streel (2007), "Excessive Pricing in Competition Law: Never say Never," in Arvid Fredenberg and Niklas Strand (eds.), The Pros and Cons of High Prices, at pp. 25-26.

20 Amelia Fletcher and Alina Jardin (2007), "Towards an Appropriate Policy for Excessive Pricing," Working Paper presented at the 12th Annual Competition Law and Policy Workshop, available at http://www.eui.eu/RSCAS/Research/Competition/2007%28pdf%29/200709-COMPed-Fletcher-Jardine.pdf.

21 Id.

While patents and copyrights by definition give their owners the right to exclude, they are very different from legal monopolies over an entire industry.[22] There is significant competition for creating patents and copyrights. Nothing prevents firms from entering that race. That is unlike state-owned enterprises, against which competition is barred, and previously state-owned companies, which commonly benefit from prior entry barriers and significant network effects. Moreover, there is often competition among patents and copyrights. There are typically numerous ways of creating products using alternative patents. And consumers can substitute between different music, books, videogames, and movies even though each is subject to a copyright.

That point is also true for Standards Essential Patents (SEPs). An SEP covers a technology that a Standard Setting Organization (SSO) has incorporated in a standard. There is debate about whether competition authorities or courts should define an antitrust market that consists of a single SEP given the static and dynamic competition among standards. But regardless of market definition, SEPs do not establish permanent barriers to entry into an industry like a postal monopoly would. At any point in time different standards compete with each other, and over time there is intense competition to develop technology for standards as they evolve and for new standards.

V. UNFAIR PRICING AND PRICE REGULATION IN CHINA

Just because other countries and jurisdictions have developed a particular antitrust policy does not mean that China must do so. Quite properly Chinese courts, competition authorities, and the State Council should consider the particular situation and economic characteristics of China and the role of antitrust policy in promoting the economic transition. In the case of unfair pricing, however, the specific circumstances of China strongly argue for embracing the international consensus to bring unfair pricing cases rarely, if ever, and for intellectual property only in connection with an exclusionary strategy.

China made a policy decision to deregulate prices and let most prices be determined by the market around three decades ago. In 1992, at the 14th National Congress of the Communist Party of China, China officially set a market-oriented economy as the target of its economic reform.[23] The Plenary Session of the Communist Party recently affirmed this policy.[24] As part of this process the Chinese government gradually removed government control over most prices in favor of letting market forces determine prices. Under the 1997 Price Law, the NDRC has wisely used its discretion to refrain from regulating prices, except in connection with certain

22 The main exception to this statement concerns music collecting societies. In some cases domestic legislation authorizes a single society to administer copyright licenses on behalf of music writers and publishers while in other cases a natural monopoly emerges. Music collecting societies are horizontal combinations of music writers and publishers. In most countries there is a single music collecting society that represents all of the music writers and publishers. Unless authorized by law these combinations can function only with an exemption under Article 101(3) TFEU. See, for example, Ernst-Joachim Mestmäcker (2006) "Collecting Societies,"in Claus-Dieter Ehlermann and Isabela Atanasiu (eds.), The Interaction between Competition Law and Intellectual Property Law, Hart Publishing. The competition authorities and courts have heard a number of claims that these national music-collecting societies have charged excessive prices.

23 See Dan Zhu, "Historical Milestones: Socialism Market Economy," People Daily, October 11, 2007, available at http://cpc.people.com.cn/GB/104019/104740/8150356.html.

24 See the Communique of The Third Plenary Session of the 18th Central Committee of the CPC, November 12, 2013, available at http://www.china.org.cn/chinese/2014-01/16/content_31213800.htm.

commodities and services that are deemed essential to consumers.[25] Notably, the NDRC has generally not regulated the prices of any product or service provided by what we would characterize as an innovation-intensive industry.[26]

Reforms and indigenous innovation policy in the last three decades have created a surge of entrepreneurship and innovation in various sectors in China. This surge included entrepreneurs starting businesses, state-owned and private enterprises initiating innovation encouraged and sponsored by the government, and foreign companies entering China to bring in additional technology and know-how. Rapidly moving and substantial dynamic competition has resulted in part from policies that enable entrepreneurs to secure rewards for the risks they took by allowing them to charge what the market will bear for their product. As a result, China has been one of the most dynamic market economies in the world, and the Chinese economy is increasingly innovation-driven.[27]

Having come to the policy conclusion that China should primarily rely on the market to determine prices it would be contradictory, and inconsistent with China's overall path towards economic growth, to use the AML to regulate prices except in unusual cases. Therefore, as a general matter, China's economic history and policies reinforce the case for applying the unfair pricing law only in exceptional circumstances. Furthermore, the decision by Chinese policymakers to encourage innovation and permit entrepreneurs to earn significant rewards for their creations is consistent with not applying the unfair pricing law to innovation-intensive industries. There are no sound policy reasons for using antitrust to pursue an intrusive approach to markets that China has otherwise abandoned with great success.

The State Council and the National People's Congress recognized the importance of intellectual property rights in the competitive process. Consistent with the advice of leading authorities and the experience of competition authorities and courts in other jurisdictions these policymakers decided that that the AML—including Article 17(1) on unfair pricing—would not apply to intellectual property rights unless it involved restricting competition.[28]

This Law does not govern the conduct of business operators to exercise their intellectual property rights under laws and relevant administrative regulations on intellectual property rights; however, business operators' conduct ***to eliminate or restrict market competition*** by abusing their intellectual property rights shall be governed by this Law. (Emphasis added.)

That is a sound approach. It restricts unfair pricing claims involving intellectual property to those cases in which unfair prices are used to exclude competitors. It is a policy that leading experts have argued for and the one that many jurisdictions around the world follow in practice.

25 NDRC of People's Republic of China Public Notice No. 11, Effective on August 1st, 2001, available at http://www.ndrc.gov.cn/zcfb/zcfbl/zcfbl2003pro/t20050707_27540.htm.

26 NDRC price regulation is, however, part of a complex government policy towards pharmaceuticals.

27 See Juro Osawa and Paul Mozur, "The Rise of China's Innovation Engine," Wall Street Journal, January 17, 2014, B1.

28 See Article 55 of the AML, supra note 1.

As we mentioned at the outset, the NDRC and the courts are at a very early stage of applying the unfair pricing law. Based on our analysis some change in direction is desirable to make their approach towards excessive pricing consistent with China's overall policies on the role of markets in setting prices and the international experience with unfair pricing laws.[29]

The NDRC has adopted price regulations that consider evidence on price differences for the same product across other buyers and sellers and whether price changes are consistent with cost changes.[30] These tests may help the NDRC identify cases in which there is no reason to believe that prices are excessive or unfair, but they are insufficient for isolating exceptional cases of excessive pricing that causes concern. It is common for prices to differ across buyers and sellers for similar products in competitive markets. It is also desirable for prices to increase in response to demand even if costs have not changed. In fact it is precisely that sort of signaling that makes decentralized market economies work more efficiently than centralized price setting. By incorporating into its regulations and analysis the more stringent tests discussed above, the NDRC would have a more robust framework for identifying those rare cases of unfair pricing that warrant intervention.

In *Huawei vs. InterDigital* the Shenzen Intermediate Court found that InterDigital had offered its patents at excessive prices to Huawei in violation of Article 17(1) and at discriminatory prices in violation of Article 17(6) of the AML.[31] InterDigital develops wireless technologies and licenses its patents on these technologies. The Guangdong High People's Court upheld this decision.[32] The parties settled the matter and there were no further appeals.[33]

The InterDigital matter is the only Chinese court case to our knowledge that has involved an application of the unfair pricing law to an innovation-intensive industry. It is difficult to conclude much about the direction that the Chinese courts will take on the application Article 17(1) to IPR given that the unfair pricing claim was just one of several antitrust claims; much of the analysis of prices themselves occurred in the FRAND contract case; the decisions themselves have not been published; and the decisions have not been heard by the Supreme People's Court. Moreover, InterDigital does not seem to have submitted sufficient evidence about its licensing agreements to permit the court to make a fully informed analysis.

29 Our longer paper discusses these issues in more detail. See Evans, Zhang and Zhang (2014).

30 In Article 11 of the NDRC Anti-Price Monopoly Regulations, "in determining if prices are unfairly high or low, the enforcement agency should consider: (i) whether the sales price or purchase price is markedly higher or lower than the price at which other business operators sell or purchase the same type of commodities; (ii) where costs are essentially stable, whether the sales price was raised or the purchase price lowered beyond the normal range; (iii) whether the level of the price increase for the sale of commodities is markedly higher than the cost increase range, or whether the range of the price reduction for the purchase of commodities is markedly greater than the transaction counterparty's cost reduction range; and (iv) other related factors." See the NDRC Anti-Price Monopoly Regulations, *supra* note 3.

31 There were two decisions regarding the abuse of dominance claim and the FRAND claim respectively. The case involving the abuse of dominance claim is Shenzhongfazhiminchuzi No. 857 (2011), and the case involving the FRAND claim is Shenzhongfazhiminchuzi No. 858 (2011). Neither decision is public. Our discussion is based on two articles published by the judges in the case as well as InterDigital's Annual report. See note 2, supra, for soruces.

32 See Zhu Jianjun, "Determination of Whether Abuse of Dominance by SEP Owners Constitutes Monopoly: Comments on the Antitrust Infringement Case Huawei v. InterDigital," China Intellectual Property News, December 5, 2013, available at http://www.cipnews.com.cn/showArticle.asp?Articleid=29779.

33 "InterDigital Settles with Huawei," WIPR, January 7, 2014, available at http://www.worldipreview.com/news/interdigital-settles-with-huawei.

Subject to these caveats, one interesting aspect of the decision is that it does not appear to have expressly addressed Article 55 of the AML, which exempts the exercise of IPRs from antitrust scrutiny unless those rights are used to eliminate or restrict market competition. [34] It may be that the court concluded that the extreme disparities it found in rates charged to different licensees had such an anticompetitive effect, but that is not clear from the information about the case that is publicly available.[35] If the court did not make such a finding, it would be hard to reconcile the decision with Article 55. In that case, the court's approach would also be inconsistent with the approach in most other jurisdictions of limiting excessive pricing cases regarding IPRs to situations in which a firm pursued an exclusionary strategy.[36]

Nevertheless, the judges for the Shenzhen Intermediate Court made a conscientious effort to address a set of difficult issues concerning negotiating FRAND royalty rates for SEPs. They were not the first to find this topic challenging. We are therefore optimistic that the Chinese courts will find the approach towards unfair pricing followed in other jurisdictions, and in particular towards innovative-intensive industries, helpful in shaping the case law on the application of Article 17(1).

VI. CONCLUSIONS

China is at the very beginning of developing the best way to apply its new antitrust laws to its economy. Chinese courts and regulators should certainly not simply parrot the practice of other countries, but China can learn from the many decades of experience and numerous cases considered by courts and competition authorities, particularly the large ones in the European Union and the United States. China carefully modeled its laws from elements of these jurisdictions, and the courts and competition authorities are looking at international practice. It therefore makes sense, in the case of unfair pricing, to consider how competition case law and policy has evolved in other jurisdictions.

Both the practice of other jurisdictions and sound economic analysis recommends that China should rarely if ever apply the unfair pricing law to innovation-intensive industries unless the unfair pricing is related to an exclusionary practice that has an anticompetitive effect. For the same reasons, and as apparently required under Article 55 of the AML, the experience of other jurisdictions and sound economic analysis strongly suggests that the unfair pricing law should not apply to intellectual property except when the unfair price is part of an exclusionary abuse.

34 See Lu Yanchun and Liu Jian, "A Preliminary Treatise on Antimonopoly Regulation of IPR Abuses," Legal Daily, March 19, 2014, available at http://epaper.legaldaily.com.cn/fzrb/content/20140319/Articel12001GN.htm

35 The existence of such disparities would not by itself, however, demonstrate that competition was eliminated or excluded in handset manufacturing.

36 InterDigital also did not have a monopoly over an entire industry like the post office. It was one of a number of entities that had SEPs over mobile wireless technologies.

The 2013 Amendments to Japan's Anti-Monopoly Act: Some History and a Preliminary Evaluation

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In this paper we discuss the main features of the 2013 amendments to Japan's Anti-Monopoly Act (the 'AMA'). The paper is divided into three parts. To provide an evolutionary perspective, Part I contains a condensed historical background of Japanese antimonopoly policy. Part II presents aspects of the 2013 amendments that we would highlight for an international audience. Part III provides a preliminary evaluation of this latest round of reforms.

I. SHORT TOUR OF SEVEN DECADES

With around 20 different series of amendments made to the Anti-Monopoly Act thus far, together with various vicissitudes of policy, the evolutions of Japanese competition law and policy are long and complex. They have been recounted on numerous occasions, and occasionally the story has been told in English.[1] We therefore do not belabor the history too much here. Nevertheless, it is worth recalling some of the notable milestones and setbacks so that the latest changes to the AMA may be seen in their historical context.

In parallel with analogous events that unfolded in Germany in the aftermath of World War II, the foreign powers occupying Japan, and specifically the US military wing operating as 'GHQ' (General Headquarters, also known as 'SCAP' – Supreme Commander of the Allied Powers), sought to install a competition law regime in an Asian society that could hardly have been less prepared for it. Since the Meiji years of the late 19th Century, Japan had been building an economic system based not on free enterprise (even if it was largely driven by a desire to 'catch up' with the Western world, and thereby to avoid colonialism), but on the principle of State-led development. As the scale of industry in key sectors grew to grotesque proportions, the *zaibatsu* (family-owned mega-conglomerates) emerged, and the economy itself came to be instrumentalized for the interrelated ob-

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For recent retrospectives, see, e.g., Michiyo Hamada, 'Institutional Structure and Change Regarding Competition Law and Policy in Japan', in Philip Lowe, Mel Marquis and Giorgio Monti, eds., European Competition Law Annual 2014: Institutional Change and Competition Authorities (forthcoming, Oxford: Hart Publishing); Etsuko Kameoka, Competition Law and Policy in Japan and the EU (Cheltenham: Edward Elgar, 2014), chapter 2. See also the various citations included in Mel Marquis and Tadashi Shiraishi, 'Japanese Cartel Control in Transition', CEU San Pablo University Madrid Working Paper No. 47/2014 (Competition Policy Series) 1-21, available at http://ssrn.com/abstract=2407825.

jectives of self-sufficiency, regional power and militarization. Infamously, pursuant to measures adopted in 1925, 1931 and 1938, many industries were required by law to be cartelized. In some respects the line between State and market melted away.

Against the background of this Lewis Carroll kind of world, the 1947 Anti-Monopoly Act was a form of shock therapy: it was not a mere set of prohibitions but a revolutionary exercise in economic engineering (and part of a broader 'economic democratization' plan) that went well beyond the US model.[2] The rigid constraints of the original Act proved to be controversial even in Washington, D.C., and while some key Japanese officials that had interacted with GHQ as the Act was being drawn up welcomed the concept of an open market economy and embraced the new legislation, it was not long before the enemies of the AMA launched legislative counter-attacks.

Thus, in 1953 – the year after Japan regained her sovereignty – the AMA was modified substantially, though it was not hollowed out completely. Japan's antitrust warriors of that age, sensing that a watering down of the legislation was inevitable, opted for a 'strategic retreat', as Hamada has called it, whereby they were able to preserve parts of the Act and even to expand its scope to a certain extent by transforming the 'unfair methods of competition' concept into 'unfair trade practices' – to be defined from time to time by the Japan Fair Trade Commission ('JFTC'). Over the years, this category of unfair trade practices has been the basis for a great deal of enforcement in relation to unilateral practices, including but not limited to monopolization-type practices.[3] In a sense, one may take the view that the 1953 amendment 'saved' the AMA, which might otherwise have been scrapped altogether, taking the JFTC with it.[4] On the other hand there is no denying that, with the introduction of an exemption system for 'recession cartels' and 'rationalization cartels', Japanese antitrust in the 1950s and 1960s withered while the instincts of the Developmental State were revitalized and vindicated, as it were, by periods of vertiginous economic growth.[5]

2 For further background regarding the economic democratization campaign and the dismantling of the giant conglomerates, see Thomas A. Bisson, Zaibatsu Dissolution in Japan (Westport: Greenwood Press, 1976). On the draconian provisions of the AMA as originally enacted in 1947, see Simon Vande Walle, 'Competition and competition law in Japan: between scepticism and embrace', in Michael Dowdle, John Gillespie and Imelda Maher, eds., Asian Capitalism and The Regulation of Competition: Towards a Regulatory Geography of Global Competition Law (Cambridge: CUP, 2013) 123-143, at 124-125.

3 See Hamada, 'Institutional Structure and Change', cited above note 1.

4 Other independent agencies were in fact dissolved: for example, the Securities and Exchange Commission was scrapped in July 1952, a mere three months after the departure of the US forces.

5 This 'vindication', i.e., the sense that the relaxation of competition law in Japan was stoking its economic engines, was deceptive. First of all, a number of other factors contributed to Japan's rapid growth, including not least the extraordinary availability of easy credit, a policy supported by the Bank of Japan, or tax reductions implemented under Prime Minister Ikeda to provoke spending. By late 1964, Japan's GNP was growing at a rate of nearly 14%, and the country rode the cresting wave through the end of the 1960s, with the economy growing at 10-12% between 1966 and 1970. Looking from a wider angle, the growth rate from 1955 to 1990 was 6.5%. Second, some of Japan's prosperity was due to industries in which competition was fierce (specifically, those in which Japan excelled internationally), even if competition law enforcement was generally lax. Japan has often been described as a 'dual economy' in light of this distinction in the competitiveness of different sectors (although the less competitive, low-productivity domestic sector is far larger than its sleeker counterpart, which partly explains Japan's prolonged slump). See, e.g., Michael Porter and Mariko Sakakibara, 'Competition in Japan', 18 Journal of Economic Perspectives 27-50 (2004).

The 1970s, and 1977 in particular, were a watershed for the enforcement and content of the Anti-Monopoly Act. Once again, institutional change arose not for purely legal reasons but as a function of context. It was the onset of rampant inflation – linked to the first Oil Shock in 1973 as well as other factors – that created an environment of public sentiment favorable to the aggressive (criminal) prosecution of oil companies in Japan for price-fixing and other allegedly illegal collusive conduct. For the first time, the JFTC's role as antitrust enforcer was well aligned with public opinion at large. Indeed, Japan in the 1970s was one of the very few settings worldwide in which the role of antitrust in society has risen to the level of 'high national politics'.[6] The proposals of the JFTC and its Chairman at that time, Takahashi Toshihide, did not sail unmolested through the Diet: the legislative debates were protracted over four years, not unaccompanied by the vagaries and scandals of Japanese politics. Eventually, the virulent, business-backed opposition to the proposals led to a number of compromises.[7] The details of this saga may be omitted here but the main outcome of the 1977 amendments – the introduction of the administrative 'surcharge' – must be underlined, as it sowed the seed for significant subsequent developments. The reason that no monetary penalty or disgorgement system had been installed in the original AMA was that, like the Sherman Act, the AMA contemplated criminal sanctions for infringements; and in Japan, there was a perception that requiring firms to pay any charge comparable to a fine would be unconstitutional on grounds of double jeopardy. Nevertheless, by the 1970s there was increasing dissatisfaction with the JFTC's limited toolbox of remedies. On the one hand, a cease-and-desist order alone had little deterrent effect because ill-gotten gains were safely retained by violators. On the other hand, criminal prosecution was both (i) difficult *per se* given the elevated standard of proof, and (ii) further complicated by what were (and to some extent still are) tense relations between the JFTC and Japan's Public Prosecutors' Office. The solution was the surcharge system; but given the sensitivity of the issue, its original form was cartoonishly weak in magnitude and scope, and in its institutional dimensions. The modest amounts of surcharges imposed following the 1977 amendments, which the JFTC had no discretion to adjust, fell well short of clawing back the full extent of anticompetitive overcharges.[8] Yet those baby steps have over time evolved into a *de facto* system of fines of 21st Century magnitude. This causes some anxiety in Japan today, and once again the specter of double jeopardy is commonly invoked by the business community and other critics.

The final historical (i.e., pre-2013) reform that should be recalled here is the 2005 amendment, which may be regarded as Japan's belated coming of age as far as competition law is concerned.[9] The momentum for the modernization of antitrust enforcement in Japan began to build slowly in the early 1990s from a confluence of

6 Michael Beeman, Public Policy and Economic Competition in Japan: Change and Continuity in Antimonopoly Policy, 1973-1995 (London and New York: Routledge, 2002) 69.

7 See ibid., pp. 73-74 and 88-95; and Hamada, 'Institutional Structure and Change', cited above note 1.

8 The modest percentages that were used to calculate relevant proportions of sales were justified by allegedly low average profits generated by businesses across Japan. By institutionalizing uniform assumptions about the profitability of an extremely wide range of industries, one has to wonder whether the surcharge system was inherently discriminatory. In any case, the low levels of assumed profitability are in stark contradiction to the findings that have emerged in a number of empirical studies generally focusing on international cartels. Typical estimates gravitate around 15-20%, whereas the original surcharge under the 1977 amendments was limited to just 2% of sales in the case of manufacturers, 1% for retailers and 0.5% for wholesalers.

9 This coming of age (which should not be misunderstood as a dilution of identity; competition law and policy in Japan remain highly distinctive in many respects) may be seen, in Teubnerian terms, as part of a process of the reciprocal 'irritation' and co-evolution of the Anti-Monopoly Act on the one hand (Teubner's 'legal irritant') and Japanese society and its culturally determined form of ambiguous capitalism on the other. For this conceptualization, see Vande Walle, cited above note 2, for example at 139.

'winds' blowing from outside and from within the country.[10] The tailwind of the Structural Impediments Initiative (1989-1993), wherein the US Government extracted promises from Japan to tighten up enforcement as part of a larger package of measures designed to address the swollen trade imbalance between the two countries, was the most conspicuous driver from the perspective of outside observers. The headwind of an endogenous change of *ethos*, linked to Japan's stalling economy, was less visible but arguably even more powerful as an explanatory factor behind Japan's 'turn' (back) toward serious antitrust.[11] This endogenous development culminated in (i) greater political commitment (under Prime Minister Koizumi), and with it the ascendance of the JFTC to the rank of a ministry-level organ, and (ii) an important new legislative proposal, under the leadership of then-Chairman Takeshima, that led to the 2005 change in the law. In the course of that 15-year span of time, the AMA itself as well as separate provisions on (government-assisted) bid-rigging and the powers of the JFTC were all progressively reinforced (and a bewildering variety of exemptions were progressively suppressed) by amendments made in 1991, 1992, 1996, 1997, 1999 and 2002. But the major principal additions and revisions made to the AMA in 2005 can be summarized as follows.

- The rates applying under the surcharge system were (again) raised, as a result of which, for example, manufacturers must now pay a charge equal to 10 percent of (cartelized) sales.[12] Related reforms included an expansion of the types of conduct for which surcharges are assessed,[13] a 'discount' where a criminal fine is also imposed,[14] and an intensification of the surcharge rate in the case of recidivism (whereby the repeat offender pays 150% of the otherwise applicable charge[15]). The reinforcement of the surcharge system, though justifiable in itself, was particularly vital in light of the second major element of the reform. Specifically:

- For the first time, and over stiff opposition, the reforms incorporated within the AMA a statutory leniency program. This aspect of the reform was undeniably driven by a tailwind that caught the imag-

10 The 'winds' metaphor, which implicitly evokes other legendary events from Japanese history, is borrowed from Hamada (cited above note 1).

11 For discussion of the links between Japan's economic malaise and the anti-monopoly 'renaissance', see Marquis and Shiraishi, 'Transition', cited above note 1. See also Vande Walle 'Competition and competition law in Japan', cited above note 2 (underlining Japan's counter-cyclical enthusiasm, so to speak, for the antitrust enterprise).

12 The fiction that the surcharge system is purely about disgorgement of illegal profits has become increasingly tenuous in Japan, and it is widely understood that the system's real concern today is deterrence. (A judgment of the Supreme Court of Japan issued on 13 September 2005 supports the decoupling of the surcharge concept from that of disgorgement.) As we suggest below in part III of this paper, the applicable surcharge rates have still not reached adequate levels to deter misconduct. However, it must be acknowledged that fine levels in themselves are probably never a sufficient determinant of compliance, particularly where, as is the case de facto in Japan (and leaving aside the special sphere of bid-rigging), individual penalties are rarely if ever imposed for price-fixing behavior.

13 For example, together with a subsequent reform in 2009, the 2005 amendment required that the application of surcharges extend beyond horizontal collusion to reach firms found to have engaged in, inter alia, resale price maintenance (repeat infringers only), 'private monopolization', the abuse of a superior bargaining position and 'unjust' low-price sales even absent a dominant position (again, repeat infringers only).

14 In the relatively rare scenario that a criminal fine is imposed in the same case, the surcharge is reduced by an amount equal to half of the fine. The discount may be seen as a solution, albeit an awkward one, to the above-mentioned concerns about double jeopardy.

15 Following the amendments made in 2009, a firm that played a leading role in a cartel is likewise to be charged 150% of the normally applicable rate. When the leading cartelist is also a recidivist, the jackpot rate of 200% is attained.

ination of Chairman Takeshima, and he refused to cave in despite a barrage of legal and cultural objections. Contrary to critics' predictions, the leniency program has proved successful[16] – perhaps even too successful, as it is not entirely clear that the high number of applications can be timely processed and converted into investigations. Although the program is generally transparent, some of the details regarding its operation have not been disclosed.[17]

• A third major reform in 2005 concerned the procedures governing JFTC investigations. As a means of rationalizing what were arguably byzantine sequential procedures, the old 'recommendation decisions' and consent decisions were abolished, and the cease-and-desist device and the surcharge payment order were combined within a unified procedure. As a controversial consequence of this restructuring, pre-order (i.e., pre-surcharge) hearings were replaced by post-order hearings guaranteeing a right to be heard which, from the perspective of a firm subject to such an order, comes palpably too late.[18]

In an almost neo-functionalist manner, the third reform described above – i.e., the switch to a post-order hearing – has itself triggered the latest round of reforms in 2013, as the Japanese legislature seems to have accepted the view that procedural fairness was illusory when a firm subject to a payment order had to appeal, at first instance, to the very institution that imposed it.

We may turn now to a discussion of these recent amendments. As will be explained, a largely unforeseen repercussion of the 2005 reforms is that they have led to the accidental suicide of the JFTC's hearing procedure.

II. HIGHLIGHTS OF THE 2013 AMENDMENTS TO THE ANTI-MONOPOLY ACT

The Japanese 'Diet' (*Kokkai*) passed the bill to amend the 'Act Concerning Prohibition of Private Monopolization and Maintenance of Fair Trade' (i.e., the AMA) on 7 December 2013.[19] The new law was promulgated six days later. This amended version of the AMA will take effect on a day to be specified by Cabinet Order no later than mid-May 2015. As of early October 2014, the Order had not yet been issued.

The 2013 reform was aimed mainly at procedural and institutional matters, but it is also apt to influence the AMA's substantive enforcement. In general, the reform can be understood as the counterpart to, and in some ways the unintended consequence of, the 2005 amendments described above. Its contents may be outlined as follows:[20]

16 Leniency was further refined by the 2009 amendments. Since the program was activated on 4 January 2006, the JFTC has been receiving an average of nearly 100 leniency applications per year (with a two-year spike in FY 2010-2011); failure to seek leniency may provoke shareholder derivative litigation. For details, see Toshiyuki Nambu, 'A Successful Story: Leniency and (International) Cartel Enforcement in Japan', 5(3) Journal of European Competition Law and Practice (2014); Hamada, 'Institutional Structure and Change', cited above note 1, at footnote 65 and accompanying text.

17 See Harry First and Tadashi Shiraishi, 'Japan: The Competition Law System and the Country's Norms', in Eleanor Fox and Michael Trebilcock, eds., The Design of Competition Law Institutions: Global Norms, Local Choices (Oxford: OUP, 2013) 232-265, at 243.

18 For further background concerning the debates over the merits of the pre-order and post-order hearings, see Mitsuo Matsushita, 'Reforming the Enforcement of the Japanese Antimonopoly Law', 41 Loyola University of Chicago Law Journal 521-534 (2010). See also First and Shiraishi, 'Japan', cited previous footnote, at 246-248 and 261-162.

19 See JFTC Press Release of 9 December 2013, 'Enactment of the Bill to Amend the Antimonopoly Act', available at http://www.jftc.go.jp/en/pressreleases/yearly-2013/Dec/individual131209.html.

20 The new features to which we refer here are found in Articles 85 et seq. and Articles 51 et seq. of the AMA, as amend-

1. The hearing procedure for administrative appeals, whereby since 2005 the JFTC has functioned as its own court of first instance, as it were, is to be abolished. The 2005 appeal system, pursuant to which the final decision of the JFTC was appealed before the Tokyo High Court (an intermediate court situated between the District Courts and the Supreme Court), is likewise to be abolished.

2. A new system for appeals brought against administrative measures adopted by the JFTC will be introduced. Exclusive jurisdiction over such appeals is attributed to the Tokyo District Court, and specifically to a panel of three or, if necessary, five judges. The hope is that this approach will allow the District Court to develop specialized antitrust expertise and to accumulate institutional experience, thus promoting quality and consistency across different judgments. On subsequent appeal the Tokyo High Court will assign the case to a panel of five judges. As has always been the case, final appeals will be heard by the Supreme Court of Japan.

3. Changes will also be made to administrative procedures that lead to the adoption of cease-and-desist orders and other measures by the JFTC. The relevant reforms involve: (i) the designation by the JFTC of hearing officers (distinct from the Hearing Examiners that have until now been hearing post-order administrative appeals[21]), who will preside over the administrative hearing; (ii) the possibility for alleged infringers to obtain an explanation regarding the contents of measures the JFTC expects to adopt; and (iii) the possibility for alleged infringers to inspect and photocopy the evidence taken from them and used by the JFTC to build its case, subject to limited grounds for refusal by the JFTC, such as where disclosure would cause harm to third parties.

In procedural and institutional terms, the above provisions amount to a fairly radical overhaul. Several observations can be made in this connection. First, with regard to the new appellate structure, the requirement of a minimum three-judge panel is a notable departure from the general custom for judicial review of administrative decisions, where only a single judge hears the case. The purpose behind this new approach is to ensure the careful examination of competition law decisions in light of the complicated fact-finding on which they are based, the unusual degree of expertise and sophisticated analysis embedded in those decisions, and their significant influence on business activities and the economy – arising, e.g., from the indirect effects of Type I and Type II errors. The shift from a two-tier to a three-tier appellate system (District Court, High Court, Supreme Court) may perhaps also be seen as introducing an additional possibility to correct errors.

Second, the notion that the JFTC's decisions should be subject to closer scrutiny is reinforced by the abolition of the 'substantial evidence' rule, which until now has to a large extent bound the Tokyo High Court to the JFTC's findings of fact. Unhampered by this rule, the Tokyo District Court will be able to assess both the accuracy

ed. For a more detailed summary, see JFTC, Outline of the Bill to Amend the Antimonopoly Act, available at http://www.jftc.go.jp/en/pressreleases/yearly-2013/Dec/individual131209.files/Attachment01.pdf.

21 The hearing officer cannot be any person that has been involved in the investigation of the case. Unlike the Hearing Examiners under the 2005 system, hearing officers will not prepare a preliminary decision. On the roles of the soon-to-be-defunct Hearing Examiners under the current system and the hearing officers under the new system, with comparisons to role of the Hearing Officer of the European Commission, see Toshiaki Takigawa, 'Balancing Fairness and Efficiency in the Globalized Competition Law Enforcement: Insights from the JFTC Experiences', CPI Antitrust Chronicle, June 2014 (1).

and the completeness of the JFTC's factual conclusions. At the same time, an embargo against the appellant introducing new evidence on appeal to challenge the JFTC's decision has also been lifted. In the shadow of this enhanced scrutiny, the quality of the case mounted by the JFTC can be expected to improve.

Third, it can be seen that the reforms are partly intended to improve elements of due process. Most fundamentally, the abolition of the 2005 (post-order) hearing procedure reflects this aim. But a number of second-order changes are equally relevant. Thus, as noted above, the JFTC's investigators may be called on to provide explanations of the expected content of cease-and-desist orders and other measures. Such explanations may concern, in particular, the facts established by the JFTC, the application of laws and regulations to those facts, and the nature of the relevant evidence. In addition, a party under investigation may appoint a representative for the purpose of presenting its opinions. It may attend hearings, submit its views, offer evidence and put questions to investigators.[22] Designated hearing officers will prepare a written record of the opinions of parties attending the hearings, which is then submitted to the JFTC. When formulating its decision, the JFTC is required to give due consideration to the record and report submitted by the designated officers.

III. PRELIMINARY EVALUATION OF THE 2013 REFORMS

Some commentators have expressed concerns about the latest amendments on the ground that they degrade the JFTC's ability to manage its competition cases. It has been suggested that, by maintaining an administrative proceeding that encompasses an adversarial hearing, the JFTC could have accumulated substantial knowledge and experience from the exchange of opinions with parties under investigation.

Others have been critical because, in their view, the 2013 amendments fail to establish sufficiently strong rights for defendants. They regard the reforms as being only a partial response to the defects, in terms of procedural guarantees and fairness, that blight the current framework. Additional safeguards are thus called for, including, e.g., the right to have an attorney present during questioning, recognition of attorney-client privilege, and other procedural means of protection.[23]

From a quite different perspective, one could also criticize the reforms for failing to address the (im)potency of sanctions prescribed by the AMA in cases involving serious infringements such as price-fixing, market sharing and similar forms of naked collusion.[24] The JFTC's anomalous lack of discretion in imposing surcharges also remains unaddressed.

A definitive assessment is problematic at the present stage, and we cannot easily draw any final conclusions. This is partly because the precise contours of the reforms have not yet been decided by the relevant Cabinet Order (see above), and more importantly because it may well take a few years of practice to determine

22 The party may submit written statements and other evidence instead of attending the hearings.

23 See Daizo Kawai, 'Influences and Practical Issues: The 2013 Amendment of the AMA', Shojihoumu No 2028, 36 (2014).

24 The persistent weakness of the surcharges provided for under the AMA, despite repeated reforms to address this issue, has been noted by many commentators. See, e.g., Shuya Hayashi, 'The goals of Japanese competition law', in Josef Drexl et al., eds., Economic Theory and Competition Law (Cheltenham: Edward Elgar, 2009) 45-69, at 67; Marquis and Shiraishi, 'Transition', cited above note 1, at page 6, footnote 2 in fine.

the ways in which the reforms will influence the practice of the JFTC and of Japan's courts. We would however make the following observations, which can frame the evaluation of the 2013 reforms going forward.

First, it is implicit from the content of this short article that elements of efficient and effective enforcement are sometimes in tension with the objective of maintaining high standards of due process. Efficiency and effectiveness are obviously important parameters of output and of output legitimacy, but due process is equally important: it is not only desirable for its own sake but also serves as a means of earning the trust of those expected to comply with the law, which is to say that effective and legitimate enforcement are to some degree interconnected.[25] This is a dynamic tension that is still evolving in Japan, and the 2013 amendments are surely only a mile marker. There is much work yet to be done to develop both the effectiveness and the due process dimensions.

Second, the reforms discussed above should not be isolated from institutional considerations. It is recalled that Trebilcock and Iacobucci classify competition law enforcement institutions according to three categories.[26] First, there are specialized and separate investigative and enforcement authorities that must bring formal complaints before courts in order to obtain remedial relief (the *bifurcated judicial* model). Second, there are specialized enforcement agencies that must bring formal complaints before separate, specialized adjudicative agencies (the *bifurcated agency* model). And third is the *integrated agency* model, generally associated with the civil law tradition, where a single agency comprehensively undertakes investigative, enforcement, and adjudicative functions. Various combinations of these three models are of course possible as well.

One recent study suggests that, in jurisdictions where courts are weak, the bifurcated and integrated agency models have some significant advantages. On the other hand, where courts are strong, independent, honest and efficient (as is generally true in the US and in other established jurisdictions), the bifurcated judicial model has some significant advantages.[27] It may be that the Japanese competition law system has not quite arrived at the stage where immediate advantages will likely be gained by assigning more responsibility and quality control powers to the courts (without going so far as to switch to a bifurcated judicial model, since the JFTC will retain its investigative and remedial powers). In the medium term, as the Tokyo District Court moves down the 'experience curve', the benefits of the 2013 reforms might begin to manifest themselves. In the meantime, however, there is a more immediate advantage that may be derived. Specifically, this relates to the perception that both due process and efficiency will be better served under the new system, since: one on the one hand it casts the shadow of judicial scrutiny over the administrative procedure; while on the other hand it eliminates an apparently superfluous layer of bureaucracy. As suggested above, however, any such improvements should be seen as intermediate in nature, as the need for reform in Japanese antitrust has not been quenched.

25 See generally Philip Lowe, Mel Marquis and Giorgio Monti, eds., European Competition Law Annual 2013: Effective and Legitimate Enforcement of Competition Law (forthcoming, Oxford: Hart Publishing).

26 Michael Trebilcock and Edward Iacobucci, 'Designing Competition Law Institutions', 25(3) World Competition 361-394 (2002), at 361-363.

27 Eleanor Fox and Michael Trebilcock, 'Introduction: the GAL Competition Project: The Global Convergence of Process Norms', in Fox and Trebilcock, eds., The Design of Competition Law Institutions, cited above note 17, pp. 1-48.

Overview of Current Antitrust Enforcement in Korea

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Antitrust enforcement in Korea has witnessed many changes in the past year since a new political leadership took place as a result of the December 2012 presidential election. Ever since the 2008 global financial crisis, Korea has experienced economic difficulties similar to most other economies in the world. Korea's difficulties were considered more troubling because they dramatically exacerbated many of its existing problems. Experts have been concerned with Korea's loss of potential economic growth momentum in two aspects: limitations of existing growth strategies and economic and social bi-polarization. The new administration has tried to solve these issues by emphasizing the so-called "creative economy" as a key economic policy and by taking measures to protect small and medium sized firms (the "SMEs"). As Korean competition policies were mandated to play a major role for this latter goal, it seems to have dominated Korean competition policy for the last one and a half years.

As widely known, Korean competition policy is composed of two large blocks: on one hand, there are the traditional antitrust policies that pay attention to the creation and maintenance of market power in the context of market competition; and on the other, fair trade policies that aim to control unfair trade practices deemed to harm firms in inferior transaction positions or SMEs. Recent political and social circumstances required the Korea Fair Trade Commission (the "KFTC") to concentrate on fair trade policies to protect SMEs, especially in the distribution industry and retail markets.

This short article briefly describes Korean antitrust enforcement since 2013 to its present stage.

ANTITRUST ENFORCEMENT

Since the landmark POSCO Decision in 2007 that set a limitation to the application of the abuse of market dominance clause by requiring a rigorous show of anti-competitive effects, the KFTC seems to have become cautious to enforce the provision. Instead the KFTC has relied on the unfair trade practice clauses in regulating single firm conducts that require proving unfairness of conduct rather than its restrictive effects on market competition. This approach resulted in a smaller number of abuse of market dominance cases. Since the 2009 Qualcomm and Intel cases that involved loyalty rebate practices, we haven't seen many notable cases of abuse of market dominance. In fact, since 2011 until today, the KFTC has been successful in only one case about hindering kiwi fruit distribution to impose corrective orders and fines of half a million USD. This is a dramatic decline compared to the 38 successful cases pursued in the sole year of 2007. Many experts are concerned with this trend pointing that it may undermine the reputation of the KFTC as the guard of sound market competition.

However, the story of cartels is totally different. The KFTC has maintained a strict approach regarding cartels throughout the recent years and private damages suits have become more popular than ever. In 2013, the KFTC imposed corrective orders on 29 cartel cases with monetary fines totaling more than USD 354 million. Major cartel cases have involved various industries including express railway construction, life and fire insurance, atomic power plant construction, car rental, and etc. The KFTC has also been active in penalizing international cartels. In July 2013, it imposed fines totaling USD 89 million on six global automakers, including local Hyundai Motor Co., for price fixing of truck prices.

In the last several years, we have seen a significant increase in the number and volume of private damages actions even without further legislative action promoting private enforcement. Although the exact number of damages suits is hard to identify, experts estimate that at least 30 damages suits were pending at civil courts as of the end of 2013. Most of the actions were follow-on lawsuits filed after a KFTC decision. The plaintiffs were diverse, ranging from corporate purchasers to a large number of indirect purchasers (for example, taxi drivers in LPG price fixing cases), and even public enterprises and local government. Several reasons may be attributed to this increase, but tough sanctions by the KFTC and antitrust policies encouraging damages suits (so that cartel gains are minimized) are acknowledged as the primary drives. Leniency policies, which became extremely popular for businesses to avoid heavy monetary fines, are also considered a major cause. In leniency cases, cartelists have a hard time avoiding liability at civil courts due to the clear evidence the KFTC obtains from leniency applicants which is then passed on to the civil courts. Hence, in such cases, the only issue remaining is calculation of the amount of damages.

The largest damages suit to be successful in history was the military oil bid rigging case in which the civil court utilized model econometric methods to quantify damages. In 2013, after thirteen years of tough litigation, the parties settled for USD 132 million to be paid to the Korean government. The most significant and influential case among recent cases was probably the 2012 wheat flour cartel case in which the Supreme Court awarded damages of USD 1.5 million to one of the largest bakery firms. In the ruling, the Court refused to recognize the passing-on defense but agreed to adjust amount of damages to avoid double compensation for fairness. Because of the significant amount of damages and findings of law confirmed in the court proceedings, this case is considered to have laid the foundation for the increased level of private litigation as seen today, despite generally hostile circumstances for antitrust damage actions.

Regarding merger control, the most recent big case was the abandonment of the proposed P3 Network alliance. The KFTC and the Anti-Monopoly Bureau of the Ministry of Commerce in China ("MOFCOM") have been reported to have cooperated to evaluate the potential competitive effects of the proposed establishment of an alliance among top three international ocean shipping companies. In June 2014, MOFCOM announced its prohibition decision and the companies eventually dropped the proposal. Consequently, the KFTC closed the case. This was a surprise to many because it came after an approval decision from the US Federal Maritime Commission and a similar approval by the European Commission. Hence, it was considered to show the new regulatory power of Asian jurisdictions while also exhibiting the trend of cooperation among Northeastern Asian antitrust authorities to deal with major international antitrust cases.

Regarding antitrust enforcement on IPRs, the new administration's economic policy focuses on the "creative economy" deeming it vital to revive a bad economy. Hence, policies to create and protect IPRs tend to take top priority. IPRs are considered critical because of their significant share of the IT industry in Korean economy, e.g. Samsung Electronics. This has been reflected in antitrust policies and the KFTC has implemented many tools to achieve such goals. The KFTC has amended antitrust guidelines to regulate IPRs and performed several Market Inquiry and Surveys to obtain market information and identify potential violations. These efforts led to the pay-for-delay case between GlaxoSmithKline Korea and Dong-A Pharmaceutical Co., Korea's no. 1 pharmaceutical company. In 2011, the KFTC imposed fines of approximately USD 2.6 million for GSK and USD 1.8 million for Dong-A, along with a cease-and-desist order. These sanctions were finally approved by the Supreme Court in February 2014. It made Korea the second jurisdiction in the world to produce a final court's judgment that confirmed cartel liability of reverse payment practices.

Lastly, regulations over unfair trade practices have become more important in recent years due to its connection to correcting unfairness among firms. This category of enforcement has been considered a tool to protect SMEs from abuses of superior bargaining positions of large businesses. In Korea, small retailers and manufacturers have been considered to be a victim of aggressive and unfair practices by large firms. Also, as the prohibition of unfair trade practices has recently acquired more attention, several new legislations have been enacted to make clear that certain trade practices are regulated in particular industries. The most recent one was the "Act on the Fair Trade in Large-Scaled Distribution Businesses," enacted in 2012 (amended in July 2013) that aimed to protect interests of small suppliers and store lessees by prohibiting certain conducts of large distribution channels like discount stores or department stores. Typical violations include delaying payment of sales prices, refusing or delaying receiving goods, passing on sales promotion costs, and etc. However, such strict enforcement of unfair trade practices has also drawn criticism from experts in that it may ignore economic efficiencies in attempting to protect inefficient SMEs. Such critics argue that such a role should be played by other government agencies rather than the KFTC even if it is deemed necessary.

ENFORCEMENT OF SUBCONTRACT TRANSACTIONS ACT

As noted earlier, current mandates of the KFTC seems to extend to protection of SMEs. In Korea where subcontracting is extremely widespread in most industries, protecting the interests of SME subcontractors is considered essential to maintain a sound market structure. As economic bi-polarization has worsened in recent years, this issue has become the top priority of competition policies and the KFTC has invested a lot of resources in this area. For example, treble damages were introduced to certain violations like unfair price cuts or cancellation of orders. Until present, only one violation of the misappropriation of technologies was subject to treble damages. The introduction and expansion of treble damages is significant in that it was pursued against opposition from many experts who argued that it was not in harmony with the Korean judiciary system.

Such aggressive enforcement efforts led to the 2013 Daewoo Shipbuilding & Marine Engineering Co. (one of the largest shipbuilders in the world) case in which a record high fine of USD 25 million was imposed for unilateral price-cutting.

REGULATIONS OVER LARGE CORPORATE GROUPS

Korean competition policy has long concentrated on regulations over certain large corporate groups (the "Chaebols"). While most of existing regulations regarding Chaebols were lifted during the last administration that valued the efficiencies of Chaebols, such issues resurfaced in the last presidential election as critical points. Their significance grew due to the aggravated economic situation of SMEs, and as a result "economic democratization" became a core issue of election debate. The current president promised to push for such economic democratization and, as a result, relevant parts of Korea competition law were amended in 2013.

Among these, provisions that prohibited direct cross-shareholding between two affiliated companies under a same large corporate group were amended to extend to circular shareholdings, and hence, any new circular shareholdings and or any measure to strengthen existing circular shareholdings among three or more affiliated companies were made illegal. The rationale of such regulation is that circular shareholding makes it possible to increase or maintain the control of a corporate group with a small amount of shares, and also be used to facilitate inheritances. The amendment does not apply to the existing circular shareholdings, but it requires disclosure of important decisions made by the board of directors, thereby indirectly influencing the voluntary dissolution of existing circular investments.

Another important regulation was the extension of existing prohibitions regarding unfair intra-group assistance. Providing abnormal benefits to families of group owners was illegalized and recipients and providers of such unfair assistance are subject to fines alike (before only providers were fined).

ISSUES REGARDING ENFORCEMENT PROCEDURES

One of the most notable issues is the availability of the new consent order system. Before 2011, when consent orders were first introduced as a result of Korea-U.S. Free Trade Agreement, there was no way to terminate an antitrust case by settlement between a defendant and the KFTC. This problem became an issue in the 2004 Microsoft tying arrangement case in Korea. Even after its introduction, however, no consent order cases were brought because the KFTC and companies were worried about public criticism about suspicions of potential collusion. In fact, many critics considered this measure contrary to legal justice and beneficial only to large companies. Yet, for the first time in 2013, the NHN Corp. and Daum Communication Co., the two largest Internet portal companies in Korea, applied for consent orders in an unfair trade practice case. These consent orders were approved in February 2014 after long negotiations regarding the appropriate remedies. The remedies included measures to address anti-competition problems that were charged to harm SMEs and consumers and financial support of one hundred million USD for SMEs. Recognizing its intrinsic efficiency, many expect consent order to be utilized more frequently in the future.

Most currently, debates over the case handling procedures at the KFTC and the appeal system against KFTC decisions have emerged as a hot topic. Many experts and companies are asking for the introduction of more sophisticated procedures for both investigation and adjudication at the KFTC, arguing that the current procedures do not guarantee full opportunities for self-defense. In addition, the current exclusive jurisdiction of the Seoul High Court for appeals against KFTC decisions is under debate, due to criticism that antitrust appeals should not be an exception when it is a general rule that appeals against government agency actions go to courts of first instance. The criticism over KFTC procedures is expected to function as pressure to make KFTC procedures more similar to judicial procedures. However, it is also recognized that there are certain limitations in improving this issue while the KFTC is obligated to process thousands of complaints every year that is a clear overload.

With regard to criminal enforcement, the exclusive authority of the KFTC to make referrals to the prosecutor's office for criminal accusation was taken away due to the concerns over inactive enforcement. In addition to the KFTC, the Public Procurement Service, the Small and Medium-sized Business Administration, and the Bureau of Audit and Inspection were also granted an authority to request criminal referrals. While the amendment is expected to check the authority of the KFTC and invigorate criminal enforcement, there also exist concerns that it may cause over-deterrence because even minor violations of the law like unfair trade practices could, in theory, be criminally prosecuted. It is left to be seen how actively this new measure will be utilized. Despite these changes, for effective enforcement of the KFTC's leniency program, leniency applicants are provided with an exemption to criminal enforcement.

INTERNATIONAL COOPERATION

The KFTC has attached much importance to international cooperation. The KFTC has entered into MOUs with more than fifteen competition authorities as of present; some of the recent ones include China, Indonesia, Brazil and Japan. It is understood that KFTC's cooperation with antitrust authorities of U.S., European Commission, and China is significant and increasing in frequency. The KFTC has also been actively involved in negotiating competition chapters in the free trade agreements with Turkey, Columbia, Australia, and Canada while participating in international organizations, such as the OECD and ICN. Its recent efforts to share its enforcement experience with China and other Asian countries through expert dispatch programs and Knowledge Sharing Program is also worth noting.

CONCLUSION

Korean antitrust law enforcement has been well known for its sincere efforts to realize active market competition in a culture and economy that respects government policy leadership and Chaebols' efficiency. However, recent changes of administration and economic difficulties asked for significant changes in the competition policy area to support SMEs and help boost a "creative economy." It led to emphasis on the enforcement of unfair trade practices to protect SMEs and regulation over abuse of IPRs. Enforcement of traditional antitrust laws, especially attention to the regulation over abuse of market dominance, has been weakened as a cost. At the same time, the KFTC's role of competition advocacy to ease market concentration and make general economic policies more competition-oriented has become relaxed, too, to go along with government policy to revive economy. It is to be seen whether such changes would prove successful or not but under difficult situation of bi-polarization, it should not be an easy job.

In any event, even after such problems described above, it can be said that Korean antitrust policy remains generally very active in building sound market competition. The KFTC keeps pushing to regulate cartels and anti-competitive mergers. Careful monitoring of IPR licensing practices is taking place. The KFTC's role in international policy leadership, especially in Northeast Asia, is another aspect to be noted. Private enforcement of cartel prohibition began to work.

The remainder of the year of 2014 is meaningful in that we will be able to see whether the policy changes in the last year result in success in line with the new Korean economy.

Singapore Joins Global Fight Against International Cartels

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On May 27, 2014, the Competition Commission of Singapore ("**CCS**") issued an infringement decision (the "**Infringement Decision**") against four Japanese ball bearings manufacturers and their Singapore subsidiaries for contravening Section 34 of the Competition Act by engaging in anticompetitive agreements and unlawful exchange of pricing information for ball and roller bearings sold to customers in Singapore. The four Japanese parent companies and their respective Singapore subsidiaries were found to be jointly and severally liable for the infringement. The CCS commenced its investigations into the alleged anticompetitive conduct in December 2011 after receiving an application for immunity under the CCS's leniency program from one of the companies involved in the cartel. Following its investigations, the CCS found that representatives of those four Japanese companies and their Singapore subsidiaries, which were competitors, met regularly in Japan and Singapore from 1980 until 2011. During those meetings, these representatives exchanged commercially sensitive information as well as discussed and agreed on their sales prices for ball bearings sold to their respective customers in Singapore.

This is the first time that the CCS has exercised the extra-territorial reach of its powers under the Act against an international cartel. The CCS imposed financial penalties totaling S$9,306,977 (US$7.4 million) on the companies involved in the Infringement Decision – this is the highest amount of financial penalty imposed by the CCS in a single infringement decision thus far, as the CCS approaches its 10th anniversary. No financial penalty was imposed on JTEKT Corporation and its Singapore subsidiary, Koyo Singapore Bearing (Pte) Ltd, which were granted immunity under the CCS's leniency program.

The Infringement Decision signals the CCS's intent to combat international cartels that have an anticompetitive impact in the Singapore market. This case demonstrated the role of the CCS's leniency program in that fight. As cartels are usually secretive and difficult to detect, it can be challenging for competition authorities to gather sufficient evidence that will allow them to sanction the cartel participants. At the same time, the participants may be deterred from coming forward to whistle-blow on the cartel because of the risk of incurring, large financial penalties, unless there is some form of immunity or reduction in penalties.

Over the years, competition authorities throughout the world, including in the EU and the US, have sought to encourage cartel participants to implicate their cartel members and thereby destabilize cartels through the use of a leniency program. Given that leniency programs in other jurisdictions have proven to be effective in

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incentivizing cartel participants to report cartel activity, the CCS has adopted a similar program as part of its enforcement strategy. As at end of third quarter 2013, the CCS already has more than 18 leniency applications, a number expected to increase.

In addition, the CCS has a leniency plus program, which encourages cartel members under investigation to report their involvement in another cartel activity in return for reduced financial penalties for their first cartel activity. For example, a company may be involved in cartel activity in Market A and Market B. If this company is already cooperating with the CCS's investigation into Market A, and is interested in seeking leniency for its cartel activity in Market B, it may obtain an additional reduction in financial penalties for its involvement in the Market A cartel by cooperating with the CCS in the investigation into Market B. This is in addition to qualifying for total immunity from financial penalties in relation to Market B.

Under Section 69(4) of the Competition Act, an undertaking that has intentionally or negligently infringed the Act's prohibitions may be subject to a financial penalty of up to 10 percent of its business turnover for each year of infringement (up to a maximum of three years). Notwithstanding, the CCS's leniency program grants partial or total immunity from financial penalties to a participating undertaking that (i) provides the CCS with all the information, documents and evidence available to it regarding the cartel activity; (ii) maintains continuous and complete cooperation throughout the CCS's investigation and until the conclusion of any action by the CCS; and (iii) refrains from further participation in the cartel activity from the time of disclosure of the cartel activity to the CCS (except as may be directed by the CCS). In addition, the cartel member must not have initiated the cartel, and should not have taken any steps to coerce another into participating in the cartel activity.

A cartel member who is the first to come forward to provide information on the cartel may be granted total immunity from financial penalties if the above conditions are satisfied. Other cartel members who apply for leniency after the first applicant may have their amount of financial penalty reduced by up to 50 percent. Such partial or total immunity from financial penalties can provide a significant incentive to whistle-blow on the cartel activity, particularly if the business turnovers of the companies involved in that cartel are high, as is the case with the Infringement Decision. In fact, three out of the four companies that participated in the cartel had applied for leniency, with the first applicant being granted full immunity whilst the other two applicants were granted a reduction in their fines.

To complement its leniency program, the CCS also has in place a financial reward scheme, where it offers rewards of up to S$120,000 (US$96,000) for whistle-blowers who provide significant and reliable information relating to competition law infringements. Such whistle-blowers may be eligible for financial rewards upon the issuance of an infringement decision by the CCS. The CCS has worked to keep the identity of the whistle-blower strictly confidential, as well as any information that may lead to his or her identification. Although there have not been any reported instances of the financial reward scheme being utilized thus far, such a scheme may aid the CCS in its enforcement actions, possibly in cases of whistle-blowing by ex-employees.

Some commentators have observed that it is imperative for the CCS to make the prosecution of international cartels an enforcement priority. The handful of infringement decisions issued by CCS thus far has involved small and medium enterprises, and the fines imposed have been relatively small. By imposing larger fines against multinational corporations involved in international cartels, the CCS hopes to signal a strong deterrence against anticompetitive conduct by the business community operating in Singapore and beyond.

Finally, it is noteworthy that on April 1, 2014, the CCS issued a proposed infringement decision against 11 freight forwarding companies and their Singapore subsidiaries. The CCS contended that those freight forwarding companies have infringed Section 34 of the Act by collectively fixing certain fees and surcharges, and exchanging price and customer information in relation to the provision of air freight forwarding services for shipments from Japan to Singapore. Similar to the above Infringement Decision, the CCS commenced investigations after receiving an application for immunity under the CCS' sleniency program from one of the companies involved in the alleged cartel. It remains to be seen whether the leniency applicant is successful in obtaining immunity or a reduction of fines if the case is ultimately proven against those companies. If so, it will be the second occasion that the CCS would have successfully relied on its leniency program to combat international cartels.

Trade Associations In Asia: A Predictable Focus Of The Authorities

Mark Jephcott

Peggy Leung[1]

INTRODUCTION

Trade and industry associations[2] may be formed by businesses for legitimate reasons that enhance competition: small businesses may find increased bargaining power when negotiating as part of a trade association, and an association may develop and enforce trade standards and best practices. However, such associations may also provide a forum for industry players to conduct themselves in potentially anticompetitive ways. For example, businesses in an industry association may collectively decide to set prices or exchange commercially sensitive information.

It is perhaps because of the proliferation of trade associations in Asia, and their propensity to be used as a vehicle for anticompetitive behavior, that trade associations have been an enforcement focus of antitrust authorities in Asia, particularly in China, in 2013. While price-setting has been the main condemned activity of anticompetitive behavior in trade associations, other, more subtle and controversial practices have been in the spotlight in jurisdictions with more mature competition law regimes.

PRICE-SETTING – ANTICOMPETITIVE BEHAVIOR THAT IS EASIER TO DETECT

In many jurisdictions, particularly those with newer competition law regimes, price-fixing behavior in trade associations features more heavily in investigations and actions by antitrust authorities. As price-setting activities tend to be relatively easy to detect and enforce against, they are frequently the first port of call for enforcement by the antitrust agencies.

CHINA – ANTICOMPETITIVE BEHAVIOR IN PREVALENCE OF TRADE ASSOCIATIONS

Many of China's trade associations were formed with regulatory or administrative duties in addition to the advancement of interests of the relevant industry, the commonly understood purpose of a trade association.

1 Herbert Smith Freehills.

2 This article will use the term "trade association" and "industry association" interchangeably to mean any association or body formed by businesses in the same sector or industry: the term also includes professional associations.

Given their quasi-governmental genesis, Chinese trade associations appear to be able to exert a greater influence over the market competition than their counterparts in mature market economies, and therefore they can detect and punish deviations from potential anticompetitive behavior more easily.[3] Anticompetitive practices are also sometimes expressed in regulatory language, such as "self-regulatory" or "self-discipline."

It is perhaps unsurprising, therefore, that trade associations have been featured in a number of investigations by antitrust authorities in China; out of 17 investigations for non-price related anticompetitive behavior published by the State Administration for Industry and Commerce as at November 2012, 16 were reportedly related to trade association activities. Although there are no similar figures for investigations into price-related violations of China's Anti-Monopoly Law ("AML") by the National Development and Reform Council ("NDRC"), 2013 saw enforcement actions by the NDRC and its local arms against a gold and jewelry trade association in Shanghai, several tourist associations in Yunnan province and an insurance "self-regulation" association in Henan province, all involving price-fixing practices.

Trade associations have also been in the spotlight for private antitrust litigation. In November 2013, a local seafood industry association in Beijing had anticompetitive provisions in its association manual struck down after a local seafood merchant took the association to court. In this case two provisions in the manual stated explicitly that members were prohibited from competing with each other on prices for scallops or from selling them to non-members of the association, with penalties for deviation and rewards for informing on non-compliance. The Beijing Second Intermediate People's Court held that the provisions violated the AML and declared them invalid. The lawsuit was the first reported private litigation case against a trade association in China, and the first case, after the Supreme People's Court published guidelines on civil disputes relating to monopolistic conduct in May 2012, in which "articles of association in violation of the AML" had been listed as a possible cause of civil action against trade associations.[4]

OUTSIDE CHINA – SOME PRICE-SETTING THROUGH TRADE ASSOCIATIONS, SOME OTHER TYPES OF CARTELS

Unlike China, most jurisdictions in Asia do not have many trade associations that can trace their roots back into government or regulatory functions. As such, the trade associations in these jurisdictions do not seem to be as prevalent or powerful as their Chinese counterparts. While some trade associations may be formed by legislation or government regulations, some of the trade associations are formed by businesses' initiatives. However, such trade associations seem just as susceptible to being used by some businesses as a means to promulgate anticompetitive conduct.

Some Asian jurisdictions have seen price-fixing activities by trade associations. In Singapore, for example, a group called the Association of Modeling Industry Professionals collectively raised prices for hiring models; al-

3 Please see more details on trade associations in China in the CPI article "Trade Associations and Private Antitrust Litigation in China" by Hao Qian on 16 April 2013 https://www.competitionpolicyinternational.com/trade-associations-and-private-antitrust-litigation-in-china/

4 http://www.chinacourt.org/law/detail/2012/05/id/145752.shtml

though an appeal in April 2013 saw the fines of some modeling agencies reduced, the Competition Commission of Singapore asserted that the association was merely a "front" for its members, and were engaged in price-fixing more than in fighting for better terms for local models.

In Malaysia, professional associations have come under scrutiny. In August 2013 the Malaysian Competition Commission (MyCC) published a report on price-setting behavior by professional bodies in 34 sectors. It found that, although many professional associations were authorized by law to set price scales for their members, some professional bodies in five sectors (namely company secretaries, arbitrators, mediators, landscape architects and dental practitioners) had set fee scales when in fact they had no authorization to do so. The MyCC noted that the prohibition of horizontal agreements under Malaysia's Competition Act applied to all commercial activities, including professional services, and that any price-setting by professional bodies without the requisite legal power or an exemption is prohibited under the Competition Act.

In other jurisdictions with comparatively newer competition law regimes, businesses have engaged in price-setting activities without forming a trade association; in these jurisdictions collusion and price-fixing between businesses seems more common than those carried out under the umbrella of a trade associations. Indonesia, for example, has seen alleged "cartelization" of many agricultural products in 2013, including garlic, beef, chicken, soybeans, rice and eggs, according to Indonesian antitrust authorities; investigations are planned or underway in several of those products.

MORE CONTROVERSIAL BEHAVIOR – INFORMATION EXCHANGES

In jurisdictions with more mature competition law regimes, trade associations have appeared to engage in potentially anticompetitive conduct that is more controversial than price fixing – probably because there is a greater awareness among businesses that price-setting is a blatant infringement of the relevant antitrust law, or because the relevant regulator has already prosecuted price-fixing cases, which are "easy-kills" for regulators overseeing incumbent regimes. Trade associations in these jurisdictions may then need to be aware of other activities that may also be regarded as anticompetitive, such as sharing business information. For the regulators, these practices may be more difficult to detect and take action against, as clear evidence is often lacking in such cases or their effects on competition may be harder to prove.

SOUTH KOREA – EXCHANGE OF INFORMATION WITHIN TRADE ASSOCIATIONS

In October 2013, BMW Korea, Mercedes-Benz Korea and the Korean Automobile Importers and Distributors Association faced allegations at a parliamentary inquiry that, through events they called "workshops," they exchanged sales information. The parties denied that they exchanged information on sales strategies or know-how, instead claiming that only information on "events schedules" was shared to avoid clashes between events.

Similarly, when some doctors of the Association of Korean Medicine were accused of exchanging information about prices and services on an online, doctors-only social club in August 2013, the Korean Fair Trade Commission was of the opinion that the doctors shared the information as individuals, rather as a group, and that the information exchanges on the club did not appear to be collaborative action by the association.

Information exchanges within trade associations appear to be difficult to identify as they often take place in informal settings and orally, and harder still to take action against. What may look like an exchange of commercially sensitive information between businesses in a trade association might be claimed to be an innocuous exchange of technical schedules or best practices. There is also a debate (at least in Asia) as to where the line is between a perfectly legitimate conservation between industry players and an anticompetitive information exchange, and whether information exchange can be an object infringement without the burden on the regulator to prove effects. Consequently, antitrust actions against these practices appear to be more rare in Asia (as compared to, for instance, the EU).

CONCLUSION

Trade associations are currently, and are likely to remain, a key focus of the antitrust enforcement agencies in Asia. As competition law regimes mature and develop in jurisdictions across Asia, cartels and other "classic" anticompetitive behavior, such as bid-rigging by trade associations, are expected to be exposed by antitrust regulators, and trade associations may come under increased scrutiny by regulators; however, after the "easy targets" like price-fixing have been pursued by antitrust authorities, other anticompetitive activities conducted via trade associations will become harder to detect and prosecute.

How Chinese Antitrust Law Has Affected the Business Operations in China: Perspective of Life Science Industry

Jet Deng

Ken Dai[1]

I. INTRODUCTION

China's market of life science is growing at more than 20 percent annually, and is expected to continue at that pace for the next decade. By 2020, the market will be worth an approximated USD 900 billion market, up from USD 108 billion in 2005. With the forthcoming surge of the aging population in China, a new round of urbanization, better availability of healthcare, and the increased expenditure on healthcare by the government, the continuous boom of the life science sector will be positively expected to grow rapidly. Such rapid growth is a magnet for global life science enterprises. A number of multinational companies have made expansions within China in the last few years, whether by mergers and acquisitions or by the establishment of a joint venture. For example, in early 2013, Catalent Pharma Solutions announced two joint ventures in China for its Softgel Technologies and Clinical Supply Solutions businesses. Further, in the midst of 2012, Johnson and Johnson acquired Guangzhou Bioseal Biotechnology Co., Ltd. for the purpose of business expansion in China.

Though the market of life science is experiencing rapid growth and is sufficiently attractive, the significant legal challenges do exist at the same time. In addition to the traditional attention given to legal risks pertaining to anti-commercial bribery, antitrust legal issues have become more and more important for life science companies, an effect that has had great impact on their business operations such as distribution agreements and joint research and development with competitors. Just recently, the National Development and Reform Commission ("**NDRC**"), one of the enforcement authorities under the PRC Anti-monopoly Law ("**AML**") has indicated that the industry of pharmaceuticals has fallen into its scope of top targeted sectors. In addition, the Ministry of Commerce in China ("**MOFCOM**"), in charge of merger control under the AML, conditionally cleared the acquisition of Gambro by Baxter, which demonstrated that the merger review had essential effects on the cross-border M&A transaction, whether on timeframe or on the outcome. As such, in order to share with the growing market of life science while to avoid running afoul of the AML, one should pay special attention to the active enforcement of the AML in China, thus ensuring the business activities compliant with the AML and incorporating such legal requirement into its commercial arrangement.

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To address the antitrust concerns currently surrounding the business operations of life science companies in China, this article will focus on the following aspects: (1) merger control; (2) price monopoly; (3) non-price monopolistic conduct; (4) private antitrust litigation; and (5) abuse of administrative powers to restrict or eliminate competition.

II. MERGER CONTROL

(A) Understanding MOFCOM

In China, MOFCOM is the sole agency responsible for conducting the antitrust review of concentration of undertakings. Within MOFCOM, the Anti-Monopoly Bureau ("AMB") enforces the provisions of merger control under the AML; currently there are seven divisions, namely Division of Office, Division of Competition Policy, Division of Consultation, Division of Law, Division of Economy, Division of Supervision & Enforcement, and Division of Coordination for the Anti-monopoly Commission.[2] With slightly more than 30 personnel in total as opposed to its burdensome workload of reviewing hundreds of cases each year, MOFCOM is quite limited in its working staff. Such insufficiency of human resources has continuously been a significant barrier to working more effectively on the merger review process.

(B) Jurisdiction

Generally, according to AML and practices by MOFCOM so far, whether a specific transaction is subject to notification before MOFCOM will depend on whether the two conditions are satisfied: (1) the transaction falls into the scope of "concentration of undertakings" under AML; and (2) the turnover of the undertakings concerned to the transaction meet threshold trigger.

(1) Categories of Concentration of Undertakings

Pursuant to AML and the current practice MOFCOM, normally the M&A transaction (whether share deal or asset deal) is qualified as a concentration of undertakings. In addition, acquisition of control or the ability to exert decisive influence over another undertaking by contract or other means will fall into the scope as well. In practice, MOFCOM will determine whether a transaction is qualified concentration of undertaking will focus on whether there is change of control of undertaking on a lasting basis, which is similar the approach in the EU. MOFCOM largely refers to the notion of change of control adhering to the international competition practices, mainly concentrating on the elements of the influence over management and operation decision making of an undertaking. As such, even a minority investment in an undertaking while having influence on the commercial

2 Under AML, there is special agency called Anti-monopoly Commission (the "AMC"), which is be responsible for organizing, coordinating and guiding anti-monopoly work and exercises certain powers, including without limitation researching and drafting relevant competition policies, and arranging for the investigation and assessment of the overall status of competition in the market and issuing assessment reports. Currently, the AMC is headed by Wang Yang, one of China's vice premiers, who is in charge of trade and investment policies. The deputies of the AMC are officials from MOFCOM, NDRC, and SAIC. The AMC is overseeing the three enforcement authorities and is operating from a separate working office which is located within MOFCOM and headed by a vice minister of MOFCOM.

strategic decision whether through the level of board of director or other means, will be regarded as concentration of undertakings, For example, the acquisition of not more than a 30 percent stake in Hong Kong Lijun International Co., Ltd. by Sichuan Kelun Pharmaceutical Co., Ltd. fell into the scope of undertaking of concentration and was notified before MOFCOM.

Further, although there is no explicit provision involving the establishment of a JV by two (or even more) undertakings under the AML, it is generally attributed by MOFCOM to the regime of merger control in practice. Until December 10, 2013, MOFCOM has issued a total of three conditional clearance decisions pertain to the JV establishment, despite none in life science sector. But it has been reported that most of the JV transactions involving the multinational companies in this industry have secured antitrust clearance from MOFCOM. For illustration, the establishment of a joint venture between and by Pfizer and Zhejiang Hisun Pharmaceuticals was notified before MOFCOM and eventually was approved unconditionally. Moreover, it should be noted that currently MOFCOM does not distinguish the concept of a full-functional JV, which is the only kind of JV subject to notification in EU.

(2) Threshold

AML and ***the*** *Provisions of the State Council on Notification Standards of Concentration of Undertakings* (**"Threshold Provisions"**) set out the notification turnover criteria.[3]Under that threshold, most of the transactions involving multinational companies will be required to conduct the process of merger review and to secure the antitrust clearance before closing.

(C) Timeframe

Under the AML, notification is required prior the implementation of the transaction. Until MOFCOM grants its approval, parties to the transaction should be very careful to avoid taking certain steps for the implementation of the transaction, which may be considered gun-jumping. Similar to the competition practice in EU or the US, there is also a pre-notification consultation mechanism in China. Undertakings can contact with MOFCOM on specific issues prior to notification.

In accordance with AML, the review process of a concentration of undertakings includes two phases: (a) phase I: preliminary review, when MOFCOM has an initial period of 30 calendar days to undertake a first-stage review upon the official acceptance of the transaction; (b) phase II: further review, which lasts 90 calendar days and can be extended if the review is not completed yet. MOFCOM has the authority to extend this stage for the maximum of 60 calendar days upon the application by parties to the concentration or at its own discretion.

3 A concentration of undertakingsshall be subject to notification upon satisfying one of the following thresholds:(a) the combined global turnover of all undertakings concerned in the last fiscal year exceeding RMB 10 billion (about USD 1.6 billion), and the China-wide turnover of at least two undertakings respectively exceeding RMB 400 million(about USD 65 million) during the last fiscal year; or (b) the combined China-wide turnover of all undertakings concerned in the last fiscal year exceeding RMB 2 billion (about USD 327 million), and the China-wide turnover of at least two undertakings respectively exceeding RMB 400 million (about USD 65 million)during the last fiscal year.

It is noteworthy that China also differs from practices of the EU in that the start-up of further review in China does not necessarily imply serious competition concerns on the concentration.

At present, MOFCOM officially accepts the notification only where it regards the materials complete, which might make the preparation and supplemental of the materials last for a number of several months. In Baxter's acquisition of Gambro, notification materials were officially accepted on March 12, 2013, more than two month after they were submitted to MOFCOM on December 31, 2012.

In addition, a few recent conditional clearance decisions issued by MOFCOM indicate that MOFCOM may require parties to withdraw notification and make a new notification to further extend the time limitation of review. This trend makes the duration of review even more unpredictable. So far, a new notification prolongs review by a range of 3 to 6 months respectively in these cases. This will definitely have great impact the timeframe for M&A transactions, in particular the cross-border deals.

Further, as mentioned above, the lack of sufficient staff plays a negative role in such prolonged review process. Finally, according to the AML, during the procedure of merger review MOFCOM is required to consult on the opinions from other competent ministries (such as the NDRC and Ministry of Industry and Information Technology, as the case may be), which also consumes sometime of the process.

In short, though the capacity building of MOFCOM is positively expected and its experience is increasing, the time required to secure the antitrust clearance is still comparatively time-consuming, which will continuously have an essential impact on M&A transactions.

(D) Substantive Test

According to the AML, when appraising whether a transaction has the effect of eliminating or restricting competition MOFCOM is authorized to consider a wide range of factors, among which market share of the undertakings concerned, HHI index and market entry of the relevant market are primary factors that MOFCOM will weigh most. MOFCOM has also issued *the Interim Provisions on Assessment of the Impact of Concentration of Undertakings on Competition*, which became effective on September 6, 2011 to offer guidance in this regard.

Based on conditional clearance decisions issued by MOFCOM so far, it is noticed that some analysis methods similar to other antitrust jurisdictions are frequently adopted, including "unilateral effect," "coordinated effect," "foreclosure effect" and "leveraging effect," For instance, In Baxter's acquisition of Gambro, MOFCOM reasoned that the proposed transaction would give the merged entity high market share in the relevant market, to raise unilateral effect consequently. After the transaction, the coordinated effect would also be compounded since Baxter and another company Nipro, two major competitors in a relevant market, had executed OEM agreement sharing competitive sensitive information such as costs and quantities.

For another illustration, in Novartis' acquisition of Alcon, MOFCOM distinguished two concerning relevant markets: ophthalmic anti-inflammatory and anti-infective combination products (**"infectoflam"**), and lens care products. In the infectoflam market, despite Novartis' promise to exit China's market provided in its notification materials, MOFCOM still showed competition concerns of unilateral effect. In the lens care products market, MOFCOM noted that one of Novartis' subsidiaries has in place a distribution agreement with Haichang Contact Lens Co., Ltd ("**Haichang**"), currently the largest manufacturer and supplier of lens care products in China. Therefore the parties would be able to collude on pricing and other issues with Haichang.

In addition, specific features of the life science sector are also taken into account by MOFCOM in its competition assessments. In Baxter's acquisition of Gambro, both CRRT and HD products were deemed markets with entry barriers to a certain extent, due to required intellectual properties and great investment needed to conduct R&D and to establish a distribution system. Similarly, in Pfizer's acquisition of Wyeth, MOFCOM considered that pharmaceutical R&D is characterized by high cost and a long cycle, leading to difficult entry.

Further, with the increasingly sophisticated experience in merger review, MOFCOM may also clear a transaction without conditions while other oversea competition authorities grant conditional clearance. For instance, in Johnson's acquisition of Synthes, though the US agency conditionally cleared this transaction, MOFCOM approved it unconditionally.

In summary, MOFCOM is learning more and more to determine whether the specific concentration of undertakings will raise competition concerns by adopting the international converged practice, such as the application of coordinated effect and unilateral effect. Such practice will guide life science companies to make self-assessments from the AML dimension at an early stage of deal structuring, thus ensuring the proposed transaction will not trigger competition concerns in the Chinese jurisdiction, and if such concerns exist, to prepare the negotiation of restrictive conditions with MOFCOM (discussion below).

(E) Restrictive Conditions (Remedies)

According to AML and *Measures for the Review of Concentration of Undertakings*, MOFCOM may impose three types of restrictive conditions on a transaction: (a) structural remedies, ***i.e.*** requirements that the parties divest specific assets or businesses; (b) behavioral remedies, ***i.e.*** requirement that parties provide the use of the network or essential facilities to other parties, or license key technologies (including patent, know-how and other intellectual properties), or terminate exclusive agreement; (c) combinations of structural and behavioral remedies.

In the life science sector, divesture is often adopted, as the cases of Baxter's acquisition of Gambro and Pfizer's acquisition of Wyeth. In Baxter's acquisition of Gambro, MOFCOM further determined that Baxter must completely terminate its OEM production agreement with Nipro regarding HD products within Chinese territory by March 31, 2016, a supplemental behavioral remedy. Novartis was also ordered to terminate its distribution agreement with Haichang within 12 months after closing the transaction in its acquisition of Alcon. It can be concluded that behavioral remedies are more likely to be imposed when coordinated-effect concern is raised in the parties' cooperation with other major competitors in the relevant market.

In short, similar to other competition and antitrust enforcement agencies, MOFCOM will not outright ban a concentration of undertaking, though it raises serious competition concerns. This practice by MOFCOM allows life science companies to bargain for favorable or acceptable conditions for the green light on specific transaction from MOFCOM.

III. PRICING MONOPOLY

(A) Understanding the NDRC

The NDRC is in charge of pricing monopoly and has established the functional department of Price Supervision and Anti-Monopoly Bureau. The Bureau consists of three divisions for enforcing AML, namely the Division I of Price-related Anti-Monopoly Investigation, Division II of Price-related Anti-Monopoly Investigation, and Division of Competition Policy and International Cooperation. It has reported about 40 people currently within the NDRC for enforcement of AML. In addition, it is noteworthy that at present the local counterparts of the NDRC at the provincial level are authorized to enforce AML within their respective jurisdiction. A number of provinces have established their own bureaus for enforcing AML, such as Jiangsu Province[4] and Guangzhou Province.[5] Such structure of enforcement institution arrangement has empowered NRDC to investigate the pricing monopolistic conducts very broadly within mainland China.

Moreover, on November 4, 2013, the NDRC announced that it will accelerate the establishment of the price complaint platform of "12358." Such a national platform also demonstrates that the NDRC intends to integrate regional resources into a unified, potent enforcement force.

Considering that most of the life science companies conduct business not only in first-tier cities, but also covering the remaining part of mainland China, the rapid growth of capacity building and its enforcement structure do place increasing regulatory challenges on this industry.

(B) Monopoly Agreement

(1) Horizontal Monopoly Agreement

Under AML and the relevant regulation,[6] in terms of horizontal monopoly agreements in relation to price, NDRC enforces the anticompetitive conduct of price-fixing, which is a hardcore restriction in China. Similar to other matured competition and antitrust jurisdictions, the form of such conducts can vary from the direct price-fixing to agreed formula to calculate the price. For instance, in the case of price-fixing in the gold industry, the Shanghai Gold &Jewelry Trade Association and five gold retailers were imposed a fine of RMB10.1 million

4 In July 2013, the Jiangsu Price Bureau established its sub-bureau of anti-monopoly, which performs well.

5 In November 2012, the Guangdong Price Bureau established its sub-bureau of anti-monopoly, which has investigated a few pricing monopoly cases so far.

6 *The Regulations on Anti-Price Monopolies*, promulgated by NDRC on December 29, 2010, became effective on February 1, 2011.

(approximately USD1.63 million). Such undertakings reached the self-implementing rule on the price of gold and platinum in Shanghai, which had fixed the calculation method and calculation formula of the retail price, and fixed price range.

In the meantime, to date, some trade associations are absent of knowledge of the AML and continue the tradition of an operation model, which includes discussion on the price and output in China. Therefore, the NCRC tends to investigate the trade association and thus police the cartel. In that sense, life science companies shall be very cautious in attending any kind of meetings organized by trade association, such as keeping the representative attendants aware of AML knowledge and implications.

(2) Vertical Monopoly Agreement

In terms of a vertical monopoly agreement, NDRC regulates two aspects: (a) fixing resale price, and (b) fixing the minimum resale price ("Minimum RPM"). Particularly, the enforcement of Minimum RPM has been active and even aggressive by the NDRC since the beginning of 2013. Earlier last year, the local counterparts of NDRC fined two well-known PRC domestic alcohol companies, Wuliangye and Moutai, for entering illegal vertical agreements and implementing Minimum RPM, respectively. The total amount of such fines has reached RMB 449 million (about USD 72 million). Further, last August, the NDRC issued a decision to impose fines on a number of baby infant formula manufacturers for conducting Minimum RPM. The total penalties imposed on all companies added up to RMB 670 million (about USD 110 million). In these two cases, the NDRC shed some light on how to determine whether the application of Minimum RPM will amount to contravention of AML, namely focusing on the following aspects: (a) Whether Minimum RPM will eliminate competition between distributors of the same brand (intra-brand competition),(b) whether Minimum RPM will remove inter-brand competition because of its negative effect within the industry, and (c) whether the usage of Minimum RPM will harm the interests of consumers. Though such guidance by the NRDC arguably lacks detailed analyses and remains ambiguous, it at least provides a preliminary analytical framework.

In practice, quite a number of life science companies have contained the Minimum RRM provision in distribution agreement (such as the Johnson case to be discussed below). Such arrangements are facing potential antitrust legal risk in China in light of the continuously active enforcement of Minimum RPM by NRDC. Just recently, it was reported that the NDRC has initiated antitrust investigation against one of well-known global life science company for Minimum RPM.

(C) Abuse of Market Dominant Position

As for abuse of market dominant position pertain to price, NDRC enforces the following:(a) selling products at unfairly high prices or buying products at unfairly low prices, (b) selling products at prices below cost without valid justification, and (c) other abusive conducts in relation price, such refusal to deal, exclusive dealing and discriminatory treatment.[7] The NDRC stipulates the details on such abusive conducts in ***The Regulations on Anti-Price Monopolies***.

7 Article 13, 14, 15 and 16 of *The Regulations on Anti-Price Monopolies*.

Actually, concerning the abuse of market dominance in the sector of life science, NDRC's took its first enforcement action against two PRC domestic companies. In that case, Shandong Weifang Shuntong Pharmaceutical Co., Ltd. ("**Shuntong**") and Weifang Huaxin Medicine Trade Co., Ltd. ("**Huaxin**") were accused of unlawfully controlling the raw material of compound reserpine tablets and increasing its sales price to boost profits. At that time, there were only two domestic producers of promethazine hydrochloride, the major raw material used to make compound reserpine tablets, a high blood pressure medication that is widely used in China. According to the NDRC's statement, Shuntong and Huaxin entered into contracts in June 2011 with the only two producers, prohibiting the producers from selling the compound to third parties without the approval of Shuntong and Huaxin. After gaining control over the source of the raw material, the two companies then increased its sales price from less than RMB 200 per kilogram to as much as RMB 300 to 1,350 per kilogram. Many reserpine manufacturers were forced to halt production and could only supply medical institutions from their remaining inventories. Given the two companies' malicious monopolistic conduct, NDRC has ordered them to stop illegal acts immediately and imposed a fine of RMB 6,877,000 (about USD 1 million, including confiscated gains of RMB 377,000 and a penalty of RMB 6,500,000) on Shuntong, and a fine of RMB 152,600 (about USD 25 thousand, including confiscated gains of RMB 52,600 and a penalty of RMB 100,000) on Huaxin.

It is understood that some life science companies might hold a significant part of the market share in a niche market. In that circumstance, such undertakings shall be very careful on reviewing its current commercial arrangements, including, without limitation, price aspects of distribution agreement, rebate policy and discriminatory price, since such business operations will be likely to fall afoul of AML with respect to abuse of market dominant position.

IV NON-PRICING MONOPOLISTIC CONDUCTS

(A) Understanding SAIC

State Administration for Industry & Commerce ("**SAIC**")is responsible for non- price-related monopolistic conducts in China, with its functional unit of Anti-monopoly and Anti-unfair Competition Enforcement Bureau. SAIC has been devoted to accelerating enforcement lately. On July 29, 2013, the online platform for antitrust cases handled by SAIC was put into operation, issuing all 12 cases with their detailed decisions that have been investigated and closed by SAIC since the effectiveness of AML. During the past five years, SAIC authorized counterparties in many provinces to handle a total of 23 antitrust cases. In contrast with the NDRC, the SAIC takes the form of specific authorization, that is, to authorize provincial counterparties on a case-by-case basis.

The spotlight on SAIC also derives from its draft *Provisions on Prohibiting Abusing Intellectual Property Rights to Exclude or Restrict Competition* under deliberation. Now the draft rule is updated with the 7th version, which distinguishes notable changes compared with the 6th. Its promulgation is highly expected to make up for the overlap field of antitrust and intellectual property, a sheer blank in China so far.

(B) Monopoly Agreement

In addition to pricing horizontal monopoly agreements regulated by the NDRC, other kinds of anticompetitive practices fall into the authority of the SAIC, such as market allocation and joint boycott. In ***the Regulations***

of the Industry and Commerce Administration Authorities on the Prohibition of Monopoly Agreement Behaviors promulgated by the SAIC, every type is detailed specifically. From the SAIC enforcement precedents released on its website, it can be readily concluded that market allocation is a primary concern and many horizontal monopoly agreements are reached via industrial association.

Regarding vertical monopoly agreements, so far neither any specific guidance nor enforcement decision was released by the SAIC. Such a situation does create the uncertainty for life science companies since there are quite a lot of commercial arrangements in distribution agreement that will be likely fall into the radar of the AML, including but not limited to territorial allocation, customer allocation, exclusive dealing or supply, non-compete clause and more. The best practice for managing such potential legal risk is to make the self-assessment on a case-by-case basis in accordance with the AML jointly by reference to the best practice in other jurisdictions.

(C) Abuse of Market Dominant Position

Non-pricing abusive conducts under AML include: refusal to deal, exclusive dealing, tying, imposing unreasonable terms and discriminatory dealing, all with the precondition that no justification can be acceptable. Likewise, ***the Regulations of the Industry and Commerce Administration Authorities on the Prohibition of Abuse of Dominant Market Positions*** by SAIC as well details every prohibition and provides for available justifications. So far, no case released has been enforced by SAIC in life science sector.

V. PRIVATE ANTITRUST LITIGATION

Similar to the US, in China, more and more undertakings have begun to use the AML to resolve the commercial disputes, thus bargaining for favorable compensation or protecting commercial interests. Such a trend has been accelerated by the effectiveness of *Provisions on Issues Concerning the Application of Law in relation to Trials of Monopoly Civil Dispute Cases*(the **"Judicial Interpretation"**) on June 1, 2011. The private enforcement of AML by Chinese people's courts is expected to active in the coming years.

Minimum RPM: Rainbow vs. Johnson & Johnson

The first private antitrust action, *Rainbow vs. Johnson & Johnson* (**"J&J Case")**, in the sector of life science is in relation to the Minimum RPM. This case also arose from the dispute between supplier and distributor. In 2010 the plaintiff Rainbow sued J&J for imposing a Minimum RPM in their distribution agreement and sought for reimbursement. The allegations were dismissed by Shanghai First Intermediate People's Court because Rainbow couldn't sufficiently prove that the Minimum RPM practice in agreements had caused a restrictive or eliminative effect on competition. This decision entailed the adoption of rule of reason. As opposed to per se illegal doctrine which dooms Minimum RPM itself illicit, rule of reason means to determine whether a case concerning RPM is illegal on the basis of analyzing its impact on competitiveness.

<u>Affirmation on applying rule of reason to Minimum RPM</u>: Although Shanghai Higher People's Court (the**"Court"**) gave the reverse decision, it reconfirmed applying rule of reason to Minimum RPM. It reasoned

that, according to the wording of AML, it is indispensable for horizontal monopoly agreements to have eliminative or restrictive impact on competition. Since vertical monopoly agreement harms competition less than horizontal one, it is reasonable to define its violation more strictly. Thus eliminative or restrictive impact on competition is also a necessary prerequisite of vertical monopoly agreement. From this perspective, rule of reason was affirmed herein.

Burden of Proof: The Court still advocated that the burden of proof concerning RPM lies in the plaintiff. The Judicial Interpretation does say that in horizontal monopoly agreement disputes, the defendant is burdened to prove that horizontal monopoly agreement does not eliminate or restrict competition. However, the reversal of burden of proof concerning horizontal monopoly agreement cannot be extended to vertical monopoly agreement.

Laying out Analytical Framework: Furthermore, unlike the view from NDRC focusing on the effect of intra-brand and inter-brand competition, and the harm on consumers' interests, and the Court has provided four key factors in evaluating competitive effects of Minimum RPM, including: (a) whether the relevant market is fully competitive; (b) whether the defendant has a strong market position; (c) the motivation of the defendant conducting Minimum RPM; and (d) the actual effects on competition of Minimum RPM.

This case typically sheds light on Chinese courts' attitudes towards Minimum RPM, that is, the rule of reason. It is not yet expressly settled whether the adoption will be generalized to other types of vertical monopoly agreements by courts. For life science companies, it is useful to make reference to this case to decide whether Minimum RPM can be retained at the distribution agreement without contravening AML.

Huawei vs. InterDigital Group

Another latest private antitrust case is also noteworthy to address, though it is not relating to the life science sector. On October 28, 2013, Guangdong Higher People's Court (Higher Court) gave the final adjudication, favoring the claims of Huawei Technologies Co., Ltd. (Huawei) against InterDigital Group (IDC), who is the holder of the 3G essential patent. It is the first case in China where an essential patent is involved. IDC was affirmed to have abused its market dominant position and shall compensate Huawei RMB 20,000,000.[8] Huawei initiated the lawsuit as a defense against patent infringement litigation brought by IDC in the US, and seemed to succeed in at least a partial counterattack.

Since some of foreign life science companies have entered into or will conclude transactions on patent licensing with certain commercial terms (such as the exclusive licensing and comparative high royalty in China), such arrangements might face antitrust risk in light of the AML, in particular where there is any dispute arising from the performance of such an agreement. Antitrust review and assessment of such transactions become essential in China.

8 See Ye Ruosi, Zhu Jianjun & Chen Wenquan, "Determination of Whether Abuse of Dominance by SEP Owners Constitutes Monopoly: Comments on the Antitrust Lawsuit *Huawei v. InterDigital*," Electronics Intellectual Property, vol.3, 2013

VI. ABUSE OF ADMINISTRATIVE POWERS TO RESTRICT OR ELIMINATE COMPETITION

Traditionally, where foreign companies enter into the Chinese market, they bargain or secure the attractive commitments (preferential exclusive granting of access or conclusion of long-term services agreement) from local governments. Such commitments make foreign investors more comfortable or confident during the process of the subsequent business operation locally, even sometime by the form of letter of covenant. With the enactment of the AML, such support from local government shall be dealt with and treated very carefully by foreign life science companies.

Under the AML, there is a special chapter prohibiting the abuse of administrative powers to restrict or eliminate competition in the relevant market, including but not limited to restricting or excluding the external enterprises from entering into local market by setting out threshold. Currently, there is typical case in this field. In 2011, a local government of China's Guangdong province issued an order requiring the use of GPS services of a private company to monitor the transportation of all hazardous goods in that city. The Guangdong Provincial Administration for Industry and Commerce (**"Guangdong AIC"**) investigated after receiving complaints from competitors, and concluded that the specific administrative order constituted an abuse of administrative power under AML. The Guangdong AIC sought the guidance of the SAIC, then made a recommendation to Guangdong's provincial government to correct the abuse. On June 12, 2011 Guangdong's provincial government ruled that the order violated Articles 8 and 32 of the AML (namely, abuse of administrative power to eliminate or restrict competition).

Therefore, in view of the aforesaid case, life science companies are advised to pay careful attention to the commitment or promise from local governments for the purpose of attracting investment. Otherwise, such granting might be invalid or declared revoked due to the contravention of AML.

VII. CONCLUSION AND LOOK AHEAD

Precedents in life science sector are far from enough to provide a clear-cut framework of antitrust enforcement in China. But clues are gaining so that companies can approach cautiously under certain guidance. It is necessary to further stress the instability where antitrust enforcement is directed in China. Therefore, any high-profile case deserves close attention, and additional regulations are very crucial including some pending legislation due to the vague nature of the AML. The only certainty is that antitrust has been, and will be affecting companies' business in China, perhaps to an extent beyond our expectation.

For Chinese enterprises, it is a hard transition period when they need to adapt themselves to the underdeveloped field of antitrust compliance. China and its domestic companies, including state-owned enterprises and private enterprises, have been long under planned economy time without the concept of monopoly, particularly in the life science sector whose development depends mostly on government funding but hardly on market competition. But things are different now. Antitrust enforcement is speeding up in recent years and referring to other matured jurisdictions increasingly. And domestic enterprises are also expanding globally, in the face of intense competition and rigid compliance requirements from other countries.

For foreign companies, situations might be even more unpredictable. Sometimes, it appears that Chinese authorities might take special attitude than their counterparties in other jurisdictions. For example, some transactions subject to merger control are cleared unconditionally in other jurisdictions, while MOFCOM imposes remedies. Under other cases, Chinese authorities seem to adopt a milder attitude, for example towards RPM. Thus foreign companies will have to conduct at least as cautiously as they do in other jurisdictions. In addition, since there are few general principles in China, most cases need to be analyzed on a case-by-case basis. Therefore it's better for multinational companies to adopt China-specific antitrust guidance and employ local consultancy when having branches in China. And despite the declared non-discriminatory enforcement between domestic and foreign companies, it is still sensible for foreign companies to adopt a more prudent code than their domestic peers.

To look forward, life science will be definitely one of antitrust hotspots in China. And with the expected introduction of more special implementing rules (IP and antitrust) and guidance (vertical restraints), life science companies will have more knowledge and understanding of ensuring compliancy with the AML in China. We should pay special attention to the rapid development of private antitrust litigation in China, and the new types of actions that will be likely occur in the coming years, such as litigation concerning reverse payments. In short, enforcement authorities and market subjects are both exploring the path ahead. Conflicts may be inevitable during this period, so interactions and communications make a lot of sense. But what we can finally reap is optimistic. Growing competition will bring China a boom in life science sector, a sector full of innovation and welfare.

COMPETITION POLICY IN ASIA

Essays on Recent Development

2013

Huawei v. InterDigital: China at the Crossroads of Antitrust and Intellectual Property, Competition and Innovation

Michael Han

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SUMMARY

The recent rulings of the Shenzhen Intermediate People's Court and the Guangdong Higher People's Court in ***Huawei v. InterDigital*** addressed several important issues at the crossroads between antitrust law and intellectual property in China in respect of standards essential patents (SEPs).

On the issue of how the holders of standards essential patents can enforce their rights, it appears from this case that the Chinese courts share similar competition concerns with regulators and courts in developed jurisdictions such as the US and EU.

However, a China-specific consideration may impact the courts decisions in relation to SEP cases: the encouragement of indigenous innovation and the government's efforts to help Chinese companies to get around the perceived technology barriers (often in the form of industry standards) set by foreign companies.

BACKGROUND

On December 5, 2011, Huawei filed two complaints[2] before the Shenzhen Intermediate People's Court (the ***Shenzhen Court***) in China, alleging that, by engaging in certain patent practices, InterDigital had (1) abused its dominant market position, contrary to the Anti-Monopoly Law of the People's Republic of China (***AML***), and (2) as an owner of several SEPs for 2G, 3G and 4G telecommunications technologies, had failed to negotiate on fair, reasonable and non-discriminatory (***F/RAND***)[3] terms with regard to licensing those patents.

1 Freshfields Bruckhaus Deringer LLP, Beijing Office.

2 *See* InterDigital's 10-K for the year of 2012, available at http://www.sec.gov/Archives/edgar/data/1405495/000140549513000010/idcc-20121231x10k.htm#sB8CBDEB8939B47C8E810BD0438747BFA.

3 The US uses "reasonable and non-discriminatory" (RAND) while EU uses "fair, reasonable and non-discriminatory" (FRAND), but they basically mean the same thing. we choose the abbreviation "F/RAND" to accommodate both the "RAND" and "FRAND."

The Shenzhen Court delivered its rulings on February 4, 2013. While these are sealed and are therefore not available to third parties, InterDigital's annual report and an article published in an IP law journal by three judges of the Shenzhen Court[4] provide a good summary of the main facts and findings of the Shenzhen Court:

(1) With respect to the abuse of dominance claim, the Shenzhen Court found that InterDigital had abused its dominant market position and thus violated the AML by (i) tying its SEPs with non-SEPs during licensing negotiations[5] and (ii) seeking injunctive relief against Huawei before the United States District Court for the District of Delaware and before the United States International Trade Commission (***ITC***), while still in negotiations with Huawei to force Huawei to accept unreasonable licensing terms including excessive royalties. The court ordered InterDigital to cease its unlawful practices and pay Huawei 20 million CNY (approximately 3.2 million USD) in damages.

(2) As to the F/RAND claim, the Shenzhen Court concluded that InterDigital failed to comply with the F/RAND commitments in relation to its SEPs by (i) commencing injunction proceedings and asking Huawei to pay much higher royalties than those paid by Apple and Samsung and (ii) insisting on Huawei's licensing, to InterDigital, all of its own patents obtained globally on a royalty-free basis. The court determined that the F/RAND royalty rate for the InterDigital SEPs concerned should not exceed 0.019 percent of the actual sales price of each product manufactured by Huawei.

On May 9, 2013, a media report indicated that InterDigital had appealed to the Guangdong Higher People's Court against the above rulings and it has now been reported that the Guangdong Higher People's Court, on October 28, 2013, affirmed most of the rulings of the Shenzhen Court (including the award of CNY 20 million in damages). However, the Guangdong Higher People's Court's ruling with respect to Huawei's tying claims appears to be unclear in the media reports. It did find that the bundled licensing of SEPs of a global scope can be justified on efficiency grounds and that, therefore, this conduct did not violate the AML. But due to the fact that the judgment of the Higher People's Court has not been published, it is currently unclear whether the Court dismissed all of Huawei's claims relating to tying or only some of them.

OBSERVATIONS AND COMMENTS

As a preliminary note, the decisions of both the Shenzhen Court and the Guangdong Higher People's Court have not been disclosed, possibly due to trade secret issues. Thus, most of the following observations are made based on the above-mentioned judges' article on the Shenzhen Court's decision and on media reports.

This case has touched upon a wide range of important issues at the crossroads between antitrust law, competition policy and intellectual property, which also have been discussed heatedly in the US and EU.

4 *See* Ye Ruosi, Zhu Jianjun & Chen Wenquan, Determination of Whether Abuse of Dominance by SEP Owners Constitutes Monopoly: Comments on the Antitrust Lawsuit *Huawei v. InterDigital*, Digital Intellectual Property (2013 No. 3).

5 But the court did not find that InterDigital's bundling of its SEPs for 2G, 3G and 4G technologies or its bundling of its global patents constituted tying.

I. Market definition in relation to technology licensing markets involving SEPs

When evaluating the abuse of dominance issue, the Shenzhen Court determined that the relevant product market should be a collection of the technology licensing market for each single patent essential to the WCDMA, CDMA2000 and TD-SCDMA standards for 3G telecommunications technologies, a decision which the Guangdong Higher People's Court appears to have affirmed. In other words, each of these technology-licensing markets constitutes a separate market in which the SEP owner therefore automatically holds a market share of 100 percent – an undoubtedly dominant market position.[6] In reaching this conclusion, the judges explained in their article that the Shenzhen Court carefully considered the interchangeability between substitute technologies, and highlighted two major characteristics of SEPs: uniqueness and non-substitutability. In particular, in the standard-setting process, once one patent has been adopted as essential to a standard, to conform to the standard, market participants forego opportunities to invent around or adopt substitute technologies, and have to obtain the license to use the SEP for their products as their only and irreplaceable choice. In other words, they become "locked in."[7]

By making it clear that an SEP owner has a 100 per cent market share in the technology licensing market for that SEP, the Chinese Courts have significantly lowered the barriers an antitrust plaintiff will face in order to establish the element of dominance in similar cases in the future.

Similarly, in ***Broadcom v. Qualcomm***,[8] the US Court of Appeals for the Third Circuit noted that in the US, to establish a monopolization claim under Section 2 of the Sherman Act, a plaintiff needs to prove market power in the relevant product market, which can be inferred from dominant market shares and high entry barriers. The court then held that Broadcom adequately alleged that the licensing of Qualcomm's proprietary WCDMA essential technology is a relevant product market, and this essential technology was not interchangeable with other technologies. Adherents to the standard had become locked in. The court seemed to be of the view that a SEP may confer on its owner significant "market power," no matter how the market is defined, as implementing the standard is essential for market entry or continuing stay.

Furthermore, the court shared the same concern as to the "lock in" effect a standard-setting process may have on companies who choose to adhere to the standard and the patent holder's ability to "hold up" them. The court explained:

Industry participants who have invested significant resources developing products and technologies that conform to the standard will find it prohibitively expensive to abandon their investment and switch to another standard. They will have become "locked in" to the standard. In this unique position of bargaining power, the patent holder may be able to extract supra-competitive royalties from the industry participants.

6 Under the AML, a company is presumed to have a dominant market position with a 50 percent market share.

7 This may lead to a superior position of bargaining power held by the SEP holder and may thereby give it an incentive to seek supra-competitive royalties from market participants.

8 *See* Broadcom Corp. v. Qualcomm Inc., 501 F. 3d 297 (3d Cir. 2007).

II. Abuse of dominance in the technology licensing market

To establish an abuse of dominance claim under the AML, it is necessary to establish "abuse" in addition to "dominance." Based on information contained in media reports on the appeal judgment in this case, it appears that the Guangdong Higher People's Court agreed with the Shenzhen Court that, by seeking injunctive relief in the US against Huawei, a willing licensee, with respect to its F/RAND-encumbered SEPs InterDigital violated its F/RAND commitments and that this conduct thereby constituted an abuse.

Notably, injunctive relief can be sought not only in court, but also before the ITC. "Section 337 investigation" is a phrase Chinese companies are becoming more and more familiar with. The ITC "adjudicates allegations of unfair methods of competition and unfair acts involving imported articles under Section 337 of the Tariff Act of 1930."[9] The remedies the ITC can impose in such an investigation can be very severe: exclusion of imported products involved in the case from the US. In the US, despite the possible trend that courts may be more and more skeptical about injunctions as a remedy in patent litigation, the ITC seems to enjoy the reputation of "pro patent."

The holding related to injunctive relief in ***Huawei v. InterDigital*** is similar to the US Federal Trade Commission (***FTC***)'s complaint, filed on January 3, 2013, against Google, which stated that Google, which acquired Motorola Mobility in 2011, reneged on Motorola's commitments to license its SEPs on F/RAND terms, by seeking injunctive relief against willing licensees of those SEPs, and that this allegedly violated Section 5 of the Federal Trade Commission Act. In the accompanying consent order, Google agreed to license its SEPs to competitors on F/RAND terms and not to seek injunctions against them, subject to a few exceptions.[10]

Similarly, on May 6, 2013, the European Commission sent a Statement of Objections to Motorola Mobility,[11] informing the company of its preliminary view that "the company's seeking and enforcing of an injunction against Apple in Germany on the basis of its mobile phone [SEPs]" gave rise to an abuse of a dominant position in violation of EU antitrust laws, "where the company has given a commitment to license those patents on F/RAND terms" and "where [Apple] has shown to be willing to enter into a [F/RAND] license."

Another similar ongoing investigation in the EU is against Samsung. The cause is again the company's pursuit of injunctive relief against Apple. "To remedy these concerns, Samsung has offered to abstain from seeking injunctions for mobile SEPs for a period of five years against any company that agrees to a particular licensing framework," and the European Commission is seeking comments with respect to such commitments.[12]

9 *See* Facts and Trends Regarding USITC Section 337 Investigations, *available at* http://www.usitc.gov/press_room/documents/featured_news/sec337factsupdate.pdf.

10 *See* In the Matter of Motorola Mobility LLC, a Limited Liability Company, and Google Inc., a Corporation (FTC File No. 121 0120), http://ftc.gov/os/caselist/1210120/index.shtm.

11 *See* http://europa.eu/rapid/press-release_IP-13-406_en.htm.

12 *See* http://europa.eu/rapid/press-release_IP-13-971_en.htm.

While the Guangdong Higher People's Court supported the Shenzhen Court's finding that the seeking of injunctive relief by InterDigital, with respect to its SEPs that are subject to F/RAND commitments, is an abuse of its dominant position, the Chinese appellate court's ruling on Huawei's tying claims is unclear at this point. It is reported to have acknowledged that the bundled licensing of SEPs can generate efficiencies and this position is welcome, as it appears to be in line with broader international practice on the treatment of bundled licensing under antitrust law. For instance, the US Supreme Court in the ***Broadcast Music*** case recognized the efficiencies that could be achieved by bundled licensing so long as licenses for each single intellectual property in the bundle would also be available upon request.[13]

III. SEPs and F/RAND commitments

The judges of the Shenzhen Court acknowledged in their article that standardization is important to ensure the interoperability of products or services of different companies and thereby to reduce production costs, protect consumer welfare and promote innovation. They defined the term "SEP" as any patented technology that has to be incorporated into a product in order to implement a certain standard.

In this case, both Huawei and InterDigital are members of the European Telecommunications Standardisation Institute (***ETSI***). Under the ETSI Intellectual Property Rights Policy, when its essential patents relating to a standard are brought to ETSI's attention, InterDigital is obliged to give a written undertaking within 3 months to ETSI stating that it will grant irrevocable licenses of its SEPs on F/RAND terms.[14] Also, InterDigital undertook to license its SEPs on F/RAND terms to other members of ETSI when it joined the organization. Despite this seeming clarity, the meaning of the term "F/RAND (fair, reasonable and non-discriminatory)" is a fact-specific question for the courts. In answering deciding this case, the Chinese Courts looked at two issues: (1) did InterDigital's licensing practices violate its F/RAND commitments? and (2) at what level should the F/RAND royalty rate be set?

Regarding the first question, InterDigital's requirement that Huawei pay significantly (sometimes even 100 times) higher royalty rates than those required of Apple, Samsung and other companies for the same set of patents, even while Huawei's global sales were much less than Apple and Samsung, appeared to the Courts to be prima facie evidence of discriminatory treatment. In addition, the Courts noted that InterDigital had also required Huawei to license back all of its global patents on a royalty-free basis (as of 31 December 2010, Huawei owned 31,869 Chinese patents, 8,892 PCT international patent applications and 8,279 overseas patents). This appears to be much harsher than a grant-back requirement[15] and the Courts appear to have taken the view that this was contrary to fair or reasonable principles.

13 Broadcast Music, Inc. v. Columbia Broadcasting System, Inc., 441 U.S. 1, 21, 24 (1979).

14 ETSI Intellectual Property Rights Policy, Article 6.1, http://www.etsi.org/images/etsi_ipr-policy.pdf.

15 InterDigital's 10-K described this condition as a "grant-back." However, a grant-back condition is to require a patent licensee to license back any technology it develops upon the licensed technology (in other words, any improvements) on a royalty-free basis, which is much narrower than what InterDigital appears to have required in this case.

With respect to the second question, the Shenzhen Court reduced the F/RAND royalty rate for InterDigital's 2G, 3G and 4G Chinese SEPs from 2 percent to up to 0.019 percent of actual sales price of each product manufactured by Huawei, and this was affirmed by the appellate court. InterDigital alleged in its 10-K filing that the Shenzhen Court failed to explain how it had reached this number, and the judges' article did not provide any insights into this calculation either. A source familiar with InterDigital was recently reported to have complained that, according to the decision of the Chinese Courts, if a royalty rate exceeded the lowest rate that had ever been applied, such a royalty rate would be deemed unfair.[16]

Interestingly, on April 25, 2013, a US federal district court in Seattle delivered its opinion in Microsoft v. Motorola, which appears to be the first case in the US in which a court has determined a F/RAND rate.[17] In this decision, following a comprehensive analysis taking into account various factors, the F/RAND rate for the licensing of Motorola's video coding SEP portfolio to Microsoft was set by the court at 0.555 cents per unit, and the F/RAND rates of Motorola's WiFi SEP portfolio were determined as 3.471 cents per unit for Microsoft's Xbox products, and 0.8 cents per unit for all of Microsoft's other products.

IV. Patent assertion by non-practicing entities (NPEs)_

A patent assertion entity (PAE)'s business model is to purchase and hold patents solely to assert or threaten to assert them in court in order to obtain licensing fees from operating companies that are already using the patents in their products.[18] PAE's business activities are now a heated topic in developed jurisdictions, particularly the US, but they are not common in China. On one hand, PAE's activities may help facilitate the functioning of technology markets. Yet on the other hand, they have received criticism for demanding excessive royalties and hindering the business operations of their licensee companies.

In the US, both the Department of Justice, Antitrust Division (***DOJ***) and the FTC have been concerned about PAE activities' impact on competition. In December 2012, the DOJ and FTC jointly held a Patent Assertion Entities Workshop to explore the benefits and harms to both innovation and competition.[19] The workshop noted the following facts: (1) in the US there was 569 patent lawsuits initiated by PAEs in 2006, while the number jumped to 2,544 in 2012 through 1 December; (2) lawsuits initiated by PAEs used to account for 19 perceecnt of all patent litigation in the US in 2006, whereas the percentage grew to 60 percent in 2012 through December 1; and (3) in the US "PAE-generated revenue cost defendants and licensees 29 billion USD, a 400 percent increase from 2005." Upon the collection of a number of public comments, on September 27, 2013, the FTC decided to conduct a study on PAE activities by issuing information requests to approximately 25 PAEs and several other entities.[20] The study will cover ordinary PAEs as well as "other entities asserting patents in the wireless

16 *See* http://app.parr-global.com/intelligence/view/1031134.

17 Microsoft Corp. v. Motorola, Inc., et al., Case No. C10-1823JLR (W.D. Wash., Apr. 25, 2013).

18 The FTC defined the term "patent assertion entities" as firms whose business model primarily focuses on purchasing and asserting patents. *See* http://www.ftc.gov/os/2011/03/110307patentreport.pdf (p.8).

19 *See* http://ftc.gov/opp/workshops/pae/.

20 *See* http://www.ftc.gov/opa/2013/09/paestudy.shtm.

communications sector, including manufacturers and other non-practicing entities and organizations engaged in licensing." InterDigital-like entities, though not PAEs, appear to be also within the Commission's interest of study.

In the current case, although in addition to patent acquisition, InterDigital is active in technology development, its conduct still shares similarities with PAEs.[21] The Chinese judges expressed in their article similar concerns as a US antitrust regulator may have for PAEs. The judges noted that InterDigital's principal business is patent licensing and that it does not manufacture any product. As a result, Huawei was in a weak bargaining position during licensing negotiations because cross-licensing would not be available, and InterDigital could make use of this advantage to extract more favorable contract terms from Huawei. The Shenzhen Court found that InterDigital had tried to exploit this advantage, by insisting on unreasonably high royalties and requesting Huawei to license back its patents on a royalty-free basis, with which the appellate court appeared to have agreed.

Although PAE activities are less common in China than in the US, it seems that the Chinese courts may view these entities as posing a danger to other businesses, especially to domestic companies' indigenous innovation efforts.

V. Damages calculation for abuse of dominance

When bringing the abuse of dominance action, Huawei sought damages as well as injunctive relief. The Shenzhen Court ordered InterDigital to cease its 'excessive pricing' and tying activities and to pay Huawei exactly what it had requested, equaling approximately USD 3.2 million, a very large damages award by the standards of the courts in China. This award was subsequently upheld by the Guangdong Higher People's Court, although it is not clear whether the tying claim was affirmed.

In terms of the calculation of the damages, the judges of the Shenzhen Court stated that neither the plaintiff nor the defendant provided satisfactory evidentiary proof for damages. The Court therefore made its own calculation based on (1) the attorney fees paid by Huawei in both the US and China, (2) the notarization fees paid by Huawei, (3) the harm to Huawei's competitiveness, (4) the characteristics of InterDigital's anticompetitive activities, (5) InterDigital's intent, and (6) the seriousness of the harms caused to Huawei. However, other than the first two elements (which may only count for a small proportion of the total damages), it is difficult to speculate how the Shenzhen Court considered the other four factors, how these translated into damages and how the appellate court upheld the damages award.

CONCLUSION

As elaborated above, ***Huawei v. InterDigital*** is a landmark case in which the Shenzhen Court and Guangdong Higher People's Court decided a series of important issues at the intersection between antitrust law and IP,

21 InterDigital may be more of a non-practicing entity (NPE). According to the FTC, NPE also includes patent owners that primarily seek to develop and transfer technology, such as universities and semiconductor design houses.

including the first example of the establishment of a F/RAND royalty rate for patent licensing in China. It sends a clear message that China wants to encourage indigenous innovation and lower technology barriers against the development of domestic technology companies.

On one hand, ***Huawei v. InterDigital*** provided some useful guidance on how competition issues in relation to standard-setting and patent litigation may be dealt with by Chinese courts. One the other hand, however, it also created uncertainty regarding to what extent a patent holder, particularly a ***bona fide*** operating company, may protect and enforce its legal rights, especially considering the relatively challenging IP enforcement environment in China.[22] This is something that multinational companies need to bear in mind in China when enforcing their IP rights.

It has been perceived that multinational companies have controlled standard-setting processes and patents, and they have much greater bargaining power over them with respect to essential technologies. Perhaps under this perception, Qiu Yongqing, a senior judge at the Guangdong Higher People's Court presiding over the case, is reported to have stated that Huawei "used antitrust law as a weapon to counterattack" monopolization by multinationals in the technology sector, and that other Chinese companies should learn from Huawei. He went on to suggest that Chinese companies should utilize antitrust litigation to overcome technology barriers and thereby better develop themselves.[23] Such encouragement by a senior judge and the ***Huawei v. InterDigital*** decision may lead to an increase in the confidence of domestic companies to file litigation for abuse of dominance and the relatively lower cost of litigation in China will certainly present a low barrier to those companies that do wish to make claims.

Therefore, for Chinese companies, the ***Huawei v. InterDigital*** decision may have set a successful example that antitrust litigation can be utilized as a relatively inexpensive and effective tool to avoid the payment of unreasonably high patent royalties. For IPR-rich multinationals, however, this should act as a warning that they face an increasing risk of antitrust litigation in China.

22 For instance, in 2010, Microsoft filed a complaint against Guangzhou Kamhing (***Kamhing***) in with the relevant government authorities, alleging Kamhing was using pirated Microsoft software, and Kamhing was subsequently penalized by the governmentauthorities. Microsoft and Kamhing then tried to negotiate a software purchasing agreement but failed to reach an agreement. In March 2012, Microsoft filed a copyright infringement claim against Kamhing in athe district court in Nansha, Guangdong, asking for damages of CNY 4.7 million. In November 2012, Kamhing initiated an antitrust lawsuit in the same court against Microsoft. One week later, the Nansha court notified Kamhing that it should file the antitrust case in the Guangzhou Intermediate People's Court. In late November, Kamhing re-filed the case in Guangzhou, alleging Microsoft abused its dominant market position by, among other things, charging customers in mainland China unreasonable and excessive prices (almost 1/3 higher than the prices for the same products in Hong Kong). *See* http://tech.ifeng.com/internet/detail_2012_11/23/19461439_0.shtml.

23 *See* http://finance.sina.com.cn/chanjing/gsnews/20131028/214517140841.shtml.

The Qihoo v. Tencent Landmark Decision

David S. Evans

Vanessa Yanhua Zhang[1*]

On March 28, 2013, in one of the most significant antitrust decisions made by Chinese courts, the Guangdong High People's Court (Guangdong High Court) dismissed claims on anticompetitive bundling and exclusionary practices brought by Qihoo against Tencent.[2] The Court issued a relatively sophisticated and nuanced analysis of market definition and market power that examined Internet-based competition, recognized the importance of multi-sided platforms in this competition, and highlighted the critical role of dynamic competition. It now stands as both a landmark decision in China and an exemplar of serious antitrust analysis of the Internet sector for courts and competition authorities around the world. This article provides a summary of how the Court approached market definition and market power.

China has a large and rapidly growing Internet sector based primarily on domestic Chinese firms. According to China Internet Network Information Center (CNNIC), there were 564 million Internet users in China - 42.1 percent of the population - at the end of December 2012.[3] Tencent, which focuses on instant messaging, was the largest firm based on monthly users with 340 million monthly active users in November 2010.[4] Qihoo, which focuses on antivirus software, was the fourth-largest with 275 million monthly active users in November 2010.[5] Most of the major global Internet players do not have significant shares of traffic in China. Instead, services similar to those offered by international players are offered by domestic companies. Most of these platforms, including Qihoo and Tencent, earn a significant portion of their revenue by selling advertising on the web pages seen by users.

Tencent attracts users by providing a variety of free services including instant messaging (IM), micro-blogging similar to Twitter, online games, online security, social networking, search and e-commerce. QQ, its free

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2 See the Guangdong Province High People's Court's Civil Judgment No. Yuegaofaminsanchuzi 2/2011. The Chinese version is available at http://www.gdcourts.gov.cn/gdcourt/front/front!content.action?lmdm=LM43&gjid=20130328040159946185.

3 See the 31st Report of Internet Development in China, CNNIC, January 2013, Chinese version available at http://www.cnnic.cn/hlwfzyj/hlwxzbg/hlwtjbg/201301/P020130122600399530412.pdf

4 iResearch data on number of users per month (November 2010).

5 *Id.*

instant messaging service, had 399 million monthly active users as of February 2012.[6] Qihoo attracts users by providing a variety of free services including online and mobile security such as anti-virus software, a web browser, and a game platform with games developed by third-party game developers. Qihoo's Safety Guard, which is an Internet security product, had 366 million monthly active users in February 2012.[7]

Qihoo's claims relate to a series of events, widely publicized in China, which took place in late 2010. It filed a private antitrust case before the Guangdong High People's Court on November 15, 2011, accusing Tencent of violating China's AML on the grounds of tying and exclusionary behavior. Qihoo asserted that the relevant antitrust product market was integrated IM. Integrated IM includes text, audio, and video communication capabilities. Qihoo also claimed that Tencent's 76.2 percent share of that product market demonstrated that Tencent has the significant market power necessary for a dominant position under China's AML.

The Guangdong High Court used the evidence before it to conduct a hypothetical monopolist test to evaluate Qihoo's proposed relevant product market definition. It considered both demand and supply-side substitutability in doing so. Integrated IM services are provided for free. Qihoo's economic expert argued that it was possible to conduct a qualitative SSNIP test by focusing on the possibility that the hypothetical monopolist could reduce quality or increase the "hidden" price of the user looking at advertisements. The Court rejected this reasoning and focused on evidence related to price: "This Court believes that this case reflects one of the main characteristics of the products and services provided by Internet Service Providers, i.e., almost all of the suppliers set the price of its basic service at zero..." The Court then went on to cite empirical evidence based on consumer surveys that users would switch away if the provider charged for the service. It concluded that while quality and advertising were relevant, "a more important factor to be considered is whether a lot of demand substitution will be generated if a hypothetical monopolist charges the service at a small scale continuously."[8]

The Court then concluded based on the evidence on price sensitivity that consumers of integrated_IM would likely switch to free component services if the hypothetical monopolist raised its price modestly from zero. Importantly, from the standpoint of sound antitrust economic analysis, the Court rejected the plea from Qihoo's economic expert to focus on functional differences between products in favor of quantitative evidence, limited although it was, on the elasticity of demand.

The next market definition issue was whether micro-blogging (Chinese services similar to Twitter) and social networking belonged in the relevant product market. Qihoo said no. To support this conclusion its economic expert calculated the correlation coefficient between the use of social networking and IM software on a weekly and monthly basis over a short period of time. It reported that these correlation coefficients were close to zero and claimed this showed lack of demand substitutability. The Court rejected this conclusion for a number of reasons. Most importantly, from the standpoint of sophistication, the Court criticized Qihoo's economic expert for not considering dynamic competition: "This Court finds that competition is a dynamic process, and when

6 iResearch data on number of users per month (February 2012).

7 *Id*.

8 The correct SSNIP test should consider the impact of price changes on both sides of the platform—users and advertisers—but the Court focused on the single-sided SSNIP analysis presented by Qihoo.

defining a relevant market in the antitrust lawsuit on the abuse of a dominant market position, we must consider the status quo and future trends of development of relevant industries." Qihoo's expert, in particular, had ignored the fact that the use of micro-blogging and social network were rapidly increasing. The Court concluded the micro-blogging and social networking services belonged in the relevant market.

The Court then examined an argument presented by Tencent that the relevant product market for evaluating Qihoo's claims consisted of "Internet application platforms." The Court concluded that the dominant form of competition in the Chinese Internet industry involved platforms competing for the attention of users and then selling that attention to advertisers:[9]

> The Court finds that, firstly, Internet application platform as a form of business model is becoming more and more common. Consequently, users, traffic, and usage time become the main focus of competition on the Internet…. Obviously, [a number of Chinese Internet companies] provide free services to attract a large number of users, and then take advantage of the huge user resources in the operation of value-added services and advertising to make profit. In turn, they use the profit generated from value-added services and advertising to support the survival and development of their free services. This has become the typical business model in the Internet industry. In this business model, the real competition among service providers is about the number of users, page views and effective usage time. The reason is that more users generate greater traffic and more effective usage time, which lead to higher profits from advertising and value-added services. Vice-versa, those companies can survive and grow their business only by providing an integrated platform to attract more users and increase their effective usage time.

While the Guangdong High Court did not conclude that application platforms was the relevant product market, it relied on the competitive constraints coming from attention rivalry, among the other factors discussed above, to reject the integrated IM product market put forward by Qihoo and its economic expert.

Having rejected Qihoo's claim that the relevant product market consisted of integrated IM in China, the Guangdong High Court also found that the fact that Tencent had a 76.2 percent share of the overall instant messaging segment could not prove that it had monopoly power. The Court went on, however, to consider whether Tencent could have significant market power even under the assumption that the relevant product market consisted of integrated IM services in China. Importantly, it rejected the notion that market share data was sufficient to establish market power in this instance. "[D]ue to special market conditions of the Internet industry, market share, in particular cannot be deemed as a decisive factor in the determination of a dominant market position."

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9 The Court's analysis is consistent with the analytical framework described in this Evans, David S., Attention Rivalry among Online Platforms and Its Implications for Antitrust Analysis, forthcoming *Journal of Competition Law and Economics.* Available at SSRN: http://ssrn.com/abstract=2195340.

advertising to make profit. In turn, they use the profit generated from value-added services and advertising to support the survival and development of their free services. This has become the typical business model in the Internet industry. In this business model, the real competition among service providers is about the number of users, page views and effective usage time. The reason is that more users generate greater traffic and more effective usage time, which lead to higher profits from advertising and value-added services. Vice-versa, those companies can survive and grow their business only by providing an integrated platform to attract more users and increase their effective usage time.

The Guangdong High Court's decision in Qihoo v. Tencent is a landmark in several respects. It provides the most detailed antitrust analysis thus far by a Chinese court concerning the proper approach to market definition generally, and in abuse of dominance cases in particular. It demonstrates that the Chinese courts, barely five years after the AML went into effect, are already adept at rendering sophisticated antitrust opinions and applying modern economic concepts. It suggests that economic analysis, and economists, will play a significant role in private antitrust litigation in China as they have in US private antitrust litigation and in cases brought by the European Commission. Qihoo and Tencent both retained economists and introduced economic evidence before the Court. Finally, it is one of the world's leading and most sophisticated antitrust decisions concerning competition in Internet-based industries. Although some commentators will certainly disagree with specifics of the analysis, the Court provided a relatively nuanced analysis of multi-sided platform competition, rivalry in attention markets, the application of the SSNIP test to products that are offered free of charge, and the role of dynamic competition.

Rethinking Resale Pricing in China

Ninette Dodoo[1]

I. INTRODUCTION

In the past year, resale price maintenance (RPM) agreements have attracted attention in China's courts as well as before China's National Development and Reform Commission (NDRC), the enforcement authority responsible for price-related infringements under the Anti-Monopoly Law (AML), and its local branches. China's courts heard their first RPM case in 2012, in the Shanghai Intermediate People's Court. The plaintiff, Beijing Ruibang Yonghe Technology and Trade Co. Ltd. (Ru ibang), claimed damages against Johnson & Johnson for, ***inter alia***, imposing minimum resale price obligations in a distribution agreement, contrary to Article 14 of the AML.[2] The action was dismissed, and Ruibang appealed to the Shanghai High People's Court (Court). On August 1, 2013, the Court allowed Ruibang's appeal awarding damages of RMB 530,000 (approximately USD 87,000) – a pyrrhic victory for a plaintiff claiming RMB 14.4 million (approximately USD 2.3 million) in damages.

The Court's judgment coincided with the NDRC's announcement of fines, a week later, on August 7, against six infant formula manufacturers and immunity for three others for fixing or imposing minimum resale prices in connection with distribution agreements (the *Infant Formula* cases). Earlier, on February 22, two local branches of the NDRC, the Guizhou Price Bureau and the Sichuan Development and Reform Commission (Sichuan DRC), announced fines against two leading Chinese premium spirits producers, Kweichow Moutai Co. Ltd. (Moutai) and Yibin Wuliangye Group Co., Ltd. (Wuliangye), for setting minimum resale prices in distribution agreements (together the *Spirits* cases).

These cases concerned the purported use of fixed and/or minimum RPM in the context of distribution agreements and measures taken by the manufacturers concerned to enforce resale price restrictions. RPM is a controversial area of competition law and policy. Approaches differ across (and even within) jurisdictions along a scale ranging from *per se* illegality to a more permissive effects-based or *rule of reason* approach that enables the potential anticompetitive effects of RPM to be weighed against its potential benefits.[3] The recent court and

1 Ninette Dodoo is Head of Clifford Chance's Antitrust Practice in China. The author acted in the Infant Formula cases. The author is grateful to David Stallibrass and Yan Yu for providing helpful comments on an earlier version of this article. The views expressed in this article are personal. These views are not attributable to Clifford Chance or to any of its clients.

2 Article 14 of the AML prohibits vertical monopoly agreements. It expressly prohibits two kinds of practices: price fixing and restricting the minimum resale price. It also prohibits other vertical agreements deemed unlawful by China's competition authorities.

3 See, generally, OECD, Competition Committee, Roundtable on Resale Price Maintenance, 10 September 2009, DAF/COMP(2008)37, pp. 23, 36-57; Matthew Bennett, Amelia Fletcher, Emanuele Giovannetti and David Stallibrass, Resale price maintenance: Explaining the controversy, and small steps towards a more nuanced policy, available at http://mpra.ub.uni-muenchen.de/21121/, MPRA Paper No. 21121, 1, posted 7 March 2010, pp. 15-17.

administrative cases highlight the areas of competition law and policy to be honed in China. As China's courts and competition authorities chart their own course, questions arise as to the treatment of RPM in China, the applicable standards, the relationship between the competition authorities and courts, the approach to investigations, the investigative techniques used to establish anticompetitive harm, the calculation of fines, etc.[4] China has yet to adopt a clear, consistent and coherent paradigm for evaluating RPM – one that explains the specific circumstances in which RPM is/is not unlawful within the meaning of Article 14 of the AML and, if so, when the conditions for exemption under Article 15 can be met – and teaches when competition and consumer welfare are/are not likely to be adversely affected by the RPM commitment.

We examine the implications of the recent court and administrative cases in China in this article, and suggest filters that may assist in identifying instances when RPM may/may not be problematic in the China context. This effort is necessarily tentative in nature, as the law on RPM is still evolving and the very few cases to date are not necessarily definitive statements of the law in China.

II. RUIBANG V. JOHNSON & JOHNSON, THE SPIRITS AND INFANT FORMULA CASES

Resale price maintenance is an agreement between supplier and distributor where a supplier restricts the price at which the distributor may on-sell the contract products. The RPM commitment may require the distributor to on-sell the products at or above a given price (fixed or minimum RPM), or below a given price (maximum RPM). The supplier may also recommend the price at which the distributor may on-sell the contract products. The distributor can also drive the RPM commitment.[5]

RPM agreements are common in China especially for suppliers dependent on a distribution model to service customers throughout China. From a supplier's perspective, an RPM commitment enables the supplier to manage and streamline the distribution chain across China. As will be discussed below, the *Ruibang v. Johnson & Johnson, Spirits and Infant Formula* cases suggest that fixed or minimum RPM is not per se illegal under the AML, but will be punished severely if found to infringe the AML. These cases addressed different forms of RPM and measures, which Ruibang, the NDRC, the Guizhou Price Bureau and the Sichuan DRC, as the case may be, considered ensured compliance with the RPM obligations under the distribution agreements concerned.

Ruibang v. Johnson & Johnson

Ruibang v. Johnson & Johnson arose from a contractual dispute over a distribution agreement concerning the supply of sutures to Chinese hospitals. Ruibang, Johnson & Johnson's non-exclusive distributor for 15 years,

4 Many of these questions, although important for the development of a clear, consistent and coherent set of principles for RPM in China, are beyond the scope of this article.

5 Buyer-induced RPM is generally regarded as more harmful than supplier-induced RPM. As the European Commission's Guidelines on Vertical Restraints explain: "Strong or well organized distributors may be able to force or convince one or more suppliers to fix their resale price above the competitive level and thereby help them to reach or stabilise a collusive equilibrium. The resulting loss of price competition seems especially problematic when the RPM is inspired by the buyers, whose collective horizontal interests can be expected to work out negatively for consumers," OJ [2010] C 130/1, para. 224.

concluded a one-year distribution agreement to supply the sutures to a Beijing hospital.[6] Ruibang brought an action in the Shanghai Intermediate Court claiming damages against Johnson & Johnson for, ***inter alia***, imposing a minimum RPM commitment in the distribution agreement and wrongfully terminating that agreement for non-compliance. Ruibang supplied the products below a price set by Johnson & Johnson. A warning followed, and later Johnson & Johnson ceased supply, eventually terminating the agreement. Johnson & Johnson concluded new distribution agreements with other distributors in 2009 omitting the minimum RPM clause.

The Shanghai Intermediate Court dismissed Ruibang's action for lack of sufficient evidence that the disputed clause restricted or eliminated competition.[7] It was thus lawful under Article 14 of the AML. Both the form and the likely effects of the RPM in the agreement had to be considered, which required evaluation of market shares; the level of competition at the supplier and distributor levels; and the impact of the RPM on competition and on the availability of the contract products in the market. Johnson & Johnson pointed to several other competing suppliers of sutures to establish that the market was sufficiently competitive and that the RPM had no adverse impact on competition.

Ruibang appealed, and on appeal the Court overturned the lower court's judgment. It held that Ruibang had adduced sufficient evidence during the appeal procedure, which showed that the minimum RPM obligation had anticompetitive effects in China and thus infringed Article 14 of the AML. The RPM eliminated intrabrand competition and reduced interbrand competition in sutures in China harming consumers' interests.[8] Relying on the Supreme People's Court's Judicial Interpretation on civil procedures in competition-related actions in China,[9] the Court reasoned that like horizontal agreements between competitors, which the AML prohibits under Article 13, an agreement with minimum RPM obligations infringes the AML only if it has anticompetitive effects.[10]

6 The agreement at the centre of the dispute was for the period 2 January 2008 to 31 December 2008. It was still in force when the AML entered into force in August 2008 and, therefore, the AML applied.

7 The Court also determined that Ruibang failed to establish to a sufficient degree that there was a causal link between the harm claimed and the damages sought.

8 The Court focused on elimination of intrabrand price competition. A minimum RPM agreement necessarily limits distributors' ability to compete with each other. Even where pro-competitive, RPM may increase prices but also quality, etc. There is little discussion in the Court's judgment on the minimum RPM's impact on non-price competition and, unlike the lower court, whether competition at the upstream level was sufficient to undermine the anticompetitive effects.

9 See, Provisions on Several Issues Regarding the Application of Laws to Civil Disputes Involving Monopoly Conduct published on 3 May 2012.

10 The Judicial Interpretation provides no explicit guidance on whether the same approach applies to vertical agreements (such as distribution agreements between manufacturers and their distributors or wholesalers). The Court reasoned that since Articles 13 and 14 define anticompetitive effects in the same manner, the requirement to show anticompetitive effects applied to vertical agreements. The Judicial Interpretation is also silent on which party bears the burden of establishing anticompetitive effects in cases involving vertical agreements. The Court relied on the general civil procedure rules according to which the party that makes a claim must establish it. The Judicial Interpretation reverses the burden of proof in cases involving horizontal agreements and requires the defendant to establish that the horizontal agreement in issue has no anticompetitive effects.

For the Court, evidence of anticompetitive effects is an essential element for establishing that (minimum) RPM is unlawful within the meaning of Article 14 of the AML. In determining whether minimum RPM has anti-competitive effects, the Court proposed four questions to address:

- Is there sufficient competition in the relevant market (i.e. the competitiveness of the market);
- Does the company driving the RPM have a strong market position (i.e. does it have a leading position);
- What is the company's motive in setting the RPM (i.e. is there evidence of anticompetitive intent); and
- What are the competitive effects of the RPM in the relevant market (i.e. do the potential anticompetitive effects outweigh the potential pro-competitive benefits).

The Court found that Johnson & Johnson had a very strong market position (it was market leader with a more than 20 percent market share,[11] it had a well-established brand, it had strong pricing power and had consistently maintained high prices for the past 15 years, it wielded considerable influence over its distributors through a system of territorial exclusivity, short term agreements and single branding); the market was characterised by strong brand loyalty, high barriers to entry, customers posed little or no competitive constraints; and that Johnson & Johnson's motives were anticompetitive. The Court found that the distribution agreement expressly required Ruibang to maintain Johnson & Johnson's price levels, and marketing strategies discouraged distributors from engaging in price competition or lowering prices in response to competitive pressures. The Court also pointed to Johnson & Johnson's tight monitoring system, which encouraged compliance. Its conduct set an example for other competitors to follow.

The Court was not convinced that the minimum RPM had any redeeming features, but nevertheless considered Johnson & Johnson's efficiency claims under Article 15 of the AML. It found no causal link between the claimed product quality and safety efficiencies and the minimum RPM obligation; nor was the Court satisfied that any services provided by Ruibang contributed to the claimed product quality and safety efficiencies. The Court was also not persuaded that the RPM was necessary to streamline the distribution system. It is worth emphasising that the Court did not rule out the possibility for a manufacturer to claim efficiencies even where it has significant market power. As the Court expressly noted, an efficiency claim could include implementing RPM for new product entry.

11 This is considerably lower than the 50 percent dominance threshold where single firm dominance is presumed under Article 19 of the AML. Although the Court questioned the reliability of the market share figures, based on publicly available information and data provided by an economist, it reasoned that Johnson & Johnson's market share was very likely higher if its share of sales in the Beijing hospital at the centre of the dispute were taken into account, and higher still across top Beijing hospitals. The reasoning raises questions for market definition and appropriate proxies for assessing market power.

The Spirits and Infant Formula Cases

On February 22, two local branches of NDRC, Guizhou Price Bureau and Sichuan DRC, announced total fines of RMB 449 million (approximately USD 74 million) on a Moutai and Wuliangye subsidiary, respectively for engaging in minimum RPM, contrary to Article 14 of the AML. The fines were equivalent to about one percent of each subsidiary's turnover.[12] Previously, in January 2013, Moutai and Wuliangye each announced that NDRC was investigating their respective commercial practice of requiring distributors to sell their products not lower than a given price. Moutai and Wuliangye penalized non-compliant distributors through various means including fines, confiscating deposits, deducting marketing support expenses, limiting supply, and monitoring compliance. The manufacturers also penalized distributors for selling outside assigned territories and undercutting prices in higher-priced territories. Each manufacturer actively cooperated with the authority's investigation and undertook to terminate the impugned conduct, cancel the penalties and return confiscated deposits, and to adopt measures correcting its conduct.

The Sichuan DRC's decision sheds further light on the approach taken in finding the minimum RPM unlawful.[13] It determined that the impugned conduct: eliminated intrabrand price competition between Wuliangye's distributors and harmed economic efficiency; limited interbrand competition between manufacturers, and set a negative example for other spirits manufacturers to follow – the presence of parallel networks of RPMs further harmed competition; and harmed consumers' interests as the impugned conduct limited opportunities for consumers to purchase products at lower prices. The Sichuan DRC also determined that as a leading spirits brand and with few alternatives in the market, Wuliangye's conduct adversely affected consumer choice. However, the decision does not consider whether there were any efficiency-enhancing reasons that might justify the RPM.

Several months later, on August 7, the NDRC imposed total fines of RMB 668.73 million (approximately USD 109 million) on six infant formula manufacturers and exempted three others for the purported use of fixed or minimum RPM in connection with distribution agreements and measures that enforced the RPM obligations.[14] The fines ranged from three-to-six percent of turnover derived from infant formula sales in the preceding financial year.[15] According to the NDRC's press release, the impugned resale pricing obligations kept prices high, eliminated or restricted intrabrand competition, undermined interbrand competition, distorted fair

12 Article 46 of the AML enables the Chinese competition authorities to impose fines of between one percent and ten percent of a party's annual turnover in the year preceding the infringement. However, the AML is ambiguous as to how to calculate this turnover and there are currently no official guidelines that clarify this issue. If the Spirits cases are followed, fines may be calculated based on the turnover of the entity involved in the infringement, rather than on the turnover of the corporate group to which it belongs.

13 The Guizhou Price Bureau's decision provides little guidance on the authority's reasons for concluding that the conduct involved is unlawful within the meaning of Article 14 of the AML.

14 Nine international and domestic manufacturers were at the centre of the NDRC's investigation. The NDRC imposed fines on Abbott, Biostime, Dumex, Fonterra, FrieslandCampina, and Mead Johnson. Three companies, Beingmate, Meiji and Wyeth, were not fined. According to senior NDRC officials in public fora, the grant of leniency and the different fine levels reflect the degree of cooperation during the NDRC's investigations, the severity of the impugned conduct, whether companies took the initiative to report relevant circumstances establishing the existence of a RPM agreement, the relative importance of the evidence provided to the NDRC, and measures taken to address the impugned conduct.

15 The manufacturers also undertook to terminate resale price restrictions and to implement/reinforce compliance measures and training for personnel. Manufacturers further undertook to reduce or freeze infant formula prices for a prescribed period of time.

and orderly competition in the market, and harmed consumers' interests and rights. The impugned conduct varied from manufacturer to manufacturer and, based on the NDRC's press release, included, inter alia, setting fixed or minimum resale prices, imposing penalties and disguised penalties for non-compliance, deducting or cancelling rebates, and limiting or terminating supply. The NDRC determined that the manufacturers' conduct infringed Article 14 of the AML, and that none of the available exemptions under Article 15 of the AML applied.

III. CONVERGENCE OR DIVERGENCE IN CHINA?

The Court's judgment in Ruibang v. Johnson & Johnson and the Spirits and Infant Formula decisions suggest different approaches between local branches of the NDRC, the NDRC and its local branches, and the NDRC and the Court.[16] The Court's judgment calls for a solid economics, effects-based assessment for minimum RPM.

The position taken by the NDRC (and one of its local branches in the Spirits cases) sits comfortably close to a by object approach, but is only a stone's throw away from per se illegality. This approach in the context of the AML's current legislative framework considers the merits of each instance of RPM on a case-by-case basis. The inquiry focuses on whether there is a RPM obligation under the distribution arrangement concerned and the form of the RPM. Fixed or minimum resale price restrictions are presumed unlawful as expressly prohibited under Article 14 of the AML, unless justified by one of the exceptions under Article 15 of the AML and it can be shown that the RPM does not adversely affect competition, and consumers share in the resulting benefits.

The NDRC's approach to fixed or minimum RPM is not dissimilar to the EU's by object approach.[17] But, greater emphasis is placed on the form of the RPM seemingly leaving little room for consideration of efficiency claims under Article 15.[18] Given the Government's priority to reduce consumer goods prices in China, as articulated in its 12th Five Year Plan, resale price restrictions that result in propping up retail prices or softening competition may rarely find protection under Article 15 in the present climate. Further, it may prove difficult

16 We focus on Ruibang v. Johnson & Johnson and the Sichuan DRC's decision in the Spirits cases, which provide detailed information on the face of the record on the RPM analyses conducted.

17 See, Luc Peeperkorn, Resale Price Maintenance and Its Alleged Efficiencies, (2008) 4 European Competition Journal, 201, p. 203: "[T]he direct consequence of including RPM in an agreement is that […] the Commission will assume that the agreement will have actual or likely negative effects; there is a presumption that such effects will result from the agreement […] that RPM will not have positive effects or that, where efficiencies are likely to result, these will not be passed on to consumers […]. <u>The moment that [a] firm brings forward convincing evidence of efficiencies, the authority is forced to show the likely or active negative effectives</u>," emphasis added. In practice, the EU's current practice of treating fixed and minimum RPM as hardcore restrictions and presuming them to restrict competition and unlikely to satisfy the Article 101(3) conditions, is a form of de facto per se prohibition. See Article 4 of Commission Regulation (EU) No 330/2010 of 20 April 2010 on the application of Article 101(3) of the Treaty on the Functioning of the European Union to categories of vertical agreements and concerted practices, OJ [2010] L 102/1; Guidelines on Vertical Restraints, supra note 5, paras. 48, 223-225. See also Frederik van Doorn, Resale Price Maintenance in EC Competition Law: The Need for a Standardised Approach, (November 6, 2009), available at http://ssrn.com/abstract=1501070, pp. 4-6; Alison Jones, Resale Price Maintenance: A Debate About Competition Policy in Europe?, (2009), available at http://ssrn.com/abstract=1932556, pp. 18-19.

18 It is worth noting that a number of senior NDRC officials discussing the Spirits and Infant Formula cases in public fora have argued that none of the manufacturers involved in the cases adduced sufficient evidence for exemption under Article 15.

to adduce detailed economic evidence of efficiencies in cases where the NDRC's investigation is conducted within a very short period and in summary fashion. If substantiated, efficiency claims are unlikely to be viewed favourably if the claimed benefits can be achieved by less restrictive means.

The Court, the NDRC and its local branches did not address recommended resale pricing. In the context of the current legislative framework of the AML, it seems that recommended RPM is unlikely to be characterised as unlawful if the supplier only recommends a resale price and does not penalize, apply pressure, or offer incentives, to encourage distributors to follow the recommended price.[19] There is of course a risk that the recommended price may serve as a focal point for distributors and might be observed by some or all of them – in which case the recommended price may be subject to challenge.

Despite diverging approaches, broad consensus appears to be emerging between different institutions in China. The evolving framework considers each instance of RPM on a case-by-case basis and requires (some) consideration of the effects of the RPM obligation on competition. This necessarily implies an assessment of the form and economic context of the RPM obligation. The outcome of the inquiry, the scope of the inquiry into the effects of the RPM on competition, the degree of sophistication and economic rigour of the inquiry, and the economic evidence underpinning the assessment may vary depending on various factors, including the institution reviewing the RPM. That is, until China adopts a clear, consistent and coherent approach to RPM.[20] There is also broad consensus that an efficiency claim will need to be significant, convincing and substantiated and result directly from the RPM.

IV. THE SIGNS FOR LAWFUL/UNLAWFUL RPM IN THE CHINA CONTEXT

RPM – especially minimum RPM – is a controversial area of competition law and policy not least because it may lead to anticompetitive harm, and it may also generate pro-competitive benefits from an economic perspective.[21] As illustrated and summarised by one set of economists:

> *"[F]rom an economic perspective RPM sits rather awkwardly […] Yes, for sure, it can be anticompetitive. But it can also give rise to important efficiency benefits, and in some cases will be indispensable for achieving those efficiency benefits […]. [M]ost economists would agree that its precise position in any given case will depend on market circumstances…"*

19 None of the institutions considered maximum RPM. The institutions can be expected to have some sympathy for maximum RPM especially in markets subject to price regulation in China.

20 A consistent approach is preferred for legal certainty. It is not uncommon for approaches to differ within jurisdictions. In the US, for example, several States still apply a per se standard to minimum RPM despite the Supreme Court's five-to-four majority opinion in Leegin overturning Dr. Miles, a century-long precedent, and holding that minimum RPM should be analysed under a rule of reason standard. Leegin Creative Leather Products, Inc. v. PSKS, Inc., 551 U.S. 877 (2007); Dr. Miles Medical Co. v. John D. Park & Sons Co., 220 U.S. 373 (1911).

21 See, for example, Luc Peeperkorn, supra note 17, pp. 206-212; William S. Comanor, The Two Economics of Vertical Restraints, 5 Rev. Indus. Org. (Summer 1990); John B. Kirkwood, Rethinking antitrust policy toward RPM, The Antitrust Bulletin: Vol. 55, No. 2/Summer 2010, 423; Warren S. Grimes, The Seven Myths of Vertical Price-Fixing: The Politics and Economics of a Century-Long Debate, 21 Sw. U.L. Rev. 1285 (1992).

"Faced with having to choose whether RPM is mostly harmful or mostly beneficial, some economists (such as us) […] plump for RPM being an 'object' infringement. Others cannot stomach the fact that this approach has the implication of presuming unlawful, on the one hand, agreements that could not possibly have an anticompetitive effect and, on the other hand, agreements that have real efficiency benefits. These economists plump for RPM being an 'effect' infringement."[22]

Other economists concur pointing to a rule of reason as a defensible basis to assess the legitimacy of vertical restraints:

"Theoretically, the only defensible position on vertical restraints seems to be the rule of reason. Most vertical restraints can increase or decrease welfare, depending on the environment. Legality or illegality per se thus seems unwarranted."[23]

Proponents of RPM's anticompetitive potential generally point to RPM's ability to facilitate collusion between distributors or between suppliers; increase or maintain prices at artificially high levels, or prevent direct price reductions; prevent price competition between distributors and thereby discourage new entry or expansion based on low(er) price models at the distribution level; enable dominant distributors or suppliers to maintain their market power; or reduce pressure on a supplier's margins.[24]

Others emphasise RPM's pro-competitive benefits highlighting the fact that RPM may address the free rider problem and encourage distributors to offer consumers additional services promoting demand; facilitate new product or brand entry; or encourage distributors to carry a supplier's products with uncertain demand or maintain more stocks of a supplier's products.[25] The limited empirical evidence and studies on the actual effects of RPM suggest that most cases involving RPM are pro- and not anticompetitive:

22 Matthew Bennett, Amelia Fletcher, Emanuele Giovannetti and David Stallibrass, supra note 3, pp. 16-17.

23 Luc Peeperkorn, supra note 17, p. 205, quoting John Tirole, The Theory of Industrial Organization, Cambridge, MIT Press (1990), 186.

24 See, for example, P. E. Areeda & Hovenkamp, Antitrust Law (2nd ed. 2004), para.1604b, at 40 noting that RPM "tends to produce higher consumer prices than would otherwise be the case. The evidence is persuasive on this point"; Luc Peeperkorn, supra note 17, pp. 206-211; Eric Gippini-Fournier, Resale Price Maintenance in the EU: In Statu Quo Ante Bellum (September 21, 2009), available at http://ssrn.com/abstract=1476443, pp. 2-16; Christian Ewald, The Economics of Resale Price Maintenance – Why Europe is Right not to Follow the US on the Slippery Slope of Leegin, Journal of European Competition Law & Practice, 2012, Vol. 3, No. 3, 300, pp. 301-302; F. M. Scherer, The Economics of Vertical Restraints, 52 Antitrust L.J. 687 (1983), pp. 702-704; Warren S. Grimes, Resale Price Maintenance: A Competitive Assessment, Federal Trade Commission Workshop on Resale Price Maintenance Panel on Anticompetitive Effects, pp. 5-10; Marina Lao, Free Riding: An Overstated, and Unconvincing, Explanation for Resale Price Maintenance, in Robert Pitofsky, (ed.), How the Chicago School Overshot The Mark: The Effect of Conservative Economic Analysis on U.S. Antitrust, Oxford University Press (2008), available at http://ssrn.com/abstract=1024221, pp. 199-207; John B. Kirkwood, supra note 21, pp. 429-454.

25 See, for example, Bastiaan M. Overvest, A note on collusion and resale price maintenance, E.J.L. & E, 2012, 34(1), 235; Kenneth G. Elzinga and David E. Mills, Leegin and Procompetitive Resale Price Maintenance (February, 10 2010), available at http://ssrn.com/abstract=1885001; Lester G. Telser, Why Should Manufacturers Want Fair Trade?, 3 J.L. & Econ. 86 (1960).

"While different theoretical models yield diametrically opposed predictions as to the welfare effects of vertical restraints, we find that […] with manufacturer/retailer of franchisor/franchisee relationships, the empirical evidence concerning the effects of vertical restraints on consumer wellbeing is surprisingly consistent. Specifically, it appears that when manufacturers choose to impose such restraints, not only do they make themselves better off, but they also typically allow consumers to benefit from higher quality products and better service provision."[26]

Unlike the US Supreme Court's structured rule of reason proposed by the majority in Leegin,[27] the by object approach employed by the European Commission, coupled with a set of guidelines, China has yet to adopt a framework that clearly explains when RPM is/is not unlawful in China. The NDRC has taken a strict approach towards RPM, whilst the Court's focus on the reduction of intrabrand price competition has set a high bar for establishing that a particular RPM obligation is not unlawful. There are currently no guidelines, and guidelines are not expected soon. A by object approach, underscored with a robust effects-based analysis, alongside a clear set of guidelines and/or safe harbours drawn from China-specific precedents would offer the much needed degree of legal certainty under the AML. In the absence of guidelines or safe harbours, are there filters that can be used by companies and their advisors to determine when RPM is/is not likely to be unlawful in China?

The likely triggers for an investigation seem to be concern over high prices in China, in particular sustained over a considerable period of time, concern over harm to the consumer interest, and complaints. The Court's judgment in Ruibang v. Johnson & Johnson also teaches that if there is sufficient competition in the market, RPM is unlikely to be found unlawful. Conversely, if a supplier (or distributor) with a strong market position and anticompetitive motives drives the RPM then the RPM is more likely to result in anticompetitive effects and be considered unlawful – unless the supplier can show that the RPM has pro-competitive benefits that outweigh the perceived negative effects. However, the Infant Formula cases show that evidence of market power is not a necessary prerequisite in every situation.

26 See, F. Lafontaine and M. Slade, Exclusive Contracts and Vertical Relationships: Empirical Evidence and Public Policy in Paolo Buccirossi (ed.), Handbook of Antitrust Economics, Cambridge, MIT Press (2008), pp. 408-409. See also, James C. Cooper, Luke M. Froeb, Daniel O'Brien and Michael G. Vita, Vertical Antitrust Policy as a Problem of Inference, 23 Int'l J. of Indus. Org. 639 (2005), p. 640; Thomas R. Overstreet, Resale Price Maintenance: Economic Theories and Empirical Evidence, Bureau of Economics Staff Report, Federal Trade Commission (1983), pp. 119-129; Pauline Ippolito, Resale Price Maintenance: Empirical Evidence from Litigation, 34 J.L. & Econ. 263 (1991), pp. 282-285. Overstreet and Ippolito are criticised for reliance on limited evidence and narrowly focusing on two theories of anticompetitive harm, the likelihood of manufacturer or dealer collusion. See, John B. Kirkwood, supra note 21, pp. 441-442; Thomas A. Lambert, A decision-theoretic rule of reason for minimum resale price maintenance, The Antitrust Bulletin: Vol. 55, No. 1/Spring 2010, 167, p. 189.

27 The Leegin majority directed the lower courts to "devise rules […] for offering proof, or even presumptions […] to make the rule of reason a fair and efficient way to prohibit anticompetitive restraints and to promote pro-competitive ones." Since then, different approaches have emerged to evaluate RPM. See, Thomas A. Lambert supra note 26, pp. 194-223 for a decision-theoretic approach and a summary of four alternative approaches together with their limitations. The alternative approaches focus respectively on the RPM's impact on consumer prices, the identity o the instigator of the RPM, the likelihood of free riding, and mechanically applying the Leegin factors. See also, John B. Kirkwood for a discussion of presumptive illegality with safe harbours, supra note 21, pp. 463-470; Christine A. Varney then Assistant Attorney General Antitrust Division, U.S. Department of Justice, Antitrust Federalism: Enhancing Federal/State Cooperation, October 7, 2009, pp. 7-14.

Ruibang v. Johnson & Johnson and the Spirits cases further suggest that RPM may be harmful if implemented in a market characterised by relatively high concentration levels at the upstream or downstream level, limited interbrand competition, high entry barriers, the presence of multiple networks of supplier/distributor relationships, and where the use of RPM is widespread and is used by most manufacturers to maintain resale prices. RPM may also be harmful if coupled with territorial exclusivity and/or single branding. In addition, RPM may be harmful if used to facilitate collusion between suppliers or distributors.

Further, the kind of product involved may be relevant in determining whether possible efficiency claims can be entertained in an individual case. As the Court indicated, RPM may be pro-competitive where a manufacturer employs RPM to facilitate product entry. One may also reasonably infer that an efficiency claim in an individual case is more likely to be considered where the product involved is most likely to be susceptible to free riding such as in the case of products with special features (e.g. differentiated, intricate, and highly sophisticated products).[28] A distributor's own efforts in promoting the product in terms of pre- or aftersales services may be relevant, as the Court suggests.

V. CONCLUSION

The Court called for a solid economics, effects-based approach for RPM in Ruibang v. Johnson v. Johnson, whereas the NDRC and its local branches adopted a position in the Spirits and Infant Formula cases that mirrors a by object approach. They made clear that a supplier that imposes a fixed or minimum RPM obligation on its distributors runs the risk of huge fines unless it can be shown that the RPM obligation satisfies the Article 15 criteria.

In spite of apparent differences in approach, the Court's assessment in Ruibang v. Johnson & Johnson and references to impact on intrabrand and interbrand competition in the Spirits and Infant Formula cases both suggest that at least some effects-based inquiry is required when assessing whether fixed or minimum RPM is/ is not unlawful. The assessment may vary depending on a various factors, including the institution reviewing the RPM obligation.

Given the recent focus on vertical agreements, companies operating in China may need to review distribution agreements to strengthen compliance. Companies will need to consider whether to conduct detailed reviews, including economic analyses, of their distribution arrangements. The potential challenge for companies is the lack of a clear, consistent and coherent set of criteria as well as standards for determining when RPM is/ is not unlawful.

28 See also, Christian Ewald, supra note 24, p. 306; John B. Kirkwood supra note 21, pp. 465-470.

MOFCOM Publishes Interim Regulations on Standards for Simple Mergers and Requests Public Comments

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INTRODUCTION

Under the 2008 Anti-Monopoly Law (AML) Articles 20-31, The Ministry of Commerce (MOFCOM) is responsible for reviewing proposed concentrations that meet transaction-size thresholds. The statute sets out a general list of relevant factors including market shares, market concentration, effect on market access, technological progress, consumers, business operators, national economic development and "other factors that may affect the market competition."[1] These broad standards have been supplemented by market definition guidelines and guidelines on competitive impact analysis, among other guidelines and regulations.[2] While the MOFCOM staff is reportedly relatively small,[3] since the effective date of the AML, it has reportedly reviewed more than 450 notified concentrations, issued 16 conditional approvals and prohibited one proposed transaction.[4] Most recently, on April 3, 2013, MOFCOM published a Draft set of Interim Regulations on Standards Employed for Simple Concentrations of Business Operators for public comment. In response to the invitation, the ABA Sections of Antitrust and International Law submitted comments on May 16.[5]

1 AML Art. 27.

2 Yee Wah Chin, Merger Control Under China's Anti-Monopoly Law, Legal Risk for China Investments, E.4.2 Dividing Point Investment Management (January 2013), available at http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2187147 (last visited June 8, 2013). Other guidelines include pre-merger notification procedures, draft merger remedy rules, and national security review of acquisitions by domestic enterprises by foreign investors.

3 Michael Martina, INSIGHT – Flexing Antitrust Muscle, China is a New Merger Hurdle (May 2, 2013) (stating that "people familiar with MOFCOM's anti-monopoly bureau … say it has only 10-12 case handlers, and all deals have to go through a pre-notification phase conducted by a department with just five people."), available at http://uk.reuters.com/assets/print?aid=UKL3N0DJ0I220130502

4 Yee Wah Chin, Merger Control Under China's Anti-Monopoly Law, Legal Risk for China Investments, E.4.2 Dividing Point Investment Management (January 2013), available at http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2187147 (last visited June 8, 2013).

5 Comments of the American Bar Association Section of Antitrust Law and Section of International Law on the MOFCOM Draft Interim Regulation on Standards Applicable to Simple Cases of Concentrations of Concentrations of Business Operators (May 16, 2013), available at http://www.americanbar.org/content/dam/aba/administrative/antitrust_law/at_comments_simple_20130516.authcheckdam.pdf (last visited June 8, 2013).

There are approximately 100 jurisdictions with competition laws worldwide and many of them review proposed transactions and prohibit the transaction from closing until the review has been completed, so-called suspensive merger-control systems. In the absence of an agreement to defer to a primary jurisdiction, this system gives the last reviewing jurisdiction the ultimate power to delay the acquisition. It is generally recognized that most mergers are pro-competitive or competitively neutral, so multiple, lengthy reviews can frustrate competitive transactions. Additionally, the investigation of complex transactions requires significant agency staff time, expertise and funding. The European Commission and the US agencies have adopted different approaches to expedite approval of non-problematic concentrations, thus freeing agency resources for the cases that present real competitive issues.

These Interim Regulations are in the tradition of longstanding procedures employed by the European Commission ("the Commission") and US DOJ Antitrust Division and Federal Trade Commission (FTC) for expedited merger review in under certain circumstances. The Commission noticed a simplified procedure for speedy review of transactions in 2005[6] and is currently engaged in a consultation to update and revise some of the provisions of the procedure.[7] The US FTC and DOJ have long responded to requests for early termination of reported transactions under the Hart-Scott-Rodino Act. Any party may request early termination before the HSR waiting period has expired and reported statistics indicate that requests were made in more than 76 percent of transactions reported in 2012, and more than 82 percent of the requests were granted.[8]

BACKGROUND

The AML, like many other merger review regimes, requires parties to a "consolidation" to file pre-merger notification if their transaction exceeds certain triggers detailed in MOFCOM notification regulations.[9] After the completed materials have been filed and the notification has been accepted, the parties are required to wait pending MOFCOM review. AML Articles 25 and 26 establish a 3-phase review period of 30, 60 and 90 days

6 Commission Notice on a simplified procedure for treatment of certain concentrations under Council Regulation (EC) No 139/2004 (2005/C 56/04) Official Journal C 56, 05.03.2005, p. 32-35, available at http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=CELEX:52005XC0305(03):EN:NOT (last visited June 8, 2013).

7 Commission Notice of XXX on a simplified procedure for treatment of certain concentrations under Council Regulation (EC) No 139/2004, available at http://ec.europa.eu/competition/consultations/2013_merger_regulation/draft_revised_simplified_procedure_en.pdf (last visited June 8, 2013); Public Consultations: EU merger control – Draft revision of simplified procedure and merger implementing regulation, available at http://ec.europa.eu/competition/consultations/2013_merger_regulation/index_en.html (last visited June 8, 2013).

8 Federal Trade Commission and Department of Justice, Hart-Scott-Rodino Annual Report FY 2012, 35th Annual Report, Appendix A, available at http://www.ftc.gov/os/2013/04/130430hsrreport.pdf (last visited June 8, 2013). Appendix A indicates that during FY 2012, 1,429 transactions were reported, there were 1,094 involved requests for early termination, 902 requests were granted, and 192 requests were not granted.

9 Measures on the Notification of Concentrations Between Undertakings; and Measures on the Review of Concentrations Between Undertakings (2009).

respectively, not including delays. This schedule has, in some cases, exceeded a year.[10] As in all suspensive merger review jurisdictions, the parties may not conclude their transaction until after it has been approved or the time period for the review has expired.

There is international consensus that competition agencies should devote their resources to focus on serious threats to the competitive process. In the merger realm, the International Competition Network recommends that the purpose of merger reviews should be to identify, prohibit or impose remedies only on concentrations that are likely to significantly harm competition."[11] In commentary, the ICN recommends that agencies adopt an analytic framework to distinguish between concentrations that threaten competitive harm and those are likely to be neutral or pro-competitive. It is an ICN Guiding Principle for Merger Notification and Review that merger review should be efficient, timely, and effective,"[12] and agencies should promulgate procedures to "provide enforcement agencies with information needed to review the competitive effects of transactions and should not impose unnecessary costs on transactions. The review of transactions should be conducted, and any resulting enforcement decision should be made, within a reasonable and determinable time frame." The ICN recommendations and best practices were generated by the consensus of the member competition agencies and, while they do not have the status of statutory law, they are essentially soft law and deemed persuasive in many jurisdictions.

PROVISIONS ON THE DRAFT RULES

The Interim Regulation is a brief document, comprising just three key substantive Articles, but has the possibility to affect the practice of merger notification by parties as well as the speed and conduct of MOFCOM's review process, depending on additional content that may be added by MOFCOM. It also leaves many important questions unanswered and the procedure to be applied to simple cases is undefined as yet. First, the Interim Regulation identifies a set of six merger scenarios that will ordinarily be entitled to review as simple cases. Second, it identifies another six factual scenarios that will disqualify a proposed transaction from consideration as a simple case. Finally, in the third substantive article, even if a proposed concentration has been identified as a simple case, MOFCOM itself may revoke that designation in four open-ended circumstances.

10 Michael Martina, INSIGHT – Flexing Antitrust Muscle, China is a New Merger Hurdle, (May 2, 2013), available at http://uk.reuters.com/assets/print?aid=UKL3N0DJ0I220130502

11 ICN Recommended Practices for Merger Analysis, Recommendation 1A, available at http://www.international-competitionnetwork.org/uploads/library/doc316.pdf (last visited June 9, 2013). The recommendation provides that "the purpose of competition law merger analysis is to identify and prevent or remedy only those mergers that are likely to harm competition significantly."

12 ICN Guiding Principles for Merger Notification and Review (Jan. 7, 2010), available at http://www.internationalcompetitionnetwork.org/uploads/library/doc591.pdf (last visited June 9, 2013) Principle #5 provides that "[t]he merger review process should provide enforcement agencies with information needed to review the competitive effects of transactions and should not impose unnecessary costs on transactions. The review of transactions should be conducted, and any resulting enforcement decision should be made, within a reasonable and determinable time frame."

Beyond the substantive provisions, Article 1 of the draft Interim Regulation ties the Regulations to the AML, which may suggest the possibility for expedited review. AML Art. 25 requires a preliminary decision "***within*** 30 days [of receipt of the premerger notification materials]," so may implicitly recognize the possibility of expedited decisions in some cases. Interim Regulation Art. 5 provides for the same penalties available under AML Art. 52, if information is concealed or false or misleading information or materials are submitted in the merger notification. Art. 6 delegates to MOFCOM the authority to interpret the Regulation, and Art. 7 will state the effective date of the Regulation. The key substantive provisions are Articles 2, defining "simple cases"; 3, identifying the factors which may exclude transactions from simple case status; and 4, concerning revocation of simple statue.

ARTICLE 2: WHAT ARE "SIMPLE CASES"?

The Regulations identify six different fact patterns that may fall within the "simple case" designation. Three are based on market share criteria and three are keyed to the economic effect within China of the proposed transaction.

Market Share Based Determinations

If a proposed concentration involves firms with relatively low market shares, then the transaction may be designated as a simple case, according to the Interim Regulation. The specific market share thresholds depend on whether the transaction is horizontal (section A), vertical (section B), or, apparently, a conglomerate merger (section C). If the merger is ***horizontal***, all of the participant firms must have a collective market share of less than 15 percent of the relevant market. If the transaction is ***vertical***, then the firms are entitled to characterization as a simple case only if they have a "collective market share" under 25 percent "in the vertical market." Finally, if the concentration is ***not vertical***, section C provides for simple case status if they have a "collective market share" less than 25 percent "in all markets."

The market share requirements for horizontal and vertical concentrations are identical to the current Commission market share percentages, 15 percent and 25 percent respectively. The Commission Simplified Procedure regulation currently does not deal with non-horizontal and non-vertical transactions. However, the Commission has issued revised Simplified Procedure Regulations and opened a public consultation on the draft provisions.[13] The proposed new market share thresholds are a combined 20 percent for transactions involving "business activities in the same product and geographical market (horizontal relationships)" and combined market shares of 30 percent for those "engaged in business activities in a product market which is upstream or downstream of a product market in which any other party to the concentration is engaged (vertical relationships)."[14] The draft Commission standards also provide a threshold for joint ventures that is based on total assets

13 Notice of Public Consultation, available at http://ec.europa.eu/competition/consultations/2013_merger_regulation/index_en.html (last visited June 9, 2013). The consultation period extends from March 27, 2013 to June 19, 2013.

14 Commission Notice on a simplified procedure for treatment of certain concentrations under Council Regulation (EC) No 139/2004, available at http://ec.europa.eu/competition/consultations/2013_merger_regulation/draft_revised_simplified_procedure_en.pdf (last visited June 9, 2013). Non-horizontal/non-vertical concentrations are addressed in sections 7 and 15 of the proposed Simplified Procedures, which note that these concentrations may be

or turnover of less than €100 million (about $132 million). The MOFCOM Interim Regulations do not provide a simple case based on the size of the transaction, assets or turnover of the parties to the concentration.

The definition of relevant product and geographic markets may be complex and require lengthy data collection and analysis. Deciding whether or not a concentration ***is*** horizontal may be contested. It may be equally difficult to determine market shares of participants in a relevant market, and merger and abuse of dominance cases have turned on precisely these issues.[15] Additional issues that are not currently addressed in these sections include the standard of proving market definitions and market shares and whether the burden is on the parties. The Interim Regulations do not state whether the parties to the concentration may submit documents and information to the relevant market shares pending a decision on whether the concentration is a simple case or whether they are required to submit a complete notification even if the concentration is ultimately deemed to be a simple case.

Effects-Based Determinations

Sections D, E, and F deal with non-market share tests for simple case status and differentiate between transactions with a nexus to the Chinese economy and those that, without a meaningful nexus, may safely be categorized as simple transactions. Section D covers concentrations that create a joint venture outside China, which does not "engage in economic activity in China." Section E is limited to acquisitions of a foreign firm that "does not engage in economic activity in China." Although the business operators involved in these transactions may be doing business in China in some other aspect of their business, the specific concentration lacks a nexus with China and, therefore is highly unlikely to cause anticompetitive effects within China. Designation of these cases as "simple" may allow MOFCOM to review them quickly and without delay.

Section F of the Interim Regulations is not keyed to a China nexus, but instead provides that a transaction is a simple case if it is a "joint venture that is jointly controlled by two or more business operators [and] becomes controlled by one or more of them." This scenario also is unlikely to threaten competition and review may be expedited. This provision is also consistent with the original and proposed revision of the European Commission's Simplified Procedures.[16]

reviewed under the normal first phase procedure if there are possible coordinated effects of concern.

15 See, for example, David S. Evans and Vanessa Yanhua Zhang, The Qihoo v. Tencent Landmark Decision at 5, CPI, available at https://www.competitionpolicyinternational.com/the-qihoo-v-tencent-landmark-decision. This abuse of dominant position case based on bundling and vertical exclusionary practices was dismissed after trial on March 20, 2013. The article notes that "[d]ue to special market conditions of the internet industry, market share, in particular cannot be deemed as a decisive factor in the determination of a dominant position." This suggests that competitive harm is the overriding consideration, and relevant market definition may contribute to the analysis but is not an end in itself.

16 Former section 5d and revised section 5c provide that the simplified procedure will, in principle, be applied it "a party is to acquire sole control of an undertaking over which it already has joint control."

ARTICLE 3 – WHAT ARE NOT "SIMPLE CASES"?

Article 3 of the Interim Regulations provides that the status of "simple cases" is not available in six scenarios. The first, section A, excludes the concentration of horizontal joint ventures, that is, those which are "competitors in the same relevant market." It appears that Art. 2(A) treats horizontal mergers with low market shares as simple cases, while Art. 3(A) appears to deny that status to horizontal joint ventures regardless of their share of the relevant market. Article 3, Section B excludes concentrations where the relevant market is not easy to define. Since the prerequisite for granting simple case status in Art. (2)(A)– (C) is premised upon the market shares of the participating firms, this exclusion is consistent with the reliance upon shares of a relevant market in Art. 2.

The final three sections of this Article, (C), (D) and (E), appear to reproduce the substantive factors that guide merger analysis set forth in Art. 27 of the AML itself. These factors are: concentration may have a detrimental impact on "access [and/or] technological progress … on consumers or other relevant business operators … on national economic development" or other scenarios that MOFCOM finds may have "a detrimental impact on market competition." If a proposed transaction is entitled to characterization as a simple case, then it may be assumed that the concentration is unlikely to harm competition under any of these negative factors. However, the inclusion of the AML Art. 27 factors in the Interim Regulation may indicate that characterization of a concentration as a "simple case" nevertheless requires MOFCOM to engage in a full AML review.

ARTICLE 4 – WHEN MAY "SIMPLE CASE" STATUS BE REVOKED?

Finally, the Interim Regulation authorizes MOFCOM to revoke "simple case" status for three reasons. These factors include misrepresentations by the parties, information provided by third parties, or significant market changes. Art. 5 of the Interim Regulations is in accord with this section, providing that if any of the notifying parties conceals facts or provides false information then this activity is serious enough for civil or criminal sanctions under AML Art. 52. Penalties under the AML may range from 20,000 to 100,000 RMB fines (in serious cases) for individuals and 200,000 to 1 million RMB (in serious cases) for business entities, plus any applicable criminal penalties.

The second factor of Art. 4 introduces third parties into the determination of "simple case" status and provides simply that the status may be revoked if that party "asserts" that the concentration "would or may" harm competition and "produces evidence of the same." The Interim Regulation does not provide that a "simple case" decision will be published, so it is not clear how or when third parties would learn about the proposed transaction and sufficient specific details to produce evidence of threat to competition. Moreover, some courts are skeptical of third party objections, especially if the complaints come from competitors, concerned more about protection of competitors than protection of competition.

CONCLUSION: SOME QUESTIONS CONCERNING THE INTERIM REGULATIONS

How and When will Simple Case Status be Determined or Revoked?

As currently drafted, the Interim Regulation does not explain how MOFCOM will decide whether a concentration is a simple case or the timing of that determination. The Regulation does not address whether the notifying parties must affirmatively request classification of the concentration as a simple case, the format and supporting documents needed, or whether a request must be made at the time the notification is filed, before the Phase 1 investigation begins, or at any other time during MOFCOM's investigation.

Art. 3 lists six scenarios in which simple case status does not apply. However, the Interim Regulations do not indicate whether the decision under this article can be challenged by the parties to the concentration and, if so, what evidence would be relevant. It is not clear whether the decision to deny simple case status is to be made before Phase 1 or at a later time.

Finally, the Interim Regulations do not provide guidance on the timing or procedure for revocation of simple case status. Facts supporting Art. 4, sections A and C (misinformation or changed market conditions) could arise at any time during simple case proceedings, but it is not clear whether that status could be revoked after the concentration has been cleared. Further clarification would provide greater transparency to the parties.

What is the Effect of Simple Case Designation?

These Interim Regulations appear to indicate that MOFCOM intends to classify certain proposed concentrations as "simple cases" and apply a streamlined procedure to them. This procedure would be consistent with current practice in a number of jurisdictions and with the global consensus on efficient merger review. Specific guidance on the analysis of a simple case would allow parties to a concentration to provide whatever information is required, allow the simple case review to proceed in a timely and efficient manner and free MOFCOM to focus on notified cases that threaten to harm competition as defined in the AML.

MOFCOM Publishes Draft Merger Remedy Rules

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Since China's Anti-Monopoly Law (the "AML") came into effect in 2008, China's Ministry of Commerce ("MOFCOM") has adopted 18 conditional decisions requiring concessions from the companies concerned before their transactions could proceed. MOFCOM's remedy policy has attracted considerable attention among multinational companies, because MOFCOM's approach often differs from that of other antitrust authorities. The antitrust community thus eagerly awaited MOFCOM's first set of comprehensive rules on merger remedies.

MOFCOM's draft "Rules on Attaching Restrictive Conditions to Concentrations between Undertakings (Draft for Comment)" (the "Draft Rules"),[1] published on March 27, 2013, address a wide range of issues, including the design, implementation, monitoring, modification and waiver of merger remedies, as well as liability for breach. Unfortunately, the Draft Rules provide no guidance on the types of remedies MOFCOM prefers to address specific types of antitrust concern, in particular the unusual behavioral remedies MOFCOM has required in a number of recent cases. The Draft Rules also include a worrying new provision apparently allowing MOFCOM unilaterally to impose stricter remedies after the fact when it concludes that the originally approved remedies were insufficient.

Hopefully, MOFCOM's final rules will address the shortcomings in the Draft Rules. In past consultations, however, MOFCOM has tended to respond to criticism by deleting or shortening controversial provisions rather than by making significant substantive revisions. It seems likely, therefore, that the final rules will continue to leave significant questions unresolved.

1 *See* http://tfs.mofcom.gov.cn/article/as/201303/20130300068492.shtml.

I. BACKGROUND

The AML allows MOFCOM to impose remedies to lessen the negative impact of a concentration on competition (Article 29). Although MOFCOM has addressed merger remedies in prior rules and interpretations,[2] these measures do not provide a comprehensive framework. The Draft Rules are intended to provide the first set of comprehensive set of merger remedies rules under the AML. The Draft Rules reflect the input of experienced practitioners and scholars and other antitrust authorities consulted by MOFCOM, including during seminars in April and August 2012. Participants in the August seminar discussed an advance draft of the Draft Rules (the "August Draft"), which were more detailed in some respects than the Draft Rules.

In practice, MOFCOM appears to prefer behavior remedies over structural remedies, such as divestitures, which are generally favored by other global antitrust authorities. 15 of MOFCOM's 18 conditional decisions appear to involve behavioral remedies.[3] For example**,** MOFCOM imposed hold-separate requirements in three transactions (*Marubeni/Gavilon, Western Digital/Hitachi, and Seagate/Samsung*), delaying efficiency benefits from those transactions without addressing the identified concerns. The *Wal-Mart/Yihaodian* decision imposed behavioral remedies that appeared designed to further MOFCOM's foreign investment policy without articulating a clear theory of harm. In *Google/Motorola,* unlike other reviewing authorities, MOFCOM required behavioral remedies to address hypothetical concerns that were not "merger specific" and could have been addressed under other provisions of the AML. MOFCOM also used behavioral remedies in *Glencore/Xstrata and Uralkali/* ***Silvinit*** to lock in favorable commercial positions for Chinese customers, without a clear analysis of how such remedies addressed specific antitrust theories of harm.

II. KEY ISSUES IN THE DRAFT RULES

A. Types of Merger Remedies

The Draft Rules divide merger remedies into three types: (i) structural; (ii) behavioral; and (iii) hybrid (Article 5). Unlike the August Draft, the Draft Rules do not list specific examples of structural remedies or behavioral remedies.

Unlike the EU and the United States remedies rules, which state a clear preference for structural remedies, in particular divestitures, in connection with horizontal mergers, the Draft Rules provide no guidance on the

2 MOFCOM's Provisional Rules on Divestitures of Assets or Businesses to Implement Concentrations between Undertakings (the "Divestiture Rules"), adopted on July 5, 2010, deal with certain aspects of divestitures as merger remedies. MOFCOM's Examination Rules on Concentrations between Undertakings (the "Examination Rules"), Interpretation regarding Rules on Notification of Concentrations between Undertakings and the Examination Rules (the "Interpretation") and Provisional Rules on Examining Competition Effects of Concentrations between Undertakings (the "Competition Effects Rules") also contain general provisions on merger remedies.

3 Marubeni/Gavilon, ARM/G&D/Gemalto, Wal-Mart/Yihaodian, Google/Motorola, Henkel HK/Tiande/JV, Seagate/Samsung, GE/Shenhua JV, Uralkali/Silvinit, Novartis/Alcon, GM/Delphi and InBev/AB involved pure behavioral remedies. Four of MOFCOM's conditional clearance decisions (i.e., Gencore/Xstrata, Western Digital/Hitachi, Panasonic/Sanyo and Mitsubishi Rayon/Lucite) involved a combination of behavioral and structural remedies.

situations in which structural or behavioral remedies may be appropriate. The absence of any such guidance is perhaps the most disappointing aspect of the Draft Rules, given the uncertainty created by MOFCOM's remedy practice in recent years.

B. Submission of Proposed Remedies

The AML and existing rules and interpretations provide no clear mechanism for MOFCOM to inform notifying parties of the nature of concerns that should be addressed by remedies. The Draft Rules remedy this gap by stating that MOFCOM should identify and explain its competition concerns "***at an appropriate point***" (Article 7) and request that the notifying parties propose remedies within a specified period, though the parties may also propose remedies earlier (Article 8). Although this is a welcome clarification, it remains to be seen how early MOFCOM will be willing to identify its concerns and how specific MOFCOM will be. As parties are unlikely to propose remedies before MOFCOM identifies its concerns, MOFCOM should identify its concerns as early as possible.

The final remedy proposal must be submitted no later than 20 days before the last day of the review process (Article 11), which appears to set an outer limit of 160 days from MOFCOM's "acceptance" of a notification, ***i.e.,*** 20 days before the end of MOFCOM's extended Phase II review period. In practice, 20 days would likely be quite tight, especially if MOFCOM plans to market test the proposed remedies, as permitted by Article 10.[4]

The Draft Rules further provide that if the notifying parties do not propose remedies in the specified time period or do not propose remedies that are sufficient to lessen the negative impact of the concentration on competition, MOFCOM shall prohibit the concentration (Article 8). In practice, MOFCOM has suggested that parties withdraw and refile their notification to provide additional time.

The Draft Rules provide greater flexibility than the EU rules, which set out a detailed timetable for the submission of remedies in Phase I or Phase II and possible extensions of the Commission's review period where remedies are submitted late in the process.[5] Unlike the August Draft and the EU remedy rules, moreover, the Draft Rules do not provide a form to be used for remedy proposals or otherwise clarify the information parties need to provide. As a result, although the Draft Rules are helpful, MOFCOM's approach in a given case will likely continue to be difficult to predict.

C. Implementation

The Draft Rules' discussion of merger remedy implementation focuses mainly on divestitures, in particular the divestiture process and the criteria a buyer must satisfy to be deemed suitable. The Draft Rules also set out new procedures for the use of up-front-buyer or fix-it-first remedies or alternative "crown-jewel" divestitures.

4 The August Draft provided that MOFCOM could publish proposed remedies for public comment, as in the United States. This procedure is not reflected in the Draft Rules, though MOFCOM presumably would not be precluded from publishing proposed remedies.

5 See Article 10 of Council Regulation (EC) No 139/2004 of 20 January 2004 on the control of concentrations between undertakings.

1. Divestiture Process

The Draft Rules largely restate the Divestiture Rules regarding the divestiture process, but they make a number of clarifications and additions, in particular in relation to time periods. The Draft Rules clarify two distinct time periods in the so-called "self-divestiture" process. Unless otherwise stated in the decision, these are: (i) a six-month period (subject to extension by up to three months) for the notifying parties to find a suitable buyer and sign an agreement (Article 17); and (ii) a three-month period (subject to extension by up to one month) after the purchase agreement is signed during which the divestiture must be completed (Article 20). These periods are in line with the EU Commission's practice. US authorities more frequently require up-front divestitures and typically allow less time to complete approved divestitures, but under US law divestitures do not require separate merger approval.

2. Suitable Buyers

The Draft Rules are largely in line with the Divestiture Rules with regard to the requirements for suitable divestiture buyers: buyers must be independent of the parties, have the requisite resources and capability to run the business and receive all necessary governmental authorizations (Articles 15, 16, and 21). In line with EU rules and typical US practice, the Draft Rules (Article 15) add a requirement that the buyer not purchase the divested business by raising capital from the undertakings participating in the concentration. In addition, Article 21 adds that the transaction must receive clearance from MOFCOM if the transaction reaches the standard merger control notification thresholds. In the US, as noted, divestitures need not obtain a separate merger clearance.

3. Up-Front Buyers

In a standard "self-divestiture" process, the notified transaction may be closed immediately after MOFCOM issues its decision. The Draft Rules provide that MOFCOM may require that the divesting party find a buyer and sign the purchase agreement before implementing the notified transaction if (i) it will be difficult to maintain the competitiveness and marketability of the divested businesses before the divestiture; (ii) the identity of the buyer has a decisive influence on whether the divested business can restore competition in the market; (iii) there are very few qualified buyers for the divested business or it will be otherwise difficult to find a suitable buyer within the specified time limit; or (iv) MOFCOM identifies other circumstances requiring special treatment (Article 18).

Unlike the EU merger remedies notice, the Draft Rules do not distinguish between up-front buyer and "fix-it-first" remedies. In the EU, an up-front buyer remedy requires that the divesting undertaking commit not to close the underlying transaction until such time as binding agreements have been entered into with an approved buyer. In a "fix-it-first" remedy, the divesting undertaking commits to identify and enter into a binding agreement with an approved buyer before the review decision is adopted.[6]

6 See paras 50 and 53-57 of Commission notice on remedies acceptable under Council Regulation (EC) No 139/2004 and under Commission Regulation (EC) No 802/2004. It is noteworthy that "up-front buyer remedies" and "fix-it-first remedies" have different meanings in the United States.

4. Crown Jewel Provisions

The Draft Rules also introduce a "crown jewel" provision (Article 19), allowing MOFCOM to require the divesting party to sell an alternative set of assets should it prove unable to sell the original package. "Crown jewel" assets are typically designed to be more attractive to potential buyers to increase the certainty of completion.

The Draft Rules do not discuss the relationship between up-front buyer remedies and crown-jewel remedies. A crown jewel divestiture should presumably be used as an alternative to an up-front buyer divestiture, rather than in combination, since both are used to increase the certainty of implementation. Up-front-buyer divestitures are normally a more straightforward way to eliminate such uncertainty than crown jewel divestitures.

5. Behavioral Remedies

The Draft Rules state that MOFCOM's decision will set the duration for implementing behavioral remedies, but if the decision is silent, behavioral remedies shall apply for ten years (Article 13). In practice, the longest defined duration applied thus far appears to be eight years (*ARM/G&D/Gemalto and Glencore/Xstrata*).

D. Trustee and Ancillary Obligations

1. Trustees

The Draft Rules include the trustee mechanism introduced by the Divestiture Rules and often applied by MOFCOM. Monitoring trustees are responsible for monitoring the parties' compliance with their divestiture or behavioral remedy obligations, and divestiture trustees are responsible for executing a divestiture during a trustee-divestiture period (when a divesting party is unable to complete the divestiture itself) (Article 4).

The Draft Rules (Article 25) list the requirements for qualification as a trustee, all of which have been observed in MOFCOM's practice. However, the Draft Rules lack guidance as to how a trustee is selected and appointed.[7] In practice, MOFCOM appears to take a more intrusive approach in selecting trustees than the EU Commission.

The Draft Rules set up monitoring and punishment mechanisms for trustees (Article 28 and 35) to help ensure that trustees maintain their independence. These provisions may also discourage trustees from exceeding their mandates, but the Draft Rules do not mention this issue. The Draft Rules also prohibit monitoring trustees from disclosing to the parties any reports the trustees submit to MOFCOM.[8]

7 In the past, MOFCOM typically has asked the undertaking concerned to propose three trustee candidates, and MOFCOM then appoints one of the three as the trustee.

8 In EU practice, a redacted copy of such reports is shared with the undertaking concerned.

2. Ancillary Obligations

Articles 23 and 24 describe ancillary obligations of the merging parties in connection with divestitures, including preserving the competitiveness of the divested business, providing support to the trustee and providing transitional support to the buyer. These requirements are consistent with the Divestiture Rules and international merger remedy practice.

E. Modification and Waiver

The Draft Rules (Articles 30–33) include mechanisms allowing for the modification or waiver of remedies. Unusually, the Draft Rules indicate that merger remedies may be modified or waived not only at the request of the merged entity (Article 31), but also ***ex officio*** (Article 30). Article 30 indicates that MOFCOM may impose stricter remedies after the fact "***if the market competitive situation has changed to the extent that the restrictive conditions cannot lessen the negative impact.***" Article 32 of the Draft Rules provides that when evaluating an application to modify or waive remedies, MOFCOM should consider whether (i) the underlying transaction has significantly changed; (ii) the competitive landscape has substantively changed; or (iii) the public interest supports a modification or waiver.

MOFCOM's ability to impose stricter remedies than those agreed to by the notifying parties is worrying, in particular because the Draft Rules do not describe the criteria that MOFCOM must apply in such cases or provide procedural protections for interested parties. The Draft Rules do not set any time limit on MOFCOM's ability to impose stricter remedies.

F. Liability

The Draft Rules for the first time provide for sanctions for non-compliance with remedy commitments (Article 34), on trustees for providing false information or not fulfilling their responsibilities (Article 35) and on the buyers of the divested business for not abiding by the Draft Rules (Article 36).

For a serious breach of remedy commitments, MOFCOM will be able to enforce sanctions available under Article 48 of the AML, withdraw its review decision, and ask the undertakings concerned to re-notify the transaction. In less serious cases, MOFCOM shall require the parties to rectify their non-compliance within a specified time period. If a divesting party violates ancillary obligations rather than the obligation to complete a divestiture, Article 34 provides that MOFCOM shall order the divesting party to propose new remedies. In serious cases, MOFCOM shall withdraw the review decision and ask the undertakings concerned to re-notify the transaction.

The Draft Rules do not indicate what circumstances are considered "serious." Moreover, Article 34 of the Draft Rules is not consistent with Article 15 of the Examination Rules, which provides that if remedy obligations are not complied with, MOFCOM may establish a time limit for correction and take further actions in accordance with the AML if undertakings fail to make these corrections. It remains to be seen how these provisions will relate to each other in practice.

CONCLUSION

The Draft Rules provide a comprehensive framework and general guidance for the design and implementation of remedies in Chinese merger cases. These rules largely echo those of the United States and the EU and incorporate lessons from MOFCOM's existing conditional clearances.

As noted above, however, a number of issues are not addressed in the Draft Rules or need further clarification. For example, there is no specific timetable for MOFCOM to communicate its concerns, without which it would be very difficult for notifying parties to propose remedies. In the past, MOFCOM has sometimes identified its concerns late in its review, leaving little time to fashion suitable remedies. The absence of standard forms to be used when submitting proposed remedies also leaves uncertainty about the information that parties will be required to provide.

The Draft Rules also lack guidance on the role of monitoring trustees. The Draft Rules prohibit monitoring trustees from disclosing to the undertakings concerned any reports that the trustees submit to MOFCOM, although sharing non-confidential versions of trustees' reports and other submissions to MOFCOM would facilitate communications between notifying parties and monitoring trustees. In addition, it would be welcome if MOFCOM would confirm that it will monitor and review trustees' performance to ensure that trustees do not exceed their mandates or make unreasonable demands.

A surprising and worrying aspect of the Draft Rules is MOFCOM's ability to impose stricter remedies on the merged entity than those agreed to by the undertakings concerned, apparently without limit in time and with no clear procedural protections for the merged entity.

Perhaps most importantly, the Draft Rules provide no guidance on the forms of remedy MOFCOM prefers to address particular theories of harm. While it is not surprising that MOFCOM would want to avoid limiting its flexibility, MOFCOM's practice of applying non-standard merger remedies is a source of considerable concern to the business community. Greater clarity on this point would be greatly appreciated in the final rules.

State of Merger Control in India

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June 1, 2011 was the day India entered into the club of the countries having fully functional competition law.[2] After considerable speculation, doubts, oppositions and persuasions, carrying all the stakeholders together, India finally set in place a mechanism for reviewing the acquisitions, mergers and amalgamations (called 'combinations' under Indian law) from the perspective of competition law. Even after having been enacted in January 2003, on account of certain legal challenges, the enforcement provisions of the Competition Act, 2002 (Act) could not be brought into force in India till as late as May 20, 2009. Even after the commencement of enforcement of provisions relating to the prohibition of anticompetitive agreements and abuse of dominant position, the opposition to the complete implementation of competition law in India did not die down. The opposition was more from domestic constituents as they saw in it another layer of Government regulation which, to the extent possible, was better kept in abeyance.

The reasons for opposing merger review regime were varied. Starting from the speculation that the CCI would be sitting over merger clearances for a long time and thus delaying business transactions, to the claims that the CCI did not have a capacity to review complex mergers being a new competition agency, all types of conjectures and surmises were being thrown around with the sole objective that a fully functional competition agency does not come to existence in India. In any case, history shows that in any jurisdiction - be it the US, Canada or EU - competition law enforcement has not been welcomed with open arms by businesses to begin with. These oppositions had their impact. Despite the competition law becoming functional as early as May 2009, it took a little more than two years for merger control to come into existence. It was of no little help that the draft merger control regulations were already prepared, in-house by the CCI, and were ready to be tested on the ground. However, the fact that the Act had certain areas in need of improvement, harmonization and, in some cases, plain typographical error removal, efforts to stall the introduction of merger review into the country succeeded. There was even talk of first amending the Act before the provisions could be brought into force.

In early 2011, good sense prevailed and the proposal of bringing in amendments before the merger control provisions could be brought into force was shelved. Instead, the logical argument that amendments only be considered if faults were found with the Act as it existed. It was the result of this changed thinking within the Government of India that a beginning towards a fully-functional competition law regime in India could be made.

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2 Notification dated March 4, 2011 http://www.cci.gov.in/images/media/notifications/SO479%28E%29,480%28E%29,481%28E%29,482%28E%29240611.pdf

The CCI finally unveiled its final draft merger regulations to the world on May 11, 2011 after consulting a wide body of stakeholders including business houses, law firms, professional associations, business and industry chambers, consumer organizations and government departments. Despite grim warnings to the contrary, June 1, 2011 came and went without any earth-shattering obstructions to the normal peaceful existence to the business enterprises; It was business as usual. On the contrary, the international antitrust community welcomed[3] the performance of an Indian merger control regime.

Very soon, the CCI realized that some areas of the regime needed improvements. For example, the review machinery of CCI was avoidably clogged by a large number of intra-group merger filings, many of which did not change the control dynamics of enterprises. To ease the burden on businesses in these cases, the CCI relaxed the merger review format by amending the merger regulations so as to ensure that those merger filings that did not result in a change of control did not have to seek approval of the CCI. Similarly, the regulator noticed that harmony between the security regulator (SEBI) requirements and merger review by CCI could be further enhanced. This was done by suitably amending merger regulations. The highlights of the first amendments to the combination regulations, of February, 2012, by the CCI are as follows:

No requirement to file for merger review if the cumulative share purchase is below 25 percent (compared to the earlier 15 percent).

No filing requirement for intra-group mergers or amalgamations involving enterprises wholly owned by the group companies.

Acquisitions of shares or voting rights pursuant to buy backs and acquisition of shares or voting rights pursuant to subscription of rights issue (without the restriction of their 'entitled proportion'), not leading to acquisition of control, included in the list of transactions in Schedule I which lists transactions where a merger filing need not be made.

The Company Secretary of the company, duly authorized by the Board, was authorized to sign Form 1 or Form 2, in addition to those persons specified under the general regulations.

The distinction for filling up Part I for certain types of transactions and Part II for the remaining transactions was removed, leading to clarity and uniformity.

On gaining further experience, the combination regulations were amended once again by the CCI in April, 2013. The main changes were as follows:

No notice need be filed for acquisition of shares or voting rights of companies if the acquisition is less than five percent of the shares or voting rights of the company in a financial year, where the acquirer already holds more than 25 percent but less than 50 percent of the shares or voting rights of the company.

3 http://www.ibanet.org/Article/Detail.aspx?ArticleUid=73c4fdd7-9776-41cd-8fbb-3a7dd96c8c7c

Where one of the enterprises had more than 50 percent shares or voting rights of the other enterprise, filing of notice with CCI for mergers/amalgamations involving these two enterprises was not needed. Similarly, if more than 50 percent shares or voting rights in each of such enterprises are held by enterprise(s) within the same group, no notice was needed.

Some rationalization in the categories of exemption for acquisition of certain current assets like stock-in-trade, raw materials etc.

On completion, more than two years after the journey into a merger control regime began, it is the right time to look at the performance of the CCI in this vital area of competition law enforcement. When the final merger regulations were notified by the CCI, there was great excitement as well as doubts about the rules being laid down by the competition agency of India. There was a great curiosity about the CCI - especially for its capacity to deliver. Until that time, despite the commencement of provisions relating to anti-competitive agreements and abuse of dominance, the markets felt hardly any impact because of the matters before CCI. Compared to the performance of neighboring Pakistan where, right in the first 18 months of its existence, the CCP had showcased a considerable amount of work it did in exposing cartels and issuing government advisories, the performance of Indian competition agency was considered quite slow. Similarly, in another neighborly comparison, although the Act in India was enacted much earlier than China's, China enacted and brought into force its Anti Monopoly law much earlier than India. It also started merger control with a bang and the Coca-Cola case became a selling point for antitrust law in China. Perhaps an open and vibrant democracy has a price.

India opted for a mandatory filing regime. As of today, the thresholds for triggering the filing requirements are as follows:

<table>
<tr><th></th><th></th><th colspan="2">ASETS</th><th colspan="2">TURNOVER</th></tr>
<tr><td rowspan="2">In India</td><td>Enterprise</td><td colspan="2">INR 1,500 Crores (approximately USD 330 million)</td><td colspan="2">INR 4,500 Crores
(approximately USD 1 billion)</td></tr>
<tr><td>Group</td><td colspan="2">INR 6,000 Crores
(approximately USD 1,320 million)</td><td colspan="2">INR 18,000
Crores(approximately USD 4 billion)</td></tr>
<tr><td rowspan="4">In India
or
outside</td><td rowspan="2"></td><td colspan="2">ASETS</td><td colspan="2">TURNOVER</td></tr>
<tr><td>Total</td><td>India</td><td>Total</td><td>India</td></tr>
<tr><td>Enterprise</td><td>USD 750 million</td><td>INR 750 Crores
(approximately USD 165 million)</td><td>USD 2.25 billion</td><td>INR 2,250 Crores
(approximately
USD 500 million)</td></tr>
<tr><td>Group</td><td>USD 3 billion</td><td>INR 750 Crores
(approximately USD 165 million)</td><td>USD 9 billion</td><td>INR 2,250 Crores
(approximately
USD 500 million)</td></tr>
</table>

As would be obvious to any discerning eye, the Indian thresholds for merger filings are extremely high - perhaps the highest in the world. Interestingly, even the default merger filing form, Form 1, is also, perhaps, the simplest in the world. After having faced the severe criticisms for having a very burdensome filing form and low thresholds, prior to the commencement of enforcement of merger control in India, these may appear to be quite stark revelations to many.

Starting from June 1, 2011, till the end of June 2013, following number of merger cases has been reviewed by the CCI:

S.N.	Year	Reviews
1	2013 (till June, 2013)	28
2	2012	82
3	2011	13
	Total	**123**

Thus, starting from June 1, 2011 - a little more than two years since the commencement of merger review having come into force - a total of 123 cases of acquisitions, mergers and amalgamations have been reviewed by the CCI. There have been studies[4] indicating the average time it takes the CCI to review a merger as just over a fortnight – which is a relatively quick merger review clearance by any standards, especially for a new agency commencing operations in the midst of questions about its effectiveness.

So far, nearly all merger filings have been through the simple form - Form No 1. On account of the pressure of stakeholders, the first draft of merger regulations was made in such a way that the opponents of merger review did not get an opportunity to create unnecessary noise. The first form for merger filing was such that, effectively, it was almost discretionary to make a merger filing. This was due to the fact that even the most basic information about a transaction was to follow on the assertion of the merger-filing party that the transaction was not falling within some stated categories given in the schedule and the regulations. It was quite a big relief to businesses, but how helpful it was for competition assessment can be gauged from the fact that, despite being under no obligation to do so, nearly all the merger filings voluntarily included the details of the transaction, as well as the reason why it was not to cause an appreciable adverse effect on competition (AAEC - the substantive test for evaluation of mergers in India). Despite having a mandatory merger review regime, the first filing requirements practically gave the merger filer entire discretion on which form to choose: Form 1 or Form 2. Form 1 is minimalistic in the information sought; a large proportion of merger filings are through Form 1 only.

For all practical purposes, nearly everybody was using Form 1. The basic reason for introducing this was that any burden on business would have been used as a handle by the hawks amongst those opposing merger controls, leading to a further possible postponement of enforcement of merger control on different grounds. The cases filed through Form 2 could be counted not only on one's fingertips, but on a single finger. These were the only cases in which some horizontal overlap amongst products and services was admitted by the parties.

4 http://www.slashdocs.com/qispu/combination-review-in-india-a-mid-year-review-by-kk-sharma-part-1.html

Prior to these cases, in no case was any horizontal overlap between products and services either admitted or claimed by the CCI during the merger review.

A look at India's journey and progression of merger control enforcement shows a very slow movement. No doubt, the prompt clearances by the CCI, a laudable achievement, have been widely appreciated.[5] However, where do we go from here? Do we have similar glowing testimonials for an in-depth analysis and incisive dissection of the issues? One possibility may be that all the cases coming before the CCI really had no competitive concerns. But if we look at the Indian thresholds, nearly the highest in the world, wherein only the big ticket acquisitions, mergers and amalgamations come under the CCI scanner, the possibility of some cases containing issues that can only be dealt with through modification cannot be ruled out, if looked at carefully. The modification mechanism (called 'remedies' elsewhere) has not yet been tried and tested in full. However, there is a silver lining.

Gradually, the CCI is increasing the rigor of review. Except for giving plain approvals, there are some notable exceptions where the CCI examined the agreements in detail and directed some agreements to be amended to change some of the conditions considered anti-competitive. Two cases stand out: Orchid Chemicals and Pharmaceuticals Ltd. (Combination Reg. No. C-2012/09/79), and Mylan Inc. (Combination Reg. No. C-2013/04/116). In the case of Orchid Chemicals and Pharmaceuticals, the CCI observed *"non compete obligations, if deemed necessary to be incorporated, should be reasonable particularly in respect of (a) the duration over which such restraint is enforceable; and (b) the business activities, geographical areas and person(s) subject to such restraint, so as to ensure that such obligations do not result in an appreciable adverse effect on competition."*[6]

Similarly, in its order dated June 20, 2013, in the case of Mylan Inc. (Combination Registration No. C-2013/04/116), the CCI has accepted the modifications offered by the parties under regulation 19(2) of the combinations regulations. In both these cases, the CCI put into practice the provisions of Regulation 19(2) of the combination regulations. Under these regulations, the parties to the combination can come forward with modifications to the combinations on their own which may be accepted by the CCI. This is something similar to the undertakings in EU.

Another case stands out for comment: the notice for acquisition given by GSPC Distribution Networks Limited ("GDNL") to acquire Gujarat Gas Company Ltd. (GGCL) (Combination Registration No.: C-2012/11/88). In this case, an undertaking was taken from GGCL to modify the agreements of GGCL with its customers. Object of this exercise is not known. This kind of action is fascinating and sometimes questionable.

The question which arises is if one party is acquiring another enterprise, what is important: the possible future conduct, or the past conduct? If an agreement being routinely entered into with its clients comes to the knowledge of the CCI during a merger filing, should the CCI start examining it in addition to the review of merger filing? In merger control, it is the counterfactual (situation where the merger has not happened) which

5 http://www.ibanet.org/Article/Detail.aspx?ArticleUid=73c4fdd7-9776-41cd-8fbb-3a7dd96c8c7c

6 http://www.cci.gov.in/May2011/OrderOfCommission/CombinationOrders/C-2012-09-79.pdf

is important for evaluating the impact of a merger on competition in the market. If counterfactual does not show any adverse impact on the competitive environment for the product under question, is it alright to get entangled in side issues? Or ideally speaking, should such cases be dealt with in a different manner? Even if some compellingly anticompetitive practice comes to notice during merger review, should it be mixed with the job at hand or dealt separately? What the CCI did in this case was to allow the merger, but accept undertakings to modify the agreements.

However, it is noteworthy that the CCI has been able to prove all of its critics wrong by ensuring that even within the country, amongst various regulatory approvals, the approval from the CCI is almost invariably the first to come. This has certainly gone down well with businesses and has helped quell negative noise about the CCI becoming another government regulator delaying business transactions and raising the cost of business. On the whole it can be said that the CCI has generally had a good start on merger review. The importance of economic analysis has been well recognised and CCI is paying enough attention to this aspect. At least 40 percent of the CCI is made up of economists. This compares well with even the most mature antitrust jurisdictions. One thing can certainly be said: the CCI is not shying away from learning from experience. Until now, two significant amendments have taken place in merger regulations, both of which aimed at ensuring a more workable and practical merger control review in India. Having travelled safely so far, we wish the CCI *bon voyage* ahead.

Competition policy in Japan: sizing up the Takeshima era

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In 2012, Kazuhiko Takeshima concluded a ten-year term as Chairman of the Japan Fair Trade Commission. We take this opportunity to reflect on the development of Japan's competition policy during Takeshima's tenure. By way of introduction (Part I), we provide some food for thought about what is meant by a "competition culture" in the Japanese context. This rather broad (but unavoidably brief) introduction, in which we present the concept of "cultural hybridization," is included here because purely juristic discussions of Japanese competition policy that neglect such matters will generally yield only a thin understanding of complex dynamic forces. In Parts II and III, respectively, we then highlight the most positive achievements recorded over the last decade in Japanese antitrust, while noting our reservations where less progress has been made; and, we report on the newly installed leadership and developments on the horizon.

I. JAPANESE COMPETITION CULTURE BETWEEN "HARMONIZATION" AND COMPETITION

The idea of a "competition culture" is continually conjured but rarely defined. The core of the idea can perhaps be located, but its outer contours remain vague. We submit it could not be otherwise: a monolithic, universal competition culture is an unattainable mirage. Even the core of the idea is too often taken for granted; scholars should deconstruct it and debate which notions can realistically have universal portability. It seems to us that, at a minimum, to achieve a competition culture, certain presumptions have to be reversed. Instead of asking why rivalry should be embedded within a country's economic infrastructure, in a country with a competition culture people ask: what exceptional circumstances might there be that justify deviating from (dynamically defined) open and competitive markets? The more deeply ingrained competing paradigms are about, say, social solidarity or consensus (or the appearance thereof) and conflict-avoidance/resolution-through-harmony (the Confucian value of *wa*[1]), the more difficult it may be to reverse that original presumption (which holds that 'excessive competition', or maybe even competition *per se*, is a social evil). There are of course additional complications: different values that have been assigned different weights by different people – efficiency, "openness," competition-as-democracy, etc. But when one digs down to these essentially contested values, at this level portability starts to fade, unless perhaps the "competition culture" circulates among relatively homogeneous societies.

1 The Japanese word wa means "harmony." Its pervasive cultural significance stretches back well over a thousand years. Article I of the Constitution of 604 A.D. declared: "wa wo motte tōtoshi to nasu" ("harmony is to be valued").

Fortunately, it is probably unnecessary to achieve universal values at that level. For example, if there is common agreement that cartels are socially bad, different understandings of the reasons for their badness are unlikely to prevent shared, albeit more shallow, cross-cultural values.

Why so much here about culture? We agree with Thomas Cheng that culture is of great significance in the global sphere of competition policy and the globalized dialogue that comes with it.[2] Many scholars have considered Japan's distinctive cultural characteristics, and we don't have room here to enter into the subject. But to appreciate the important changes afoot in the last two decades, it is useful to recall Japan's point of departure, the so-called "harmonization" culture. This term refers not just to relations between people but also to business relations. In some sense, ***wa***-based "harmonization" is antithetical to both rivalry (where, on a micro level, one's gain is another's loss) and litigation (which eschews more humble notions of mediation and forgiveness). Small wonder that the antitrust transplant of 1947 could not be tolerated in its original form by the host body.[3]

In the Japanese context, the idea of a "competition culture" has not displaced the country's harmonization culture (and maybe could not do so), but the absorption of the idea has triggered a process of cultural hybridization.[4] Each of these cultural orientations is diluted to some degree but the resulting blend (which will continue to develop over decades) is becoming the relevant variety of competition culture for Japanese society and Japanese business operators.

It is implicit in the foregoing introduction that Japan has been going through a period of cultural change (hybridization), and the seeds of change were sown in the 1970s. For reasons of space we limit our remarks to the recent past (i.e., the "Takeshima era") and the foreseeable future.

II. TAKING STOCK

1) Achievements of Mr. Takeshima

The greatest achievements in Japanese competition policy over the past 10 years can be summarized as: (i) stronger enforcement of the Antimonopoly Act (Law No. 54 of 1947, as amended); (ii) increased international cooperation; and (iii) greater alignment of procedures with those of competition agencies overseas. More concretely, with regard to (i), i.e., stronger enforcement, the most significant

2 Cheng, "How Culture may Change Assumptions in Antitrust Policy", in Ioannis Lianos and D. Daniel Sokol, eds., The Global Limits of Competition Law, Stanford University Press, 2012, chapter 13.

3 Several historical accounts discuss the initially radical antitrust measures imposed during the Allied occupation, and their progressive softening once Japan regained its sovereign independence in April 1952 by virtue of the San Francisco Peace Treaty. See, e.g., Mitsuo Matsushita, International Trade and Competition Law in Japan, Oxford University Press, 1993.

4 This perspective builds on but deviates from the idea that there is room for just one culture in a given community (here the Japanese business and public communities), and that one culture lays siege to another until the other is driven out and replaced. This dichotomous view of culture is a rather natural assumption and is reflected, for example, in Akinori Uesugi, 'Where Japanese Competition Policy is Going – Prospect and Reality of Japan', speech at Fordham Law School, 7 October 2004, pp. 2-3.

reform was arguably the amendment of the AMA in 2005, which introduced a leniency program for the first time. Since then, a remarkable 623 leniency applications have been filed with the JFTC. Another change that enhanced the power of the agency was the conversion of the administrative hearing procedure to an ***ex post*** hearing system. In addition, while the JFTC strictly enforced the AMA to expose price-fixing and bid-rigging cartels during the Takeshima era, emphasis was also placed on enforcement of the prohibition of abuse of a superior bargaining position (ASBP) and on stopping violations of the Subcontract Act.[5] In November 2010, the JFTC established a task force in the investigation division to focus on ASBP cases. As of this writing, more than 90 cases have led to an administrative warning from the JFTC, and three administrative surcharge payment orders have been imposed.

As for (ii), international cooperation, one of the authors has been involved in a number of international cartel cases in which the JFTC coordinated with the US Department of Justice and with EU's DG Competition more and more frequently than ever before. To our knowledge, although it coordinates with agencies overseas, the JFTC does not appear to be sharing the evidence and testimony obtained through its investigations with them; however, under the AMA it may be authorized to do so. When the JFTC begins to exchange information as a routine practice, this will drastically change the landscape of antitrust investigations in Japan. But the JFTC has already begun to expand the global reach of its enforcement activities, actively applying the AMA to cases involving (only) foreign firms, a chief example of which is the failed business combination between BHP Billiton and Rio Tinto.[6]

As regards (iii), i.e., the JFTC's attempts to achieve greater procedural interoperability with other jurisdictions, the JFTC abolished the notorious prior consultation procedure in merger control, whose opaque features had long been criticized by many Japanese businesses. Although the JFTC submitted a bill to abolish another procedure that has drawn criticism, i.e., ***ex post*** administrative hearings, the bill languished in the Diet while Japan turned its attention to the Fukushima nuclear accident and subsequent debate over whether to suspend operation of the country's nuclear power plants.

Perhaps less obviously, during Takeshima's era the interpretation of the AMA has been advanced as a result of challenges brought against the JFTC's decisions. Many appeals have been filed with the Tokyo High Court, and thereafter to the Supreme Court. The Supreme Court's judgment of February 20, 2012 in a bid-rigging case is a recent and important example. In this case, the Court held that:

(a) it was the underlying ("fundamental") agreement that amounts to an unreasonable restraint of trade;

(b) since the fundamental agreement is defined as forming a consensus as to who will win the anticipated

5 The stated purpose of the Subcontract Act (originally enacted in 1956 and amended several times) is "to ensure that transactions between main subcontracting entrepreneurs and subcontractors are fair and, at the same time, to protect the interests of the subcontractors, thereby contributing to the sound development of the national economy."

6 Japan Fair Trade Commission, Termination of Prior Consultation Process regarding establishment of a joint venture for producing iron ore by BHP Billiton PLC and BHP Billiton Limited, and Rio Tinto PLC and Rio Tinto Limited (18 October 2010).

bid and its final price, it is obvious that the business activities of each undertaking are thereby restricted, and consequently the necessary condition (where an unreasonable restraint of trade is alleged) of a "mutual restriction" is satisfied; and

(c) an administrative surcharge should be applied to cases where the undertaking designated to accept the order as a result of coordination based on the fundamental agreement does accept it, since, in this case, the business activities of undertakings are found to be restricted and competition is substantially restrained.

The judgment just described does much to clear up some longstanding points of obscurity as regards the proper interpretation of the AMA.

2) Doubts

While Mr. Takeshima deserves praise for his significant achievements, certain aspects of the JFTC's practice in the last decade can be criticized. For example, while the JFTC has strengthened the enforcement of the AMA, its investigators have not always held themselves to adequate standards of due process. It has to be recalled that the JFTC's investigators are career bureaucrats steeped in an administrative culture. They are not qualified lawyers. Most of them spend their entire professional life at the JFTC. They are deeply loyal to their employer but few of them have had the opportunity to internalize respect for due process through personal experience. In Japan it is a well-known fact that, when interrogating witnesses, JFTC agents have given short shrift to due process, and witness statements are taken with little regard for legal guarantees familiar in other jurisdictions. This unsatisfactory state of affairs has not been touched upon at all during Mr. Takeshima's mandate.

In terms of substance, neither the enforcement of the prohibition of "private monopolization" nor the policy behind it has received attention during the Takeshima era. These issues have essentially been eclipsed by the much greater emphasis on cartels and on the abuse of a superior bargaining position.

3) A 'balance sheet'

Just ten years ago, the JFTC still could not shake loose its "sleeping dog" reputation. The enforcement of the AMA focused predominantly on domestic bid-rigging. There was hardly any action in the areas of price-fixing cartels and international cases. Mr. Takeshima tore up this placid picture, revitalized the institution and began coordinating with overseas competition agencies and modernizing much of the JFTC's enforcement policy. As we have noted, the JFTC still faces several challenges going forward. Nevertheless, under Mr. Takeshima's leadership the JFTC has exceeded expectations and it is poised, for the first time in its six-decade history – if left free from political tragicomedy – to leave its dysfunctional past behind for good.

III. LOOKING AHEAD

The new JFTC Chairman, Kazuyuki Sugimoto, took office on March 5, 2013. Due to the political confusion already mentioned, and due in part to concerns about the fact that Mr. Sugimoto was from the Ministry of Finance, it took almost five months for the Diet to confirm him. Mr. Sugimoto's career background was similar to that of Mr. Takeshima in the sense that he built his career as a top-level bureaucrat at the Ministry of Finance, serving as vice-minister there from July 2008 until July 2009. Under the Yoshiro Mori cabinet, from 2000 to 2001, Mr. Sugimoto was a senior adviser to the prime minister, and he made significant contributions to the reform of the pension system in 2004. As for competition policy, Mr. Sugimoto served as first secretary of Japan's Mission to the European Economic Community from 1988 until 1991, where he was able to observe the administration of EEC competition policy and to learn about its distinctive characteristics. At the press conference held for his inauguration on March 5, 2013, Mr. Sugimoto stated his belief that, without competition, there could be no economic growth – a note of continuity with the messages of the last decade.

Mr. Sugimoto also made clear that his leadership focus would be on: (i) rigorous enforcement of the AMA; (ii) active enforcement of the Subcontract Act and other regulations such as those on the abuse of a superior bargaining position to protect small- and medium-size businesses; and (iii) improved antitrust compliance and the prevention of bid-rigging.[7] In addition, he emphasized the importance of international coordination. While these goals were already pursued under Takeshima's administration, Sugimoto's administration is expected to devote more effort and resources to achieve them – although it is unclear where the additional resources will come from. As if to drive the point home, the very next week (March 13, 2013), the JFTC conducted a dawn raid involving no less than 50 undertakings for the suspicion of fixing prices for underground cable. This was followed on March 27, 2013 by another raid of more than 10 domestic construction firms on suspicion of bid-rigging.

Under Sugimoto the JFTC resubmitted the bill to amend the AMA on May 24, 2013. This bill would abolish the *ex post* hearing procedure for antitrust cases in favor of what is perceived to be a more transparent system designed to (i) give companies suspected of anticompetitive behavior more of a chance to defend themselves before the JFTC issues cease-and-desist orders, and (ii) change the jurisdiction for competition appeals to the Tokyo District Court. Despite the political shift from the former Democratic Party of Japan (Noda's administration) to the Liberal Democratic Party (Abe's administration), the reform of the hearing procedure is still strongly supported by Japanese business communities. Although the regular session of the Diet closed on June 26, 2013, the bill is being deliberated during the official closure period so that it can be adopted with a minimal delay during the next legislative session.

7 Japan Fair Trade Commission, Taking Office as the Chairman of the Japan Fair Trade Commission (March 2013).

Developments in Criminal Enforcement of Competition Law in Korea

Hee-Eun Kim[1]

I. KOREA'S NEW PRESIDENCY AND COMPETITION LAW ENFORCEMENT

On December 19, 2012, Korea elected Ms. Park Geun-hye to lead a new government for the next five years. Not only is Ms. Park the first woman president of Korea, she is also the daughter of former president Park Chung-hee. Mr. Park is regarded as the driving force of the remarkable economic growth through the 1960s and 70s, the period which began the *per capita* increase in Korea's nominal GDP from US $100 in 1962 to more than US $22,000 in 2012.

While the "pie" has grown enormously in only half a century, economic and social issues from the rushed industrialization and unequal distribution of wealth pose challenges to Korea's future growth. Hence, a balance between "economic democratization" and continued expansion tops President-elect Park's agenda of economic and industrial policies. As part of these policies, she has pledged to facilitate fair and transparent competition among large- and small-sized enterprises and to protect underdogs in the market. Notably, she has proposed reform of the enforcement framework for the Monopoly Regulation and Fair Trade Act ("the MRFTA") and related laws, including:

amending provisions in the MRFTA which currently provide that only the Korea Fair Trade Commissions ("the KFTC"), a government agency responsible for public enforcement of competition law, can refer criminal offenses of the MRFTA to the Prosecutor's Office, Korea's public prosecutors;

introducing "collective redress" and expanding the availability of "punitive damages" to encourage private enforcement; and

adopting a number of provisions related to corporate governance of business conglomerates.

It is still early to predict how the proposals will ultimately be implemented, but the new presidency appears poised to improve the landscape of Korea's competition law enforcement. While each of the above three topics is important, this short piece focuses on the first, namely a possible change to the criminal enforcement

1 Attorney at Covington & Burling LLP Brussels Office. The views expressed in this article are the author's, and should not be construed as reflecting those of the firm or its clients. Thanks are due to Lars Kjølbye and Nancy Brohn for their comments.

framework which currently grants the KFTC exclusive power to submit criminal offenders of the MRFTA to the Prosecutor's Office. The background, institutional issues, and more substantive components of criminal enforcement and deterrence are briefly explored.

II. OVERVIEW OF COMPETITION LAW ENFORCEMENT IN KOREA

The KFTC commonly employ administrative sanctions for enforcing competition law. Corporate offenders may be subject to a "surcharge" of up to 10 percent of the "relevant" sales, and to corrective measures such as cease-and-desist orders.

Competition law offenders are also liable for private damage compensation, except when they prove the absence of intent or negligence on their part (Article 56 of the MRFTA). Victims of a competition law offense do not have to await the outcome of pending KFTC proceedings in order to bring a private damage lawsuit. Still, private enforcement is rarely used in Korea. In order to facilitate such enforcement, the KFTC is considering ways to support consumer groups bringing private damage actions.

Criminal sanctions can be imposed on corporate offenders (including directors and employees) as well as individuals. Notably, Article 66 of the MRFTA provides for a jail term of a maximum of three years and/or a criminal fine of up to KRW 200 million (approximately 140,000 Euros) for offenses concerning abuse of market dominance, merger control, cartel, and certain restrictions on business conglomerates. Article 67 of the MRFTA provides for a jail term of a maximum of two years and/or a criminal fine of up to KRW 150 million (approximately 106,000 Euros) for less serious offenses, such as unfair trade practices, resale price maintenance, and anticompetitive cross-border agreements. Articles 68 through 70 of the MRFTA set forth further details on criminal sanctions.[2] Prosecuted cases so far have been concluded with criminal fines, without imprisonment yet.

III. THE KFTC'S EXCLUSIVE POWER TO MAKE A REFERRAL TO THE PROSECUTOR'S OFFICE

While the KFTC imposes administrative measures, criminal sanctions are up to the Prosecutor's Office. However, the Prosecutor's Office cannot initiate such sanctions on its own. According to Article 71(1) of the MRFTA, it can do so "only after a complaint is filed by the [KFTC]."

The competition authority's exclusive power to refer to criminal prosecution was included in the MRFTA enacted in 1980, on the rationale that a competition law violation has "distinguishable characteristics" compared to other criminal violations.[3] In other words, violation of competition law is an economic crime that requires a robust analysis of legal and economic impact and the KFTC is deemed best suited to undertake such task.[4] In 1995, the Constitutional Court of Korea considered whether this exclusive referral power infringed the right to

2 An English translation of the MRFTA is available at http://eng.ftc.go.kr.

3 Id. (discussing that it can also "enhance effectiveness of the leniency program by inducing suspects to cooperate in KFTC investigations").

4 For similar reasons, Korea's National Tax Services (NTS) has exclusive authority to refer certain tax law violations to the Prosecutor's Office.

equality and the right of access to courts. The Court upheld the KFTC's exclusive role but also observed the need for balance:

"For effective enforcement and deterrence of anticompetitive conduct, administrative sanctions such as a corrective measure or a surcharge alone are not sufficient, and it is necessary to make use of criminal sanctions which have strong effect of psychological coercion. […] However, there is a concern that reckless criminal enforcement may chill business activity, and such a consequence achieves neither 'promoting fair and free competition' nor 'encouraging business activity.' Therefore, if possible, criminal sanctions against anticompetitive conduct should be limited to a case where the offense is so obvious that its impact on our economy and consumers is significant […]. The purpose of granting the KFTC exclusive authority to file a criminal referral is to achieve the goal of the MRFTA by allowing the KFTC to independently examine anticompetitive conduct through detailed market analysis […] and, depending on the market conditions of the relevant period, to regulate anticompetitive behavior only by administrative measures."[5] (unofficial translation)

Reflecting the Court's ruling, the following checks and balances were subsequently introduced:

The KFTC's exclusive power is limited by Article 71(2) of the MRFTA which provides that "[i]f necessary, the [KFTC] shall file complaints together with the Prosecutor General for cases involving the offenses listed in Articles 66 and 67 [of the MRFTA] because the violation is deemed gross and considerable it may substantially suppress competition." In this regard, the KFTC adopted a set of guidelines on the types and criteria of cases subject to a mandatory referral to the Prosecutor General;[6] and

The Prosecutor General can notify the KFTC of the existence of a potential criminal offense and request the KFTC to make a referral in such circumstances (Article 71(3) of the MRFTA).

As shown in **Table 1**, the KFTC made referrals to the Prosecutor's Office in 491 out of the total 56,527 cases the KFTC handled from 1981 to 2010.[7] Some criticized the low percentage (0.9%) of referrals to the Prosecutor's Office, although it should be noted that the KFTC is obliged to process all cases filed with it. The total number of cases (56,527) includes many involving relatively minor offenses which would not normally be referred to the Prosecutor's Office. If the scope were limited to illegal cartel cases from 1981 to 2010, the ratio would rise to 44 out of 504 (11%).[8]

5 Cho v. KFTC, Constitutional Court of Korea Case No. 94 HeonMa 136 (July 21, 1995), page 8.

6 KFTC, KFTC Guidelines on the Referral of Violations under the Monopoly Regulation and Fair Trade Act, KFTC Guidelines No. 140 (as amended as of August 20, 2012). A Korean version of the Guidelines is available at http://ftc.go.kr.

7 KFTC, Statistical Yearbook of 2010, page 32, available at http://eng.ftc.go.kr.

8 Jaeho Moon, KFTC, Cartel Enforcement Regime in Korea, GCR Law Leaders Asia-Pacific 2012 (March 2, 2012), available at http://eng.ftc.go.kr.

Table 1. Number of KFTC Cases by Measures

	Referral to Prosecutor's Office*	Corrective Order	Corrective Recommendation	Request for Correction	Fine	Warning or Voluntary Correction	Mediation	Others	Total
'81~'90	23	685	310	0	0	307	0	22	1,347
1991	10	169	70	0	0	301	0	21	571
1992	8	145	31	0	0	304	28	92	608
1993	7	220	59	3	0	341	90	189	909
1994	13	207	110	5	0	307	87	200	929
1995	33	199	119	3	0	414	118	229	1,115
1996	16	250	179	4	0	454	152	481	1,536
1997	35	221	330	9	0	600	133	825	2,153
1998	37	535	57	5	1	465	183	836	2,119
1999	11	621	149	4	4	356	126	867	2,138
2000	22	441	35	0	43	356	121	652	1,670
2001	23	347	84	4	52	3,352	71	735	4,668
2002	11	497	110	5	107	1,858	48	711	3,347
2003	18	449	102	2	91	2,011	30	835	3,538
2004	22	478	100	1	159	2,191	38	957	3,946
2005	12	756	163	0	81	2,306	32	949	4,299
2006	47	644	178	1	70	2,411	35	1,052	4,438
2007	48	928	124	0	78	1,938	108	1,256	4,480
2008	33	737	76	1	146	1,954	236	1,364	4,547
2009	43	486	85	0	53	2,225	311	1,461	4,664
2010	19	277	66	0	42	1,419	302	1,380	3,505
Total	491	9,292	2,537	47	927	25,870	2,249	15,114	56,527
Ratio	0.9%	16.4%	4.5%	0.1%	1.6%	45.8%	4.0%	26.7%	100%

Source: KFTC Statistical Yearbook of 2010, page 32

*Note: The number of the referrals to the Prosecutor's Office includes not only the referrals made under the MRFTA but also those under other related laws concerning unfair labelling and advertising, subcontract, etc. For example, only 4 out of the total 19 referrals in 2010 were brought pursuant to the MRFTA.

IV. CHALLENGES TO THE KFTC'S EXCLUSIVE REFERRAL POWER

Despite the introduced improvements in institutional checks and balances, the KFTC still faces criticism that its exclusive referral power should be further limited. In the wake of several recent domestic cartel cases, critics argue that criminal enforcement must be pursued vigorously to increase the level of deterrence. Pointing to the 'low' percentage of referrals, they claim that one way to strengthen such enforcement is to limit the KFTC's exclusive referral power so that more criminal cases can be pursued through other routes. Without the KFTC's exclusive referral power, victims of a competition law offense could file a complaint directly with the Prosecutor's Office or the latter could itself launch an investigation and prosecute offenders.[9]

9 A 2007 attempt by the Prosecutor's Office to prosecute competition law offenders without the KFTC's referral was challenged in court.

The KFTC raises a number of counterarguments: first, the percentage of criminal referrals (as noted, 11%) is in fact relatively high in comparison with other OECD member countries; second, as the Constitutional Court noted, the KFTC is best placed to perform economic analysis of harm and to assess whether anticompetitive conduct is "gross and considerable"[10] so that criminal sanctions must be sought; and third, as most cartel activities are revealed through leniency applications, it is important to maintain incentives to apply for leniency. (Currently, the KFTC does not make a criminal referral against successful leniency applicants.) If the Prosecutor's Office were to start pursuing criminal charges against leniency applicants, it could become challenging to manage the leniency program.[11]

V. THE RELATIONSHIP BETWEEN THE KFTC AND THE PROSECUTOR'S OFFICE: LESSONS FROM THE UK?

Limiting the KFTC's referral power is likely to increase the influence of the Prosecutor's Office over competition law enforcement. In terms of institutional design, the relationship between the UK Office of Fair Trading ("the OFT") and the Serious Fraud Office ("the SFO") - the UK's public prosecutors for serious or complex fraud except in Scotland - may provide useful guidance. After criminal sanctions against criminal cartel activity were introduced in 2002,[12] the OFT and the SFO agreed a Memorandum of Understanding (MOU) setting out the basis for their cooperation. In relation to criminal referrals, this MOU provides that:[13]

- If the OFT receives information that criminal cartel activity may have occurred, the OFT will undertake any necessary initial criminal enquiries. If the SFO receives information suggestive of criminal cartel activity "prior to any related referral from the OFT," the SFO will first forward such information to the OFT so that the OFT can perform any necessary initial criminal enquiries (Paragraph 3);

- If, upon the initial check (and informal discussions with the SFO), the OFT identifies a criminal cartel case possibly falling within the SFO's ambit, the case will be referred to the Director of the SFO (Paragraph 4);

- If the SFO accepts the OFT's referral, a criminal case team will be formed consisting of both SFO and OFT officials under the leadership and direction of an SFO case controller (Paragraph 6);

10 Article 71(2) of the MRFTA.

11 *E.g.*, The Aju Business, Interviews with Mr. Joong Weon Jeong (KFTC) on July 10, 2012 available at http://eng.ajnews.co.kr/view.jsp?newsId=20120710000011 and on July 29, 2012 available at http://japan.ajnews.co.kr/view.jsp?newsId=20120710000010, both in Korean.

12 Section 188 of the UK Enterprise Act 2002 imposes a maximum of five years' imprisonment and/or unlimited fine for individuals who "dishonestly" engage in prohibited cartel activities such as price-fixing, limiting supply or production, market-sharing, or bid-rigging.

13 Memorandum of Understanding between the Office of Fair Trading and the Director of the Serious Fraud Office (October 2003), OFT 547, available at http://www.oft.gov.uk/shared_oft/business_leaflets/enterprise_act/oft547.pdf. In this respect, the OFT also has published several guidelines: e.g., OFT, Powers for Investigating Criminal Cartels: Guidance (January 2004); and OFT, The Cartel Offence: Guidance on the Issue of No-Action Letters for Individuals (April 2003), both available at http://www.oft.gov.uk.

• The SFO makes a decision to cease SFO-led cartel investigations or to prosecute offenders in consultation with the OFT (Paragraph 14).

The MOU provides further arrangements between the SFO and the OFT on case team composition, decision-making during investigations, dispute resolution within the case team, and leniency.

It is noteworthy that the OFT appears to play an essential role in performing initial enquiries to determine whether criminal cartel activity requires the SFO's involvement. Also, somewhat similar to the way in which the KFTC's exclusive referral power functions, private prosecutions can be submitted only with the OFT's consent.[14]

VI. A FEW THOUGHTS BEYOND INSTITUTIONAL DESIGN

Kovacic and Hyman observe that, while multiple enforcement bodies serve "distinct purposes," multiplicity also has its "costs." They note that the risks associated with an institutional change can be reduced if a "process of patient experimentation, reflection, and benchmarking" is followed.[15] In the context of the announced reform of Korea's competition law, such a process could productively look beyond the institutional aspects to also examine the substantive components of criminal enforcement, including review of the penal provisions under Korean competition law (notably, Articles 66 and 67 of the MRFTA).

Such broader examination could cover a range of related issues. While criminal sanctions in many jurisdictions primarily target hardcore cartel offenses such as bid-rigging, the penal provisions in the MRFTA apply to almost any type of anticompetitive conduct, including minor violations. Has the broad scope of these provisions contributed to deterrence? Furthermore, the limited level of criminal sanctions actually imposed may well have undermined such deterrence. While the law provides for a maximum three-year jail term and/or a criminal fine of up to KRW 200 million (approximately 140,000 Euros), the criminal fines charged to individuals so far have not exceeded KRW 10 million (approximately 7,100 Euros), apart from the absence of imprisonment so far. Finally, it would probably make sense to balance any changes to the current criminal enforcement system with the benefits of the leniency program.

14 Section 190 of the UK Enterprise Act 2002.

15 William E. Kovacic and David A. Hyman, Competition Agency Design: What's on the Menu?, GWU Legal Studies Research Paper No. 2012-135; GWU Law School Public Law Research Paper No. 2012-135, (November 21, 2012), available at SSRN: http://ssrn.com/abstract=2179279.

COMPETITION POLICY IN ASIA

Essays on Recent Development

2011
2012

Revisiting China's Merger Control
Where Are We Going After the Three-Year Milestone?

Xinzhu Zhang &

Vanessa Yanhua Zhang*

I. INTRODUCTION

After thirteen years of incubation, the Chinese government eventually enacted the Anti-Monopoly Law (hereinafter AML), yet at a time when China's economy was still in transition from a centrally planned economy to a market economy. Discussion of China's experience in antitrust is important in at least two respects. On the one hand, as a country with newly established antitrust regimes, its experience will certainly contribute to the understanding of antitrust issues among antitrust agencies in other jurisdictions all over the world. On the other hand, and perhaps more importantly, due to the unique experience that China has achieved remarkable economic successes in the absence of a comprehensive competition law, it will contribute to both policy and academic debates clarifying whether antitrust has any role to play in promoting economic development.[1] Similarly to the competition laws in other jurisdictions,

the AML consists of three bodies of substantive legal rules against monopolistic/collusive agreements, abuse of dominance conduct, and anticompetitive merger and acquisitions. However, while it has been three years since the AML came into effect, on 1 August 2008, its enforcement has developed slowly and unevenly. Merger control is probably the most advanced enforcement area. For example, several hundreds of cases have been completed by the Anti-Monopoly Bureau of the Ministry of Commerce (MOFCOM), China's merger review agency, and several high-profile cases have been decided. Thus, it may be more valuable to review the enforcement of AML with a focus on merger control. As the cases have accumulated and more decisions have been released, it is a good time to take stock and revisit the question: where are we going after the three-year milestone?

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1 See T. S. Ulen, "The Uneasy Case for Competition Law and Regulation as Decisive Factors in Development: Some Lessons from China", in M. Faure & X. Zhang (eds.), Competition Policy and Regulation: Recent Developments in China, the US and Europe, Edwards Elgar Publishing, Cheltenham, 2010.

In a previous paper, published in 2010[2], we have discussed the patterns of China's merger control policy and tried to provide some implications on what we could look forward to. Since its publication, there have been some new developments in the merger control policy in China. To begin with, many new cases have been reviewed. According to MOFCOM,[3] from 1 August 2008 to the end of December 2011, it has completed merger reviews of 382 cases, with seventeen cases in 2008, 80 in 2009, 117 in 2010 and 168 in 2011. Among those 382 completed cases, 371 were cleared by MOFCOM without any condition, which account for 97% of the total number of closed cases. Ten cases were approved with conditions and one was blocked, which account for 3% of the total. From analyzing those case decisions, we find that although the rules and provisions of China's merger control policy are largely consistent with those of other jurisdictions such as the US and the EU, MOFCOM takes its own approach to reviewing mergers and making decisions.

The rest of this article is organized in the following way: Section 2 analyzes the merger review regulations; Section 3 discusses the eight cases that were released during the period September 2009-June 2011.[4] Section 4 provides a preliminary analysis of those cases. In Section 5 we try to shed some light on the patterns and implications of China's merger control policy and Section 6 concludes the discussion.

2. RECENT REGULATIONS ON MERGER REVIEWS

2.1 The Market Definition Guidelines

In terms of regulations and rules for implementation of the AML, the Competition Commission of the Chinese State Council issued the first antitrust guidelines, i.e. The Guidelines on the Definition of Relevant Market (the Market Definition Guidelines), on 7 July 2009.[5] The Guidelines incorporate and integrate some concepts and principles from the horizontal and non-horizontal merger guidelines issued in other jurisdictions, such as the US and the EU. As usual, they also contain certain Chinese characteristics. They also bear some similarity to the US Horizontal Merger Guidelines, released by the US Department of Justice and Federal Trade Commission on 19 August 2010 (the 2010 US Horizontal Merger Guidelines),[6] and the EU Horizontal Merger

2 See X. Zhang & V.Y. Zhang, "Chinese Merger Control: Patterns and Implications", 6 Journal of Competition Law and Economics 2, 2010, pp. 477-496.

3 See X. Zhang, "Antitrust Cases Grow in China since the Anti-Monopoly Law Took Effect", Xinhua News 21 September 2011, available at <www.gov.cn/jrzg/2011-09/21/content_1953353.htm>. See also MOFCOM Press Release, "MOFCOM Held a Press Conference on 2011 Review of Antitrust Enforcement", 31 December 2011, available at <http://english.mofcom.gov.cn/aarticle/subject/cv/lanmua/201112/ 20111207909371.html>. MOFCOM Press Release, "MOFCOM Held a Press Conference on the Interim Measures for Investigating and Publishing of Concentration of Undertakings Failing to File Notification", 10 January 2012, available

4 For the discussion of the cases that were released during August 2008 and August 2009, please refer to another article written by us: Zhang & Zhang 2010.

5 See the State Council of People's Republic of China Press Release, The Guidelines on the Definition of Relevant Market, 7 July 2009, available at <www.gov.cn/zwhd/2009-07/07/content_1355288.htm>.

6 The revised 2010 US Horizontal Merger Guidelines are available at <www.justice.gov/atr/public/guidelines/hmg-2010.html>.pdf. In this respect, the OFT also has published several guidelines: e.g., OFT, Powers for Investigating Criminal Cartels: Guidance (January 2004); and OFT, The Cartel Offence: Guidance on the Issue of No-Action Letters for Individuals (April 2003), both available at http://www.oft.gov.uk.

Guidelines.[7] The guidelines were issued by the Competition Commission of the State Council rather than any of the three antitrust enforcement agencies. This implies that these guidelines are applicable not only to merger review but also to investigation of monopolistic agreement and abuse of dominance conduct. This treatment is similar to the approach in both the US and the EU and has the advantage of coherence in dealing with different types of cases. However, the Market Definition Guidelines fail to mention the caveats applying to different types of cases, for example, the benchmark price issue that was caused by pre-merger market power. It thus casts a shadow on how to solve such technical problems in case investigation in order to avoid important issues, such as the Cellophane Fallacy.

2.2 The Interim Rules

Two years after the Market Definition Guidelines were announced and one year after the US released the 2010 Merger Guidelines, MOFCOM published *the Interim Rules on the Assessment of Competitive Impacts of Concentrations of Undertakings* (the Interim Rules), which took effect on 5 September 2011.[8]

The Interim Rules provide the road map on how MOFCOM will assess mergers or other concentrations under the AML. The Interim Rules possess several notable features. First, the Market Definition Guidelines and the Interim Rules have been treated with different legal approaches. The former were issued by the Competition Commission of the State Council as guidelines, whereas the latter were enacted by MOFCOM as regulatory rules. Second, Article 4 of the Interim Rules states that two types of competition harms for horizontal mergers will be considered: the unilateral effect and the coordinate effect. Such an approach is similar to those in the US and the EU. In addition, Article 4 states that competition harm for non-horizontal mergers will also be taken into account. From this perspective, one may conclude that China's approach to assessing competition effects of non-horizontal mergers is closer to that of the EU than to that of the US, where competition effects for non-horizontal mergers are obviously downplayed. However, there is one major difference between the Chinese and the European approaches: in the EU, a higher standard of proof for non-horizontal mergers is explicitly required, which is consistent with modern economic theory. In China, however, the issue of standard of proof for non-horizontal mergers is not mentioned explicitly. This might cause more non-horizontal mergers to be blocked or approved with remedies if lower standards of proof were imposed.

3. RECENT CASES

As we have mentioned in the introduction, three cases that were closed between August 2008 and August 2009 have been discussed in one of our previous articles, namely InBev/Anheuser-Busch, Mitsubishi Rayon/Lucite, and Coca-Cola/Huiyuan.[9] We will thus cover mainly the eight cases that were closed during the period September 2009-December 2011. Those eight cases include GM/Delphi, Pfizer/Wyeth, Panasonic/Sanyo, Novartis/Alcon, Uralkali/ Silvinit, Alpha V/Savio, and GE/Shenhua Joint Venture.

7 See EU Horizontal Merger Guidelines, available at <http://eur-lex.euro pa.eu/LexUriServ/LexUriServ.do?uri=CELEX: 52004XC0205%2802%29:EN:HTML>.

8 See MOFCOM Notice No. 55 [2011], Interim Rules on Assessment of Competitive Impacts of Concentrations of Undertakings, 29 August 2011, available at <http://fldj.mofcom.gov.cn/aarticle/zcfb/201109/ 20110907753173.html>.

9 See Zhang & Zhang 2010.

3.1 GM/Delphi

On 18 August 2009, the US auto manufacturer, General Motors (GM) notified MOFCOM of its proposed acquisition of the US auto parts producer, Delphi. In fact, Delphi used to be a part of GM but divested away and became a fully independent publicly held corporation in 1999 in the midst of globalization and specialization in the industry. Since then, GM's parts purchase from Delphi has reduced sharply from 80% to about 11% in 2008, although Delphi has continued to be GM's largest parts supplier. One special feature about this merger case is that Delphi has been in bankruptcy protection since 2005 because of industrial slowdown and rising costs.

MOFCOM released the case decision on 28 September 2009.[10] MOFCOM took the position that both Delphi and GM were the leading firms in the relevant markets. However, the term "market dominance" was not used and no information on market structure was available. Because of the merging parties' influence in each relevant market, MOFCOM was concerned mainly about the vertical foreclosure of various Chinese auto manufacturers brought about by the reconstructed vertical relationship post-merger and the fact that Delphi was the major supplier for them. MOFCOM was also worried that market entry might be more difficult for other Chinese auto parts suppliers to deal with GM after the merger.

Eventually, MOFCOM imposed behavioural remedies that GM/Delphi should continue to supply Chinese auto manufacturers on a non-discretionary basis and should not exchange confidential information related to any third party; they should cooperate with its customers to facilitate the switch to other auto parts suppliers; GM's purchase should be diversified and GM should be non-discriminatory when purchasing auto parts from other suppliers.

3.2 Pfizer/Wyeth

On 9 September 2009, the US pharmaceutical giant Pfizer submitted its notification for approval of its proposed acquisition of another US pharmaceutical company, Wyeth. In fact, this merger was proposed at a time when the pharmaceutical giants around the world were all facing a similar problem of expiration of their major patented drugs. For example, Pfizer's most popular drugs in terms of prescription volumes, the anti-hypertension and anti-anginal drug, Norvasc, the allergy treatment medicine, Zyrtec, and the anti-cancer drug, Camptosar, had all expired in 2008. In addition, its star drug, Lipitor, the cholesterol lowering drug, was also due to expire in 2010. Similarly, Wyeth's major patented drugs, the anti-depressant, Effexor, and the anti-high blood pressure drug, Protonix, were to expire soon. Under these circumstances, the consolidation was one of the important means of strengthening the firm's financial position. In fact, post-merger, Pfizer-Wyeth would become the largest pharmaceutical company in the world.

On 29 September 2009, MOFCOM conditionally approved the global acquisition of Wyeth by Pfizer.[11] Interestingly, instead of following other jurisdictions' lead, the decision was made ahead of approval from the US

10 See MOFCOM GM/Delphi Decision, Notice No. 76 [2009], 28 September 2009, available at <http://fldj.mofcom.gov.cn/aarticle/ztxx/ 200909/20090906540211.html>.

11 See MOFCOM Pfizer/Wyeth Decision, Notice No. 77 [2009], 29 September 2009, available at <http://fldj.mofcom.gov.cn/aarticle/ztxx/ 200909/20090906541443.html>.

Federal Trade Commission, Australian ACCC and the Canadian Competition authority. The main competition concern centred on the swine mycoplasmal pneumonia vaccine business. Indeed, MOFCOM was worried about the post-merger market share of the two companies (49.4%) and increased market concentration (post-merger HHI 2182, ΔHHI = 336). In fact, it is one of the few cases where more detailed information on the relevant market structure was released. Meanwhile, MOFCOM considered there to be a significant entry barrier problem. Therefore, MOFCOM ordered the divestiture of Pfizer's swine mycoplasmal pneumonia vaccine business.

3.3 Panasonic/Sanyo

MOFCOM received the notification of the proposed acquisition of Sanyo Electric Co. (Sanyo) by Panasonic Corporation (Panasonic) on 21 January 2009. The two Japanese companies were major international producers of electronics products, and China was the major manufacturing base for both Sanyo and Panasonics. Their product lines included many kinds of consumer electronics with famous brands. To a great extent, the two Japanese companies had overlapping product lines. But the chief strength of Panasonic was in consumer electronics, and Sanyo was the world leader in various types of new energy cells such as solar cells, fuel cells and chargeable cells. The consolidation would strengthen Panasonic's competitiveness in solar cells and make it the world leader in R&D in new energy cells on the whole.

MOFCOM cleared this case with conditions on 30 October 2009.[12] Interestingly, it is one of the released cases that have entered Phase III. MOFCOM's antitrust review focused on three lines of products: highly concentrated button batteries, civil batteries, and vehicle batteries, which were defined as relevant product markets.

MOFCOM revealed that post-merger, the merging parties would have combined global market shares of 61.6%, 46.3% and 77% in the relevant markets, respectively. Based on this market share information, MOFCOM concluded that the relevant markets were highly concentrated and that the merging party would cause competition harm by raising prices unilaterally. MOFCOM ordered substantial business divestiture in all three markets: (1) for button batteries, Sanyo should divest all its business to an independent third party; (2) for civil batteries, MOFCOM let the merging parties decide whose business would be divested but that divestiture of one party's business would be sufficient; and (3) for vehicle batteries, since Panasonic and Sanyo had high market shares and were essentially the only two firms in this market, Panasonic was, in addition to business divestiture, ordered to reduce its shareholding in Panasonic EV Energy Co. (PEVE), a joint venture between Panasonic and Toyota, from 40% to 19.5% in order to maintain competition in this market. Besides, to reduce its control of the joint venture by Panasonic, it should also waive its voting rights at PEVE's Shareholders Meeting, its right to appoint directors to the Board, and veto power regarding PEVE's battery business.

3.4 Novartis/Alcon

On 20 April 2010, MOFCOM received notification from the merging parties of the proposed acquisition of Alcon by Novartis, both Swiss pharmaceutical companies.[13] In fact, Novartis was the seventh largest pharma-

12 See MOFCOM Panasonic/Sanyo Decision, Notice No. 82 [2009], 30 October 2009, available at <http://fldj.mofcom.gov.cn/aarticle/ ztxx/200910/20091006593175.html>.

13 In fact, it was only the second step of the acquisition agreement between Novartis and Nestle signed in April 2008.

ceutical company globally while Alcon, owned by the giant food producer, Nestle, was the largest producer of eye-care products in the world. Again, the merging transaction was proposed at a time when Novartis was facing the thorny problem of the expiration of its patented drugs and increasing competitive pressure from generic drug producers. Indeed, the consolidation was consistent with the worldwide trend of diversification in the pharmaceutical industry. Meanwhile, Nestle's decision to sell Alcon was reflective of its moving in the direction of focusing on its competitive strength – food production.

MOFCOM conditionally cleared the proposed acquisition on 13 August 2010, just a day before the end of Phase II.[14] MOFCOM found that the proposed acquisition would raise anti-competitive concerns in the ophthalmological anti-infective, anti-inflammatory/antiinfective combinations market and in the contact lenses care products market. It seemed that this conclusion was largely based on the relevant market share information. Indeed, in the ophthalmological anti-infective, antiinflammatory/ anti-infective combinations market, Alcon's market share in China, which was likely to be the geographical market mainly because of international transfer pricing, a common practice in the pharmaceutical industry, was over 60%, although Novartis had less than 1% of the market share in China.[15] Interestingly, Novartis demonstrated its strategic decision to exit the global market as well as the China market. However, MOFCOM did not consider this strategic plan sufficient to ensure future market competition. It thus ordered that Novartis cease sales of its ophthalmological anti-infective, anti-inflammatory/anti-infective combinations under current brands in China and not sell such products under the same or different brands in the Chinese market for the following five years.

In the contact lenses care product market, MOFCOM showed that the combined market shares of Novartis and Alcon would be 60% globally and 20% in China post-merger. MOFCOM also revealed that Novartis had a distribution agreement with the largest contact lenses manufacturer, Hydron Contact Lens Co. Ltd. (Hydron), the largest seller and producer in China, whose production accounted for over 30% of the contact lenses care market in China. MOFCOM was worried that this agreement would facilitate post-merger coordination between Novartis/Alcon and Hydron on price, quality and sales territories of contact lenses care products. Therefore, Novartis was ordered to terminate its distribution agreement with Hydron within twelve months after the decision was released.

3.5 Uralkali/Silvinit

The proposed acquisition of Silvinit by Uralkali, the two major potash fertilizer producers and the world's leading exporters based in Russia, was filed with MOFCOM on 14 March 2011. Both are vertically integrated companies with control of the whole production chain, from potash ore mining to supply to ultimate consumers,

As the first step, Novartis bought 25% of Alcon's shares in the second half of 2008. Novartis would acquire 52% more shares of Alcon from 1 January 2010 to 31 July 2011. But for the acquisition in the first step, the merging parties may not need to notify the antitrust agency for antitrust review because it may not constitute a merger.

14 See MOFCOM Novartis/Alcon Decision, Notice No. 53 [2010], 13 August 2010, available at <http://fldj.mofcom.gov.cn/aarticle/ztxx/ 201008/20100807080639.html>.

15 Globally, although there is no market share information on individual firms, the combined market share post-merger would be 55%.

and China was one of the main export markets. Interestingly, this case raised the keen attention of observers of China's antitrust enforcement because of the extraterritorial jurisdiction issue involved. Indeed, the case decision was released in the midst of a heated debate over this complicated issue when the proposed acquisition of the Rio Tinto Group (Rio Tinto) by Broken Hill Proprietary Billiton Ltd. (BHP Billiton), two of the three largest iron ore producers and exporters based in Australia, was announced and discussed.

On 2 June 2011, MOFCOM released a conditional approval of this merger case.[16] This paved the way for the extraterritorial enforcement of the AML. MOFCOM defined the relevant product market as potassium chloride with a global geographical market. MOFCOM found that the potassium chloride market was highly concentrated simply because its production was controlled by a few big companies. Indeed, more than 80% of the global reserves were held by the top three producing countries. The merged company, Uralkali/Silvinit, would emerge as the second largest exporter of potassium chloride with over a third of the global market. In addition, the combined global market share of the top two companies would be over 70%. Moreover, until recently China had been highly dependent on the international potassium chloride market with over 50% of the importation of potassium chloride depending on Uralkali/Silvinit or their associated companies.

The increased concentration post-merger raised MOFCOM's concerns on the Uralkali/Silvinit's increased market power through the ownership of more potassium resources and stronger production capacity in the wake of increasing demand from China and other booming economies. MOFCOM was at the same time concerned about the anti-competitive coordination between the fewer suppliers remaining in the global market. Meanwhile, MOFCOM identified that barriers to entry into the potassium chloride market would be high due to the scarcity of exploitable potassium reserves and massive assets and time required to expand the existing facilities or to explore new mines. Eventually, MOFCOM proposed a behavioural remedy and ordered the Uralkali/ Silvinit to continue providing the whole range of potassium chloride products to its Chinese clients in sufficient quantities, to maintain the current sales method and process as well as customary negotiation procedures by taking into account the historical and current trading situation with its Chinese clients and the characteristics of the Chinese market. It further stipulated that a monitoring trustee be appointed by the merged party to ensure compliance with the commitments and report to MOFCOM on their implementation.

3.6 Alpha V/Savio

On 14 July 2011 MOFCOM received notification of the acquisition of Savio Macchine Tessili S.p.A. (Savio), an Italian textile manufacturer, by Penelope S.r.l. (Penelope), wholly controlled by Alpha Private Equity Fund V (Alpha V). MOFCOM officially initiated Phase I review on 5 September 2011.

The focus of the competition analysis fell into a narrowly defined product market – the "auto-winder electronic yarn clearer market". As the wholly controlling shareholder of acquirer Penelope, Alpha V holds 27.9% of the shares in Uster Technologies Ltd. (Uster). Meanwhile, Loepfe Brothers Ltd. (Loepfe) is the wholly owned

16 See MOFCOM Uralkali/Silvinit Decision, Notice No. 33 [2011], 2 June 2011, available at <http://fldj.mofcom.gov.cn/aarticle/ztxx/201106/ 20110607583288.html>.

subsidiary of the target company, Savio. According to MOFCOM, both Uster and Loepfe are the only two manufacturers in the world of automatic winder electronic yarn clearers. Their global market shares in 2010 were 52.3% and 47.7%, respectively. Their shares of the Chinese market were quite similar.

On 31 October 2011, MOFCOM conditionally approved the acquisition.[17] It was concerned about the possibility that the two competitors, Uster and Loephe, may coordinate their business activities via Alpha V post-merger, which in turn would restrict and eliminate competition in the relevant market. Meanwhile, MOFCOM analyzed market entries and found that there existed substantial entry barriers for new participants due to capital and R&D investments. Therefore, MOFCOM ordered Alpha V to divest its shares in Uster to an independent third party within 6 months after the decision and refrain from participating in or influencing Uster's operations and management before the divestiture was completed. The whole divestiture process shall be supervised by a monitoring trustee appointed by Alpha V.

3.7 GE/Shenhua Joint Venture

On 13 April 2011, MOFCOM received notification of formation of a joint venture between GE China and Shenhua, a state-owned enterprise (SOE). The proposed transaction was initially announced in January 2011.[18] MOFCOM officially started the Phase I review on 16 May 2011. With two extensions, one on 15 June and the other on 13 September, MOFCOM finally announced its decision on 10 November 2011, almost at the end of the Phase III review. In this proposed transaction, GE China and Shenhua are to establish a 50/50 joint venture (JV) to license coal-water slurry (CWS) gasification technology to industrial and power projects in China. GE Infrastructure Technology, a subsidiary of GE, will provide GE's CWS gasification technology to the proposed JV. Meanwhile, Shenhua is the largest supplier of the coal used for gasification and also possesses businesses such as electricity generation, rail and port transportation, coal chemical engineering, etc. This JV will integrate GE's technology and experience and Shenhua's coal resource.

MOFCOM cleared the proposed JV with conditions on 10 November 2011.[19] It was worried that the CWS gasification technology licensing market is highly concentrated, within which GE Infrastructure Technology and another two Chinese institutions are major players. Among the top three players, GE's market share is the highest. Meanwhile, MOFCOM investigated the upstream market and found that CWS gasification technology requires specific raw coal, which makes operation of CWS gasification technology heavily dependent on supply of such raw coal. In fact, MOFCOM identified Shenhua as the largest supplier of raw coal in 2010, though no market share information was provided. In particular, it was unclear whether Shenhua had a dominant position in the relevant market of the specific coal for CWS gasification technology. MOFCOM was thus concerned

17 See MOFCOM Alpha V/Savio Decision, Notice No. 73 [2011], 31 October 2011, available at <http://fldj.mofcom.gov.cn/aarticle/ zcfb/201111/20111107809156.html>.

18 See GE Press Release, "GE and Shenhua Announce Formation of Cleaner Coal Technology Joint Venture in China", 18 January 2011, available at <www.genewscenter.com/Press-Releases/GE-and-Shenhua- Announce-Formation-of-Cleaner-Coal-Technology-Joint-Venture-in- China-2ddd.aspx>.

19 See MOFCOM GE/Shenhua Decision, Notice No. 74 [2011], 10 November 2011, available at <http://fldj.mofcom.gov.cn/aarticle/ zcfb/201111/20111107824342.html>.

about the vertical competition effect; in other words, that the merged party may foreclose its competitors by taking advantage of its market position in the supply of the specific coal. In addition, MOFCOM conducted entry analysis and found entry barriers to the CWS gasification technology market are quite high due to technological complexity, intellectual property rights and long R&D and industrialization cycle.

Eventually, MOFCOM issued behavioral remedies and ordered the JV partners not to require customers to use only the JV technology, or not to increase the cost of using competing technologies by either limiting the supply of specific raw coal or by imposing conditions on the coal supply. Interestingly, this was the first joint venture case that has received serious antitrust review and was approved conditionally.

3.8 Seagate/Samsung

On 12 December 2012 MOFCOM imposed conditions on the Seagate/Samsung merger.[20] The review of the merger was initiated on 13 June 2011 after the draft notification was first submitted to MOFCOM on 19 May 2011. After an in-depth investigation and consultation with external experts, MOFCOM concluded that the Seagate/Samsung merger would cause competitio harm owing to anti-competitive coordinated effects. In the competition analysis, MOFCOM stated that the reduction in the total number of competitors would have enabled the remaining competitors to coordinate their conduct in the particular circumstances of the market. Given the relatively high market concentration with five players worldwide, where Seagate's market share was 33%, Western Digital's 29%, Hitachi's 18%, Toshiba's 10% and Samsung's 10%, MOFCOM found that the product, namely hard disk drive (HDD), is homogeneous and market competition transparent.

MOFCOM then imposed behavioural remedies on the proposed transaction. It ordered the merging parties to maintain Samsung HDD as an independent competitor, set up an independent subsidiary to price and market Samsung's products and build a Chinese wall to avoid information exchange between Seagate and the Samsung subsidiary competitor. Meanwhile, Seagate should increase its capacity to produce Samsung HDD within 6 months after the decision and not change its current business model or force its customers to purchase exclusively from Seagate or its affiliates. Moreover, Seagate should not require TDK (China), an independent supplier, to supply HDD heads to Seagate and its affiliates on an exclusive basis, or restrict TDK's supply to other producers. Seagate should promise to invest at least US $800 million each year during the next 3 years to promote innovation and benefit customers with more innovative products and business solutions. MOFCOM also ordered Seagate to appoint a trustee to monitor compliance.

4. PRELIMINARY CASE ANALYSIS

In the merger cases that MOFCOM released, there are horizontal and non-horizontal mergers. Although horizontal and non-horizontal mergers seem to be treated similarly in the Interim Rules,[21] economic theory and

20 See MOFCOM Seagate/Samsung Decision, Notice No. 90 [2011], 12 December 2011, available at <http://fldj.mofcom.gov.cn/aarticle/ zcfb/201112/20111207874274.html>.

21 See the Interim Rules, supra note 8.

practices in other jurisdictions suggest that the fundamental problems with these two types of mergers differ and that the standards of proof are also different. Therefore, we discuss these mergers separately.

4.1 Horizontal Mergers

Under the AML, the legal principle for merger review is to evaluate whether a merger may restrict or exclude competition, which is consistent with international practice. [22] However, since many important implementing rules in the Market Definition Guidelines and the Interim Rules are simply too vague, the enforcement has some Chinese characteristics.

4.1.1 Market Definition

In most cases, MOFCOM had a clear definition of relevant product markets. For example, in the cases of Pfizer/Wyeth,[23] Panasonic/Sanyo[24] and Novartis/Alcon,[25] multiple relevant product markets were defined. As to the relevant geographical markets, however, MOFCOM was not always clear. In the Pfizer/Wyeth[26] case, for example, MOFCOM clearly defined China as the geographic market. But in the case of Novartis/Alcon,[27] it was not clear whether the world market or China was defined as the relevant geographic market.

An interesting question is, what has been the main approach that MOFCOM has used to define relevant markets? From the information released, it seems that MOFCOM has depended mostly on a qualitative economic approach, which is to analyze demand and supply substitutability, as required in the Market Definition Guideline.[28] For example, there is no indication that they have ever used the Critical Loss Analysis, a common method to implement the SSNIP test in many jurisdictions, or more generally, the quantitative economics approach, to define relevant markets.

4.1.2 Market Power

Market power is the pre-condition for any merger to create competition harm. The AML and the Interim Rules have specified the legal principles to infer marker power. But they fail to provide detailed rules on how to implement in practice. This would definitely leave some legal uncertainties.

Indeed, market share is one of the most important calibrations that have been used by MOFCOM in the merger reviews. In particular, MOFCOM is more concerned with market shares that are close to or over 50%. In

22 See the US Horizontal Merger Guidelines, and the EU Horizontal Merger Guidelines, supra notes 6 and 7.

23 See MOFCOM Pfizer/Wyeth Decision, supra note 11.

24 See MOFCOM Panasonic/Sanyo Decision, supra note 12.

25 See MOFCOM Novartis/Alcon Decision, supra note 14.

26 See MOFCOM Pfizer/Wyeth Decision, supra note 11.

27 See MOFCOM Novartis/Alcon Decision, supra note 14.

28 See Art. 4 of the Market Definition Guidelines, supra note 5.

the Pfizer/Wyeth[29] merger, for example, MOFCOM found that the combined post-merger market share of Pfizer and Wyeth would be 49.4% in the swine mycoplasmal pneumonia vaccine market (Pfizer 38%, Wyeth 11.4%), which is considered significantly higher than that of their nearest rival Intervet (18.35%) and other individual competitors (less than 10%). With such a post-merger market share, MOFCOM was worried that the merging parties would have the ability or the market power to expand the market and unilaterally raise the price.[30]

Besides market share, MOFCOM has also taken into account market concentration as another important calibration of market power. For example, in the Pfizer/ Wyeth[31] merger, MOFCOM released the post-merger HHI 2182 and the change of HHI pre- and post-merger ΔHHI 336. With this market concentration information, MOFCOM concluded that the swine mycoplasmal pneumonia vaccine market in China is highly concentrated and that this proposed transaction would have an anti-competitive effect.

The use of market share and concentration seems to establish the legal approach for MOFCOM to presume market power. But since there are no safe harbours specified in the Interim Rules, one may wonder what has been the basis for MOFCOM to treat this information in practice. One possibility is that they might have used the benchmarks from other jurisdictions such as the EU and the US.[32] Another possibility is that they might have used the market share thresholds in Article 19 of the AML, which is used to assess abuse of dominant conduct. But this raises the question whether the same standard of proof for presuming market power should be adopted for these different types of anti-competitive conduct. Besides, one may wonder how the rebuttal process, if there is any, would be carried out in practice.

4.1.3 Competition Effects

The Interim Rules stipulate in Article 4 that two types of competition harm will be considered for antitrust review of horizontal mergers.[33] These are the unilateral effect and the coordinate effect. Such legal rules are consistent with economic theory and international practice. However, the Interim Rules were silent on whether there is any difference in the assessment of these two types of competition harm. In particular, they failed to specify how to assess the unilateral effect in a differentiated product market. For example, the Interim Rules gave no indication whether the diversion ratio should be emphasized in addition to market share and concentration information.

29 See MOFCOM Pfizer/Wyeth Decision, supra note 11.

30 Id.

31 Id.

32 In EU, the Commission would not identify horizontal competition concerns "in a market with a post-merger HHI below 1,000". It would not identify horizontal competition concerns "in a merger with a postmerger HHI between 1,000 and 2,000 and a delta below 250, or a merger with a post-merger HHI above 2,000 and a delta below 150", except certain special circumstances listed. See Arts. 19-20 of the EU Horizontal Merger Guidelines, supra note 7. In the US, antitrust enforcement agencies would consider mergers resulting in an unconcentrated market, i.e. HHI below 1,500, "are unlikely to have adverse competitive effects and ordinarily require no further analysis". See the 2010 US Horizontal Merger Guidelines, supra note 6.

33 See Art. 4 of the Interim Rules, supra note 8.

In the horizontal merger cases, MOFCOM was concerned about the presence of unilateral price and/or non-price effects. As analyzed previously, MOFCOM has to presume this type of competition harm based mainly on market share and/or concentration information. But one problem might be that it has placed undue emphasis on post-merger market share or concentration ratio instead of the change of market structure. In the Novartis/Alcon[34] case, for example, although Novartis had a market share of over 60% in China's ophthalmological anti-infective, anti-inflammatory/anti-infective combinations market, Alcon's market share was only less than 1%. In other words, the merger would not cause lessening of competition in this market due to Alcon's negligible market share.

In the cases of Novartis/Alcon[35] and Uralkali/Silvinit,[36] however, MOFCOM was worried about not only unilateral effect but also coordinate effect. In particular, MOFCOM considered only the coordinate effect in the contact lenses care products market in the Novartis/ Alcon[37] case, but was concerned about both types of competition effects in the Uralkali/Silvinit[38] case. In considering coordinate effect, it seems that MOFCOM has depended largely on the combined share of the two or three largest firms. However, from the information released by MOFCOM, it was not clear whether the market would become not only more concentrated but also more symmetric.

4.1.4 Counter-Factors to Market Power

Even though market share and concentration information have been used to presume market power and competition harm, counter-factors to market power were also considered, perhaps to a lesser extent.

4.1.4.1 Entry

In all cases, MOFCOM has conducted a brief entry analysis. In general, MOFCOM focused on industrial specifics such as contractual relationship (GM/Delphi[39]), economies of scale (GM/Delphi[40]), switch costs (Panasonic/Sanyo[41]), intellectual property rights (Pfizer/ Wyeth[42], Panasonic/Sanyo[43], Novartis/Alcon[44] and Alpha V/

34 See MOFCOM Novartis/Alcon Decision, supra note 14.

35 Id.

36 See MOFCOM Uralkali/Silvinit Decision, supra note 16.

37 See MOFCOM Novartis/Alcon Decision, supra note 14.

38 See MOFCOM Uralkali/Silvinit Decision, supra note 16.

39 See MOFCOM GM/Delphi Decision, supra note 10.

40 Id.

41 See MOFCOM Panasonic/Sanyo Decision, supra note 12.

42 See MOFCOM Pfizer/Wyeth Decision, supra note 11.

43 See MOFCOM Panasonic/Sanyo Decision, supra note 12.

44 See MOFCOM Novartis/Alcon Decision, supra note 14.

Savio[45]), monopoly of natural reserves (Uralkali/ Silvinit[46] and GE/Shenhua[47]) etc., to assess whether there were significant entry barriers. The interesting question seems to be: although the Interim Rules have specified the principles to conduct entry analysis,[48] which emphasize that entry must be possible, timely and sufficient, why have there not been specific rules on how to implement these principles? In particular, it is unclear what constitutes the standard of proof for the presence or absence of significant entry barriers.

4.1.4.2 Buyers' Power

MOFCOM also considers buyers' power in merger reviews to assess whether it will outweigh the increased market power caused by the proposed mergers. For example, in the Panasonic/Sanyo merger, MOFCOM found that buyers' power is not strong enough to offset the anti-competitive effect.[49] Although some large downstream users may have bargaining power while dealing with the merged entity, the countervailing effect cannot be extended to small and medium-sized users who do not possess such power.

4.2 Non-Horizontal Mergers

For non-horizontal merger reviews, two issues are particularly important. One is higher standard of proof required in comparison with horizontal merger reviews. The other is consistency between review of non-horizontal mergers and investigation and prosecution of abuse of dominance conduct. Compared with other jurisdictions such as the US and the EU, it seems that MOFCOM has been more concerned with competition harms of non-horizontal mergers. Indeed, the only case that has been blocked so far, i.e. the Coca-cola/ Huiyuan[50] merger, involved portfolio effects in conglomerate merger. And in several vertical merger cases with conditional approval, MOFCOM has focused on foreclosure effects.

Even though there are not many details in the Interim Rules, MOFCOM has mainly followed the way the European Commission deals with non-horizontal mergers. In reviewing vertical mergers, MOFCOM often considers foreclosure effect as the major competition harm. This effect may emerge in upstream or downstream industries depending on market power of the relevant merging parties in the production chain. Again, the key point is that foreclosure effect must be created by vertical mergers themselves.

In the GM/Delphi[51] merger, for example, MOFCOM found that Delphi was the exclusive auto parts supplier to many domestic Chinese automakers, which were competitors of GM. This exclusive supply relationship and

45 See MOFCOM Alpha V/Savio Decision, supra note 17.

46 See MOFCOM Uralkali/Silvinit Decision, supra note 16.

47 See MOFCOM GE/Shenhua Decision, supra note 19.

48 See Art. 7 of the Interim Rules, supra note 8.

49 See MOFCOM Panasonic/Sanyo Decision, supra note 12.

50 See MOFCOM Coca-cola/Huiyuan Decision, Notice No. 22 [2009], 18 March 2009, available at <http://fldj.mofcom.gov.cn/aarticle/ztxx/ 200903/20090306108494.html>.

51 See MOFCOM GM/Delphi Decision, supra note 10.

the competition between GM and its competitors in the downstream market made MOFCOM concerned that the proposed transaction might have anti-competitive impacts on the stability of supply, prices and quality of auto parts that used to be produced by Delphi and sold to other domestic automakers. The proposed transaction might thus eliminate competition in the downstream automobile industry by foreclosing other domestic automakers. In particular, MOFCOM was also worried about the hold-up problem between Delphi and other domestic automakers and wanted to ensure that Delphi would not increase switch cost for downstream automakers when they considered switching to other auto parts producers. In the GE/Shenhua[52] case, MOFCOM was concerned about the fact that Shenhua is the major supplier of the specific raw coal that the Coal-Water Slurry (CWS) gasification technology relies upon. Thus the proposed transaction, if not reined in, might eliminate competition in the market for the CWS gasification technology by foreclosing other competitors that own the technology.

On the basis of the information released, there might be two problems with these arguments. One is that MOFCOM failed to prove that the merging parties would have the ability to foreclose competitors downstream. In the GM/Delphi case, for example, at least on the basis of economic theory and international practice, Delphi should have significant market power in the auto parts market. But MOFCOM only mentioned that Delphi was a leader in global and Chinese auto parts markets, providing no further analysis or information of market share or concentration ratio of the auto parts market.

Meanwhile, in the GE/Shenhua[53] case, MOFCOM only mentioned that Shenhua was the major supplier of the specific raw coal. However, it did not provide any information on whether Shenhua was dominant in the upstream market, thereby giving the JV the ability to foreclose its competitors in the downstream market.

The other problem is that MOFCOM failed to show whether post-merger, the merging parties would have incentives to foreclose competitors. In the GM/Delphi[54] case or the GE/Shenhua[55] case, for example, if the merging parties legitimately had market power in the upstream market and would therefore earn super industrial profit, why did it have the incentive to exclude competitors in the downstream market? It reminds us of the Chicago critique of the single monopoly profit theory. In other words, more evidence should be needed to prove that such a vertical merger could indeed create profit in some other markets or could help protect rents in the auto parts or the CWS gasification technology market. Meanwhile, GM might also increase procurement of auto parts from Delphi, which would potentially make it more difficult for other domestic auto parts makers to enter GM's procurement system. The merging parties might put other auto parts makers in an inferior position in the upstream auto parts market by foreclosing Delphi's existing and potential competitors. Obviously, MOFCOM was also concerned about GM's market power in the downstream auto market. To prove foreclosure theory in this case, a higher standard of proof is needed, which means that MOFCOM should prove that GM not only had market power in the downstream market and thus had the ability to exclude competition, but that it also had incentives to do so.

52 See MOFCOM GE/Shenhua Decision, supra note 19.

53 Id.

54 See MOFCOM GM/Delphi Decision, supra note 10.

55 See MOFCOM GE/Shenhua Decision, supra note 19.

5. PATTERNS AND IMPLICATIONS

With more provision rules and regulations being issued and more merger cases being reviewed, MOFCOM is building its capacity to deal with cases more efficiently and effectively. The released cases decisions and the filing process we have participated in, either as independent economist for MOFCOM or as economist for filing firms to prepare competition analysis reports, seem to suggest that some enforcement patterns are emerging that provide important implications for understanding MOFCOM's enforcement policy in the future.

5.1 Reliance on Market Share to Assess MarketPower

Until this stage, MOFCOM has assigned more weight to market share in assessing market power. Indeed, in most cases, if not all, market share and, to a lesser extent, concentration ratios are required information to be submitted to MOFCOM. MOFCOM will then mostly use the market share or concentration ratio to determine whether the merging parties possess market power in the market concerned.

Since there is no regulation on how and what MOFCOM should request from the filing party, MOFCOM can essentially demand any information at any time it deems necessary. For example, if the relevant market defined by MOFCOM is different from what was claimed by the filing parties, MOFCOM may also request market share information of certain product or geographic markets that they are interested in. Right now, the issue of source of evidence has not yet been raised. Indeed, information from third parties is generally accepted even though information from official sources is prioritized.[56]

5.2 More Concerns about Non-Horizontal Mergers

In the assessment of competition effects in horizontal mergers, the Chinese experience is more or less consistent with international practice in the sense that MOFCOM has focused on unilateral effects and coordinate effects.

In non-horizontal merger reviews, however, it seems that MOFCOM has been more concerned with nonhorizontal competition effects than other jurisdictions, such as the United States and the European Union. One reason may be that MOFCOM has taken less consideration of the higher standard of proof for such claims of competition harm. Another possibility is that it may have something to do with the unique organizational structure of enforcement agencies. Indeed, unlike the jurisdictions where merger and non-merger cases are investigated in an integrated way, in China, decentralization of enforcement power might create some coordination problems owing to externalities that merger and non-merger enforcement agencies exert on each other.

56 Interestingly, there appeared some incoherence here. In the Renren v. Baidu case, which was a case under the People's Court, the plaintiff submitted two pieces of market share information, one appearing on Baidu's website and the other on the Securities Daily, a national newspaper. But the court dismissed such information, which would likely be accepted by the MOFCOM.

5.3 Use of Trustee to Monitor the Remedies

In the recently released case decisions, MOFCOM has issued both structural and behavioral remedies. Owing to its capacity limit and increasing numbers of merger filings, it is difficult for MOFCOM to supervise the implementation of remedies. Often, MOFCOM would allow the use of trustees to monitor the implementation process. In the Novartis/Alcon[57] case, for example, MOFCOM ordered Novartis to appoint a monitoring trustee to supervise the implementation of remedies according to the newly issued divestiture guidelines.[58] In the Uralkali/Silvinit[59] decision, MOFCOM allowed the merged party to appoint a monitoring trustee to report to MOFCOM on the implementation of the behavioural remedies to ensure compliance.

5.4 Difference from the US and EU Approaches

In the review process and released decisions, MOFCOM has chosen its own approach to implement the rules and provisions of merger control, although the principles of the rules and provisions possess great similarity to those of the US and the EU. Two good examples are the GM/Delphi case and the Seagate/Samsung case, which are vertical and horizontal mergers respectively. Both mergers were cleared in the US and the EU without any conditions. MOFCOM, however, imposed remedies on both mergers with competition concerns. In the Seagate/Samsung case,[60] in particular, MOFCOM imposed a very rare type of remedy requiring Seagate to operate Samsung's hard disk drive business as a separate business and as an independent competitor for at least 1 year, as this would postpone closure of the deal and increase the transaction cost for the merging parties.[61]

6. CONCLUSION

China's merger control policy has combined the principles underlying US and EU merger controls while forging its own way forward. Compared with other jurisdictions, it has grown dramatically within a period of just 3 years. Although it has received some criticism from scholars and practitioners, and has much room for improvement, MOFCOM has been on the right track in building an independent and transparent merger review system. Even though China is not yet a member of the International Competition Network (ICN), it will be open to international antitrust enforcement cooperation and becoming an active member of the global competition community.

57 See MOFCOM Novartis/Alcon Decision, supra note 14.

58 See Press Release, MOFCOM, Provisions on Divestiture of Assets or Businesses to Implement Concentrations of Undertakings ("Divestiture Guidelines") (5 July 2010), available at <http://fldj.mofcom.gov.cn/ aarticle/zcfb/201007/20100707012000.html>.

59 See MOFCOM Uralkali/Silvinit Decision, supra note 16.

60 See MOFCOM Seagate/Samsung Decision, supra note 20.

61 See further discussion of this type of ring-fencing remedies in Francois Renard, "A Practitioner's Look at Merger Control

To File or Not to File: The Treatment of Offshore Joint Ventures under the EU and China's Merger Control Regimes

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Joint ventures ("JV") encompass a broad range of commercial operations. The creation and operation of a JV can be subject to competition scrutiny in every jurisdiction that it affects, and in some cases, even those jurisdictions that are not obviously affected by the creation of the JV. A common question for parties to an international JV transaction is whether the JV needs to have a sufficient "nexus" to the jurisdiction in question for the transaction to fall within its merger control regime. This note focuses on the merger regulations of the European Union and China, and their potential extraterritorial jurisdiction over newly created offshore JVs.

I. EU MERGER CONTROL REGIME

Pursuant to the EU Merger Regulation (the "EUMR"), a JV will be notifiable if: (i) it constitutes a "concentration"; **and** (ii) it meets certain jurisdictional thresholds, that is, it has a "Union dimension" (the "jurisdictional test"). On receiving the notification, the European Commission (the "Commission") will review whether the transaction could be expected to result in a "significant impediment to effective competition" (the "substantive test").

It is important to distinguish between the jurisdictional test and the substantive test. Transactions must be notified where the jurisdictional test is met, even where they will have no effect on competition in the European Union.

A. Concentration

The creation of a JV qualifies as a "concentration" under the EUMR if the JV performs "on a lasting basis all the functions of an autonomous economic entity." A JV meeting this definition is referred to as a "full function" JV, and constitutes a concentration if each of the following three criteria are met:

1. "joint control" is acquired over the JV (***i.e.*** each parent has a veto over strategic commercial decisions);
2. the JV is formed on a lasting basis; and
3. the JV is an autonomous and independent player on the market.

1 Herbert Smith LLP. The authors would like to thank their colleagues Karen Ip, Molly Herron and Nanda Lau for helpful comments on earlier drafts. This article does not constitute legal advice and should not be relied on as such.

B. Union dimension

The creation of a JV will have a Union dimension if either the first or second set of turnover thresholds set out below is met. The relevant turnover for these purposes is that of the "undertakings concerned," ***i.e.*** the parent undertakings (and their corporate groups) in a JV scenario.

First set of thresholds: (a) The combined worldwide turnover of all the undertakings concerned exceeds €5 billion; **and** (b) the EU-wide turnover of each of at least two of the undertakings concerned exceeds €250 million, unless each of the undertakings concerned achieves more than two thirds of their EU-wide turnover in one and the same EU Member State.

Second set of thresholds: (a) The combined worldwide turnover of all the undertakings concerned exceeds €2.5 billion; (b) In each of at least three EU Member States, the combined aggregate turnover of all the undertakings concerned exceeds €100 million; (c) In each of at least three EU Member States included for the purpose of point (b), the aggregate turnover of each of at least two of the undertakings concerned exceeds €25 million; **and** (d) The aggregate EU-wide turnover of each of at least two of the undertakings concerned exceeds €100 million, unless each of the undertakings concerned achieves more than two thirds of their EU-wide turnover in one and the same EU Member State.

C. Failure to notify

A full-function JV with a Union dimension must be notified and cannot be implemented until it has been cleared by the Commission. Pursuant to the EUMR, an undertaking that violates this obligation may face fines of up to 10 percent of its aggregate worldwide turnover. This requirement is very real: in 2009, the Commission imposed a fine of €20 million on Electrabel, a Belgium company, for acquiring control of CNR, a French company, without having received prior approval under the EUMR.[2]

II. CHINA'S MERGER CONTROL REGIME

Similar to the EUMR, a JV will be assessed under the Anti-Monopoly Law (the "AML") if it: (i) constitutes a "concentration"; and (ii) meets certain jurisdictional thresholds.

A. Concentration

A concentration is defined under the AML as: (i) merger; (ii) acquisition of control over another undertaking by acquiring equity interests or assets; and (iii) acquisition of control or being able to exert a decisive influence over another undertaking by contract or other means. "Control" is not defined under the AML and

2 *See* Press Release, European Commission, Commission fines Electrabel 20 million euros for acquiring control of Compagnie Nationale du Rhône without prior Commission approval (June 10, 2009), http://europa.eu/rapid/pressReleasesAction.do?reference=IP/09/895 and a summary of the decision Case COMP/M. 4994-Electrabel/Compagnie Nationale du Rhône, 2009 O.J. (C 279) 08.

Chinese merger rules are silent on the treatment of JVs. In practice the Anti-Monopoly Bureau of the Ministry of Commerce ("MOFCOM") has taken the view that the creation of a JV constitutes "acquisition of control by contract or other means" and it has exercised jurisdiction over JVs that would not meet the "full-function" criteria under the EUMR.

B. Turnover thresholds

If a transaction qualifies as a concentration under the AML, it must be notified to MOFCOM if it meets one of the two sets of turnover thresholds set out below.[3] Similar to the European Union, the relevant turnover for these purposes is the group-wide turnover of the parent undertakings in a JV scenario.

First set of thresholds: combined worldwide turnover of all undertakings exceeded RMB 10 billion **and** China-wide turnover of each of at least two undertakings exceeded RMB 400 million in the previous financial year; or

Second set of thresholds: combined China-wide turnover of all undertakings exceeded RMB 2 billion **and** China-wide turnover of each of at least two undertakings exceeded RMB 400 million in the previous financial year.

C. Failure to notify

Similar to the European Union, a transaction that meets the jurisdictional thresholds under Chinese merger rules must be notified and cannot be implemented until it has been cleared by MOFCOM. Where business operators fail to comply with the mandatory notification provisions, MOFCOM is empowered to terminate and/or unwind the transaction, dispose of relevant assets, shares or businesses within a certain period, and impose fines of up to RMB 500,000. To date, there is no public record of any party having been fined under the AML for failure to notify. MOFCOM has released two drafts of its rules on investigating and sanctioning non-compliance, and it can be expected that the agency will soon step up its enforcement against any violation of the notification obligations.

III. EXTRATERRITORIAL JURISDICTION

Pursuant to the EUMR and Chinese merger regulations, the relevant turnover thresholds may be achieved by the parents to the JV alone, regardless of the geographic presence of the JV. It is therefore not uncommon for a JV to be notifiable where it will operate exclusively outside the European Union/China, on the basis of its parent undertakings' group turnover achieved in the European Union/China (as applicable).

Notably, under the EU merger control rules, in cases where the jurisdictional thresholds are met by the parents, and the JV will have negligible activities in the European Union, the parties are entitled to submit a short

3 MOFCOM may also review a transaction that falls short of these thresholds if it considers that the transaction has the effect or potential effect of eliminating or restricting competition.

form notification, provided that the JV will have EU turnover or EU assets of less than €100 million. However, there is still no short form notification procedure available under China's merger control regime and it remains to be seen whether MOFCOM will introduce such a procedure for offshore JVs that have little or no nexus with China.

Parties with significant sales in the European Union or China should therefore be mindful of the extraterritorial jurisdictions of the EU and Chinese merger regulations over offshore JVs.

MOFCOM's Approach to Merger Remedies: Distinctions from Other Competition Authorities

Michael Han

Zhaofeng Zhou*

China's Anti-monopoly Law ("AML") took effect in August 2008. From the AML's inception to the end of 2011, the Chinese Ministry of Commerce ("MOFCOM," the authority responsible for merger review under the AML), had imposed "restrictive conditions"— known as remedies in other jurisdictions, such as the European Union — in 10 transactions out of the 382 it had reviewed.[1]

MOFCOM has not yet issued a general guidance on merger remedies,[2] and there have been few studies on the Chinese merger remedies regime. This article attempts to examine the key distinctions between MOFCOM's approach to merger remedies and the approach taken in other jurisdictions. It also briefly analyzes the implications of such distinctions for companies, which may need to consider offering remedies to obtain merger clearance in China.

I. MERGER REMEDIES

Merger remedies are conditions that a competition authority may impose on merging parties so that a proposed merger may be cleared. Such remedies will be imposed in cases where competition in the relevant market is likely to be negatively impacted as a result of the transaction. Remedies are conventionally classified as either structural or behavioral:

(i) Structural remedies refer to the one-off measures adopted by a competition authority that are intended to restore the competitive structure of the market.

(ii) Behavioral remedies (also called conduct remedies) refer to the ongoing measures designed to modify or constrain the behavior of the merging firms.

1 See MOFCOM Press Release, available at http://www.gov.cn/jrzg/2012-01/10/content_2041384.htm (in Chinese).

2 Although MOFCOM is drafting a general merger remedy rule called Provisions on the Imposition of Restrictive Conditions on Concentration Carried out by Undertakings, it is still unclear when these provisions will be adopted.

Compared to behavioral remedies, structural remedies are more definitive and certain, less costly to administer, and readily enforceable. Structural remedies will often consist of a requirement to divest part of the concentration entity or group. However, structural remedies cannot be applied to all merger situations because there may not always be appropriate businesses that can be divested in order to reduce the negative impact of the merger on competition. Thus, an effective package of remedies may contain both structural and behavioral elements. As to its general approach to merger remedies, MOFCOM is generally in line with other merger review authorities: remedies have been required in cases where transactions give rise to serious competition issues and both types of remedies have been imposed by MOFCOM. Nevertheless, there are a number of distinctions between MOFCOM's approach and the approach of other competition agencies.

II. DISTINCTION ONE: FEWER REMEDY CASES IN CHINA

Between 2008 and 2011, MOFCOM imposed remedies in 10 transactions, accounting for 2.6 percent of the 382 transactions it reviewed. According to the statistics released by the EU Commission, during the same period, the EU Commission imposed remedies in 62 transactions out of 1189 transactions, about 5.2 percent.[3] MOFCOM thus appears less aggressive than the EU Commission with respect to merger remedies. Companies seeking merger clearance from MOFCOM may welcome this distinction, as it shows that MOFCOM, as a young agency, has generally been cautious in asking for remedies in merger cases.

III. DISTINCTION TWO: MORE RECEPTIVE TO BEHAVIORAL REMEDIES

Many jurisdictions, such as the European Union,[4] prefer structural remedies. Before their adoption of the 2011 revision to the Antitrust Division Policy Guide to Merger Remedies ("U.S. 2011 Merger Remedies Guide"), U.S. antitrust authorities also preferred using structural remedies. However, the U.S. 2011 Merger Remedies Guide seems to allow more use of behavioral remedies that proscribe the merged companies from engaging in specified anticompetitive behavior. It expands the types of behavioral remedies available by providing for relatively more complex, interventionist, and ongoing restraints.

To date, MOFCOM has been more receptive to behavioral remedies than many other competition agencies. It has imposed: (i) behavioral remedies in the cases of InBev/AB,[5] GM/Delphi,[6] Uralkali/Silvinit,[7] GE/Shenhua

3 See European Commission Merger Statistics, September 21, 1990 to January 31, 2012, available at http://ec.europa.eu/competition/mergers/statistics.pdf.

4 See Notice on Remedies Acceptable under Council Regulation (EC) No. 139/2004 and under Commission Regulation (EC) No. 802/2004, 2008 O.J. (C 267) 1, available at http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:C:2008:267:0001:0027:EN:PDF.

5 For a detailed discussion of this clearance, see Freshfields Bruckhaus Deringer's client briefing "China's MOFCOM imposes conditions on InBev's acquisition of Anheuser-Busch," available at http://www.freshfields.com/publications/pdfs/2008/nov08/24645.pdf.

6 For a detailed discussion of this clearance, see Freshfields Bruckhaus Deringer's client briefing "MOFCOM conditionally clears two offshore acquisitions," available at http://www.freshfields.com/publications/pdfs/2009/oct09/26807.pdf.

7 For a detailed discussion of this clearance, see Freshfields Bruckhaus Deringer's client briefing "MOFCOM conditionally clears Uralkali's acquisition of Silvinit," available at http://www.freshfields.com/publications/pdfs/2011/jun11/30598.pdf.

and Seagate/Samsung; (ii) structural remedies in the cases of Pfizer/Wyeth,[8] Panasonic/Sanyo and Alpha V/Savio, and; (iii) combined remedies in the cases of Mitsubishi Rayon/Lucite and Novartis/Alcon.[9] As shown from the above conditional clearance cases, there have been more behavioral remedy cases than structural remedy cases in China. In addition, while certain types of behavioral remedies (e.g. commitments not to raise prices post-merger or not to discriminate against customers) are generally unacceptable to competition agencies because their implementation would be difficult for the agencies to supervise, such behavioral remedies have been accepted by MOFCOM in a number of cases.

IV. DISTINCTION THREE: A MORE FLEXIBLE AND LESS BURDENSOME APPROACH

Compared to other agencies, MOFCOM tends to be more flexible with the remedies that can be accepted. In the Uralkali/Silvinit case, for example, MOFCOM found that the relevant market was highly concentrated and that the combined entity would become the second biggest player in the market, controlling, together with the largest player, approximately 70 percent of the worldwide supply of potassium chloride. MOFCOM could have required a divestiture or simply blocked the deal given the highly concentrated nature of the relevant market. Yet it opted to take a very flexible approach to remedies and only required the parties to:

(i) continue to follow the current method of sale and related procedures;

(ii) continue to supply a broad range and a sufficient volume of products to Chinese customers, and;

(iii) maintain the customary negotiation procedures and take into account the historical and current trading situation with its Chinese customers.

Another example demonstrating MOFCOM's flexibility is in relation to the "upfront buyer requirement" in a divestiture case. The upfront buyer requirement refers to the situation where a competition authority requires that the notifying party offering the commitment enters into a binding agreement with an identified suitable buyer (the "upfront buyer") before the concentration is cleared. The up-front buyer requirement enables a competition authority to review the proposed remedy and the proposed buyer before allowing the merger to proceed.

Up-front buyer requirements are typical of the U.S. approach to divestitures. They may also be required in divestitures under the EU Merger Regulations,[10] although they are less typical than in the U.S. However, the Chinese Provisional Measures on the Implementation of Assets or Business Divestiture for Concentrations of

8 For a detailed discussion of this clearance, see Freshfields Bruckhaus Deringer's client briefing "MOFCOM conditionally clears two offshore acquisitions," available at http://www.freshfields.com/publications/pdfs/2009/oct09/26807.pdf.

9 For a detailed discussion of this clearance, see Freshfields Bruckhaus Deringer's client briefing "Chinese Ministry of Commerce imposes conditions on Novartis for its acquisition of Alcon," available at http://www.freshfields.com/publications/pdfs/2010/Aug10/28640.pdf.

10 Commission notice on remedies acceptable under Council Regulation (EC) No 139/2004 and under Commission Regulation (EC) No 802/2004, OJ 2008/C 267/01, paragraphs 53-55.

Undertakings[11] do not mention anything in relation to the upfront buyer requirement. Although this absence does not preclude MOFCOM from requiring an up-front buyer to be found prior to a concentration, so far MOFCOM has not adopted this up-front buyer approach in its existing divestiture clearances.

MOFCOM's flexible attitude should be welcomed by parties faced with potentially difficult competition issues, as it increases the range of possible remedies that may be acceptable and allows parties to offer less burdensome remedies that would have less impact on the deal value.

V. DISTINCTION FOUR: REMEDIES OFTEN REQUIRED TO ADDRESS NON-COMPETITION ISSUES

In other jurisdictions, such as the EU and the U.S., remedies are used to address only competition concerns. MOFCOM, on the other hand, often would require remedies in order to address non-competition concerns. Non-competition concerns appear to be the reason for remedies in 5 out of 10 conditional clearances by MOFCOM. Of these clearances, the InBev/AB case is the most obvious instance of using remedies to address non-competition concerns. Although it acknowledged openly in its decision that the transaction did not give rise to any competitive concerns in China, MOFCOM still required the merged entity to notify it and obtain its prior consent for future transactions involving the increase of shareholding in two of the merged entity's existing joint ventures in China or any acquisition of the merged entity's other two major Chinese domestic competitors. These remedies mainly restrained AB-Inbev's ability to undertake any further major acquisitions in the Chinese beer brewering industry; it is probably fair to say such remedies reflected MOFCOM's discomfort with the increasing level of foreign control of the Chinese beer brewering industry and its interest in protecting domestic players.

Similarly, in the Mitsubishi Rayon/Lucite case, although MOFCOM was only concerned with the significant overlap between the parties with respect to one product, MOFCOM nevertheless required that, for five years from the closing of the transaction, the merged entity may not, without MOFCOM's prior approval, acquire other producers or even build new plants in China, not only with respect to the problematic product but also other non-problematic products. These remedies were probably the result of industry policy concerns, as such remedies (particularly with respect to those non-problematic products and the restriction on the establishment of new facilities) would not help to address any competition concerns but would have quite the opposite effect.

Given the broadness of such non-competition issues, it is sometimes difficult for parties to anticipate them and make any plans to offer remedies when they enter into the transaction.

11 On July 8, 2010, MOFCOM published the Provisional Measures on the Implementation of Assets or Business Divestiture for Concentrations of Undertakings (Divestiture Guidelines), which had an effective date of July 5, 2010.

VI. CONCLUSION

What do these distinctions mean for companies that may need to offer remedies to obtain MOFCOM's clearance?

On the positive side, there has been only a limited number of remedy cases and MOFCOM appears to be generally wary of seeking remedies. Moreover, when remedies are required, MOFCOM also tends to be relatively flexible with the remedies that would be acceptable. Unlike other competition agencies which generally prefer structural remedies, MOFCOM is equally open to behavioral remedies. In many cases, the remedies imposed did not seem to be overly burdensome for the parties. This means that the parties would have more choice and freedom with respect to the type of remedies that they can offer to MOFCOM.

Nevertheless, the result of a Chinese merger review (e.g. whether a transaction could be subject to conditional clearance) is often more unpredictable than in other jurisdictions due to the non-competition concerns.

Companies also need to bear in mind that MOFCOM could take a completely different approach with respect to the need for remedies. One good example would be the GM/Delphi case, which was a vertical merger subject to merger reviews in a number of jurisdictions including China. In the U.S. and the EU, competition authorities intervene in vertical mergers only if the merging parties will occupy a dominant market position in either the upstream or downstream market, giving rise to foreclosure issues. Thus with the GM/Delphi case, neither the U.S. nor the EU had imposed any remedies because neither party was found to be in a dominant market position or had significant market power in either the upstream or downstream market. In contrast, MOFCOM nonetheless intervened and imposed certain behavioral remedies even though it did not conclude in its decision that either GM or Delphi was in a dominant market position or had significant market power.

Another more recent and worrisome example is the Seagate/Samsung case, involving Seagate's acquisition of Samsung's global hard disk drive business. This case had been cleared unconditionally in seven other jurisdictions including the U.S. and the EU before MOFCOM imposed remedies. Notwithstanding similar competitive conditions in Europe and in China that would follow the merger, including three global competitors and high barriers to entry, the European Commission concluded that the transaction would not likely result in a substantial lessening of competition. MOFCOM, on the other hand, came up with a different conclusion and as a result, imposed a remedy (among others) that required Seagate to operate the target business globally as a separate business for a period of at least one year. The remedy effectively prevented the parties from closing the global transaction for at least one year. This conditional clearance shows MOFCOM is getting increasingly confident in reaching its own decision independent of other antitrust agencies.

In conclusion, as a young competition agency, MOFCOM is forging its own approach to merger remedies, even if it is generally in line with the principles adopted in the EU and the U.S. Businesses need to pay attention to the differences between the approach taken by MOFCOM and other competition agencies when assessing the need for remedies, particularly in a multi-jurisdictional filing case. Companies should not rely exclusively on a European or U.S.-style analysis when formulating a view about the merger review risks in China.

Assessment of Information Technology Mergers in China

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1. INTRODUCTION

In the four years since the enactment of China's Anti-Monopoly Law (AML), the Ministry of Commerce (MOFCOM) has attracted attention with its conditional clearance of mergers in the information technology (IT) sector. Amongst the 15 conditional clearances to date, three decisions involve transactions in the IT industry. These are Seagate Technology PLC's (Seagate) acquisition of the hard disk drive (HDD) business of Samsung Electronics Co., Ltd. (Samsung); Western Digital Corp.'s (Western Digital) acquisition of the HDD business of Hitachi Global Storage Technologies (HGST), later renamed Viviti Technologies Ltd.; and Google Inc.'s (Google) acquisition of Motorola Mobility (Motorola). Yet, these cases are but a few of the transactions, regulations and industrial policies that are shaping how competition law will be applied to the IT sector in China.

This article provides an overview of MOFCOM's three conditional clearance decisions in the IT sector, considers MOFCOM's approach to horizontal and non-horizontal mergers in this sector, and draws out some of the implications for future IT mergers in the China context.

2. BACKGROUND

MOFCOM has approved the vast majority of transactions reviewed unconditionally since August 2008 when the AML came into effect. Based on available statistics, only roughly 2% of transactions have resulted in a prohibition or conditional clearance decision. None of these interventions related to the IT sector until recently. On 12 December 2011, MOFCOM announced its approval of Seagate's US$1.38 billion acquisition of Samsung's HDD business subject to behavioral remedies. Three months later, on 2 March 2012, MOFCOM approved Western Digital's US$4.3 billion acquisition of HGST in the same sector subject to structural and behavioral remedies. In both cases, MOFCOM concluded that the transaction would have anti-competitive outcomes: the transaction would eliminate a major competitor, reduce the competitive pressures on the remaining competitors in terms of pricing and increase the risk of coordination in the HDD market. On 19 May 2012, MOFCOM announced its approval of Google's US$12.5 billion acquisition of Motorola subject to behavioral remedies. It determined that Google would have the ability and incentive to favor Motorola following the transaction, and thereby undermine effective competition in the smart mobile devices market.

The Seagate/Samsung and Western Digital/HGST decisions provide insight on MOFCOM's approach to horizontal mergers, whilst Google/Motorola highlight its treatment of non-horizontal mergers in the IT sector. These cases are discussed in turn below as well as their possible implications for future IT transactions.

3. HORIZONTAL MERGERS

3.1. Seagate/Samsung

The Seagate/Samsung and Western Digital/HGST decisions concerned consolidation in the concentrated HDD market, a market with only 5 major global competitors. According to MOFCOM, the major HDD competitors prior to either transaction were: Seagate (33%); Western Digital (29%); HGST (18%); Toshiba (10%); and Samsung (10%) with comparable shares in China. Seagate/Samsung resulted in a 5 to 4 merger, and Western Digital/HGST reduced the number of remaining competitors from 4 to 3. Both reviews occurred in the context of parallel reviews in other jurisdictions, including in the EU and US.

3.1.1. Procedure and Substance

The Seagate/Samsung merger was notified to MOFCOM on 19 May 2011. MOFCOM declared the notification complete on 13 June 2011 and cleared the transaction on 12 December 2011. It cleared the transaction at the end of the Extended Phase II review period, after exhausting the total statutory review period of 180 calendar days (i.e. 30 days for Phase I, 90 days for Phase II, and 60 days for Extended Phase II).

MOFCOM defined the relevant market as the HDD market and determined that this was global in scope. MOFCOM's decision shows increased sophistication in the assessment of market dynamics. In one of the most detailed decisions to date, it considered:

- the structure of the HDD market: noting its concentrated nature, high degree of transparency and high barriers to entry given, inter alia, IP and other technology requirements and no new entry in the past 10 years;

- purchasing in the HDD market: which involved confidential bidding procedures and computer manufacturers sourcing typically from only two to four HDD manufacturers;

- capacity utilization: noting that available capacity was limited with all 5 major global manufacturers recently operating at approximately 90%;

- innovation: emphasizing the importance of innovation on the competitiveness of HDD manufacturers; and

- buyer power: noting that distributors generally did not wield sufficient countervailing buyer power, large computer manufacturers rarely opposed price increases and instead passed such increases to end customers, and end customers had limited buyer power given how dispersed they were in the market.

MOFCOM concluded that the transaction would have anti-competitive effects in the HDD market, as it would eliminate a significant HDD competitor globally as well as in China, reduce the competitive pressures on HDD manufacturers in terms of pricing in bidding procedures organized by computer manufacturers. It also considered the increased risk of coordination between the remaining competitors given the degree of market transparency, which enabled HDD manufacturers to predict the competitive behavior of competitors.

3.1.2. Remedies

MOFCOM imposed behavioral remedies requiring Samsung to remain an independent competitor for 12 months from the date of MOFCOM's decision – at which time MOFCOM will determine whether to release Seagate from this obligation having regard to prevailing market conditions (and upon Seagate's application). The main conditions imposed to ensure independence include that Seagate would establish an independent subsidiary to set the price of Samsung-produced HDDs, sell HDDs through independent sales teams, and operate separate production lines with own equipment, processes and systems. Seagate was also required to establish firewalls to prevent the exchange of competitive information between Seagate and Samsung's sales teams. Seagate would establish an independent R&D center for Samsung's HDD products, but was permitted to provide technical assistance.

In addition, Seagate undertook to increase Samsung's production capacity within six months of the decision and without altering its existing business model substantially or forcing Samsung's existing customers to purchase HDDs from Seagate on an exclusive basis. Seagate also undertook not to force TDK China Co. Ltd. (a company that handled HDD assembly for Samsung) to supply HDD magnetic heads to Seagate exclusively. Seagate also committed to invest at least US$800 million yearly over the next three years to develop innovative products and solutions.

3.2. Western Digital/HGST

3.2.1. Procedure and Substance

Western Digital's merger with HGST was notified to MOFCOM on 2 April 2011. MOFCOM declared the notification complete on 10 May 2011. On 1 November 2011, Western Digital withdrew its notification, a few days before expiry of the Extended Phase II review period, and re-filed it citing changes in the underlying facts notified to MOFCOM. MOFCOM re-started its "clock" on 7 November 2011 after accepting the revised notification. It subsequently cleared the transaction on 2 March 2012 towards the end of the second Phase II review period.

As in Seagate/Samsung, MOFCOM defined the relevant market as HDD and determined that the market was global. It considered the same market dynamics, including market structure, purchasing, capacity utilization, innovation and buyer power.

MOFCOM reviewed both transactions at the same time and analyzed the effects on competition resulting from each transaction on its own merits, as well as their combined effect on the HDD market if both transactions were cleared. MOFCOM's decision in Western Digital/HGST highlighted HGST's competitiveness as a strong and innovative HDD manufacturer suggesting that MOFCOM viewed HGST as more likely to be an effective competitive constraint on pricing in the HDD market than an independent Samsung. MOFCOM concluded that the Western Digital/HGST merger would lead to the elimination of a significant competitor in an already concentrated market, reduce competition and incentives to innovate and increase the risk of coordination between the remaining competitors.

3.2.2. Remedies

Like the EU and US, MOFCOM required Western Digital to divest HGST's 3.5-inch HDD assets to a third party within 6 months. The business was subsequently sold to Toshiba Corp.

However, MOFCOM went further and imposed significant behavioral remedies requiring HGST to remain separate from Western Digital. It required Western Digital to operate HGST as an independent competitor for 24 months from the date of MOFCOM's decision – at which time MOFCOM will determine whether to release Western Digital from this obligation based on prevailing market conditions upon application by Western Digital. This included retaining HGST's independent legal personality and conducting its business independently in relation to R&D, production, procurement, distribution, after-sales service, administration, accounting, investment and HR appointments. Western Digital was also required to establish information firewalls to prevent the exchange of competitive information with HGST.

3.3. Possible Implications for Horizontal Mergers

The decisions reflect MOFCOM's evolving approach to IT mergers involving competitors. The Seagate/Samsung and Western Digital/HGST decisions represent the most detailed analysis of coordinated effects to date. Although both cases focused on coordinated effects, a number of the lessons learned can be expected also to inform the approach to unilateral effects cases.

First, in marked contrast to earlier decisions involving coordinated effects, Seagate/Samsung and Western Digital/HGST appear to acknowledge that the mere risk of post-merger coordination in a concentrated market is not enough to establish coordinated effects. The decisions suggest that MOFCOM will conduct detailed analyses of the market(s) implicated in a transaction and will consider, inter alia, the market structure, procurement cycles and purchasing decisions, pricing and price determination, market transparency, barriers to entry/expansion, buyer power, etc. and determine whether the resulting post-merger market structure would be conducive to coordinated effects. In particular, it will consider whether and how collusion might occur in the market, the nature of the collusive mechanism, why collusion is significantly more likely to occur after the merger, as well as why that merger would make collusion more effective or sustainable following the merger.

Its approach to coordinated effects (and unilateral effects) is reflected in its Interim Provisions on the Assessment of the Effects on Competition of Concentrations of Undertakings (Interim Provisions). The Interim Provisions regrettably provide limited guidance on MOFCOM's precise approach – in particular when transactions will/will not raise substantive concerns. However, the Interim Provisions acknowledge that high-technology mergers can benefit technological progress by enabling companies to rationalize resources in terms of technology and R&D capability. At the same time, the Interim Provisions note that such mergers may have adverse competitive effects if they reduce incentives to innovate. The Seagate/Samsung and Western Digital/HGST decisions highlight MOFCOM's preoccupation with the perceived negative impact on technological progress.

Second, MOFCOM will not hesitate to adopt decisions that diverge from other jurisdictions – even after other jurisdictions have approved the transaction. In the EU and US, Seagate/Samsung was cleared unconditionally whereas Western Digital/HGST was cleared subject only to the condition that Western Digital divest HGST's 3.5-inch HDD assets to a third party. It is unclear whether MOFCOM adopted a different threshold for intervention, or whether it simply focused on different facts.

In practice, a different outcome is likely where China presents unique or particular features. The AML enables MOFCOM to take account of both competition and non-competition factors in its analyses. As such, close attention is paid to the impact of a transaction on national economic development, industrial policy and, generally, the Chinese social and economic fabric even in cases with a global dimension. It bears emphasizing in this context that the IT sector is sensitive in China, which is home to the world's largest consumers of PCs and the manufacturing facilities of the world's major computer manufacturers. The technology sector is also regarded as a key sector for national security purposes in China.

Third, the decisions highlight MOFCOM's willingness to consider behavioral or non-structural remedies as a credible alternative to structural remedies, which are generally regarded as more intrusive. It is worth noting in this regard that the AML enables MOFCOM to impose remedies to "mitigate" identified concerns, and not necessarily to eliminate such concerns altogether (as would a structural remedy). The power to mitigate arguably lowers the threshold for intervention. This power might also explain MOFCOM's apparent readiness to accept behavioral remedies in favor of structural remedies.

Behavioral remedies are not necessarily a soft option in the China context as the Seagate/Samsung and Western Digital/HGST decisions show. The "hold separate" arrangements imposed in Seagate/Samsung and Western Digital/HGST are far-reaching and burdensome in terms of intrusiveness into the companies' internal organization and management, and monitoring costs. MOFCOM imposed extensive conditions requiring the merging entities to keep a number of key functions separate, including R&D, production, procurement, distribution, after sales services, administration, accounting, investment and HR, and to maintain information firewalls. In Seagate/Samsung, the "hold separate" obligation applies for 12 months, and in Western Digital/HGST the obligation will remain in place for 24 months. MOFCOM has reserved the right to consider whether to extend the term of the "hold separate" obligation in both cases.

Quite apart from the administrative burdens of a "hold separate" remedy, how such a remedy would enable merging parties to realize anticipated post-merger synergies is questionable. For example, development costs that could be saved as a result of one R&D team (as opposed to two separate teams) developing products. MOFCOM's decisions do not specify whether MOFCOM will carefully consider efficiencies that might arise in a given transaction and whether any merger-specific efficiencies might outweigh the loss in competition resulting from a transaction.

Fourth, MOFCOM may include a review clause in its decisions enabling merging parties to apply to MOFCOM to waive the conditions imposed. Not all MOFCOM decisions include a review clause, although MOFCOM may entertain applications for waiver in such cases. In line with international practice, merging parties would need to show a material change in market conditions, that the remedy is no longer necessary, or that it cannot be implemented.

Lastly, MOFCOM may coordinate its review with other jurisdictions such as the EU and the US. The pull and re-file in Western Digital/HGST suggests that MOFCOM may have coordinated its review with the FTC in order to be satisfied with the sale of HGST's relevant HDD assets to Toshiba Corp. The FTC's press release on its conditional clearance of Western Digital/HGST noted that it coordinated its review with various competition authorities, including MOFCOM.

The degree of cooperation between MOFCOM and other competition authorities has increased over time. It is also common for merging parties in global transactions to keep MOFCOM abreast of merger clearances and/or the review process in other jurisdictions. Coordination of reviews among different jurisdictions can be expected to increase and deepen in the future – especially in cases involving a global remedy, or a remedy relating to a market that is also affected in China, or where coordinating a clearance timetable is important.

4. NON-HORIZONTAL MERGERS

4.1. Google/Motorola

In Google/Motorola, MOFCOM focused on the acquisition of Motorola's portfolio of standard essential patents (SEPs), and combination of Google's mobile operating system (OS) Android and Motorola Mobility's mobile devices (including mobile phones and tablets).

4.1.1. Procedure and Substance

MOFCOM used the full statutory review period to clear the transaction, resulting in the review process taking approximately 6 months. The Google/Motorola merger was notified to MOFCOM on 30 September 2011. MOFCOM accepted the notification as complete on 21 November 2011 and subsequently cleared the transaction on 19 May 2012.

MOFCOM determined that the relevant markets were the global markets for smart mobile devices and operating systems for smart mobile devices. It found that Google was dominant in the market for smart mobile device OSs globally and in China (with a 73.99% market share).

In challenging the transaction, MOFCOM concluded that the transaction would have a negative impact on the China markets for smart mobile devices and smart mobile device OSs. MOFCOM was concerned that Google would have the ability and incentive, post-merger, to favor Motorola to the detriment of other smart mobile device manufacturers. In its view, Google could provide new versions of its Android OS to Motorola first before providing this to other manufacturers for initial "testing" purposes and/or Google might be inclined to use only Motorola for testing purposes. This would place Motorola in an advantageous position, thereby significantly impeding competition in smart mobile devices. MOFCOM was also concerned that by acquiring Motorola's portfolio of standard essential patents, Google would have the ability and incentive to impose unreasonable conditions on patent licensees resulting in an adverse impact on competition in the smart mobile device and smart mobile device OS markets, and thereby harming consumers.

4.1.2. Remedies

MOFCOM imposed behavioral remedies to address the identified concerns, including that:

- Google must license its Android platform (current and future versions) on a free and open source basis, consistent with its current practice;

- Google must treat Original Equipment Manufacturers (OEMs) on a non-discriminatory basis with respect to its Android platform; and

- Google must observe the fair, reasonable and non-discriminatory (FRAND) commitments made by Motorola Mobility concerning use of its SEPs.

All the remedies imposed – except the FRAND condition – apply for a period of 5 years from the date of MOFCOM's decision. Upon expiry of the 5-year period, MOFCOM may adopt a further decision based on prevailing market conditions.

4.2. Possible Implications for Non-Horizontal Mergers

Google/Motorola offers insight on MOFCOM's approach to IT mergers like the Seagate/Samsung and Western Digital/HGST decisions – albeit in relation to non-horizontal mergers and vertical foreclosure concerns. Many of the lessons considered above apply equally in this context.

First, the decision highlights the propensity for diverging outcomes in cases involving global markets. The transaction was approved in other jurisdictions without remedies except in China where it was scrutinized. This is not altogether surprising given the mobile network growth in China (with some 80 million new subscribers coming online every year for the past decade). Google's fractured relationship with China might also account for the lengthy review period. In 2010, Google had several disagreements with the Chinese government over online freedom and alleged intrusions by hackers – resulting in Google deciding to shift its service from Mainland China to Hong Kong.

Second, the decision suggests that the approach to non-horizontal mergers and analyses of vertical foreclosure in particular is still evolving. MOFCOM's decisions to date do not contain the same level of detail or appear to display the same increasing degree of sophistication shown in relation to horizontal mergers. The Interim Provisions make clear that MOFCOM will consider input and customer foreclosure in its analyses of vertical mergers but does not provide further particulars. Regrettably, the Google/Motorola decision provides limited guidance on MOFCOM's precise approach to assessing vertical foreclosure effects.

As noted above, MOFCOM was essentially concerned with two issues: (a) Google's smart mobile device OS as a key input into smart mobile devices; and (b) SEPs as key to smart mobile devices. However, the decision does not clearly articulate why the transaction raised specific competition concerns in the China context where the salient facts were the same as those relied on by other jurisdictions. The outcome of MOFCOM's assessment is all the more surprising, as the decision noted that "Motorola [did] not have any obvious advantage over its competitors" and that the smart mobile device market is competitive.

The focus on Google's significant market share in smart mobile device OSs (and its incontestability in the absence of meaningful competitive constraints) suggests that pre-merger dominance or market power is a pre-requisite for a vertical theory of harm and that market share will play an important role in determining whether a company has the ability to foreclose competition.

However, the threshold for assessing a company's incentive to foreclose competition is not entirely clear. Nor does the decision specify the rationale for concluding that a foreclosure strategy would result in a significant impediment to competition downstream. The decision suggests that MOFCOM adopted a different intervention threshold. Unlike MOFCOM, other regulators such as the Commission in the EU concluded that Google had no incentive to favor Motorola handsets in providing early access to new versions of the Android OS, as Motorola's handset business generated minimal profits and such a strategy risked undermining Google's relationship with other Android OEMs and its search and advertising revenues. Further, the Commission found that Google's ability to favor certain handset-makers was not merger-specific. This is because Google already selected one or a few handset manufacturers for early testing of new Android OS versions. It is thus unclear why MOFCOM concluded that Google had the necessary incentive to foreclose competition. It bears repeating that the IT sector is sensitive in China. The AML, as noted above, requires merger analyses to balance competition issues against non-competition factors that might affect the healthy development of China's socialist market economy.

Lastly, FRAND or FRAND-type commitments are relatively common in the context of vertical mergers in China. In Google/Motorola, MOFCOM required Google to observe FRAND commitments made by Motorola concerning use of its patents. MOFCOM's concerns mirrored those of the Commission and the US Department of Justice (DOJ). Both jurisdictions took note of Google's public commitment that Motorola's SEPs would remain available under FRAND terms (including a provision allowing prospective licensees to challenge Motorola's published 2.25% FRAND rate). However, MOFCOM considered it necessary to formalize this commitment by including the FRAND commitment as a remedy in the decision. It remains to be seen whether MOFCOM will seek to determine what amounts to fair, reasonable and non-discriminatory terms for the SEPs in issue in this case. In line with its approach in other cases, it can be expected that MOFCOM may require Google to set a framework or benchmark against which to assess whether licensing terms are truly FRAND in nature.

This is not the first time that MOFCOM has imposed FRAND or FRAND-like remedies in vertical mergers – sometimes in cases that might not attract intervention in other jurisdictions. Earlier this year, MOFCOM imposed FRAND commitments in relation to a joint venture between Henkel Hong Kong Holding Ltd. and Tiande Chemical Holdings Ltd. A FRAND-like remedy was also imposed in relation to General Motors Corp.'s acquisition of Delphi Corp.. Unlike the earlier decisions, the FRAND commitment imposed in Google/Motorola is not detailed and does not provide any specifics on how the remedy should be implemented stating simply that "Google shall observe the FRAND commitment made by Motorola". It is unlikely that this reflects MOFCOM's likely approach in the future. In practice, MOFCOM's conditional clearance decisions are short, and generally reflect only the salient aspects of a given remedy leaving implementation details to a later stage for negotiation with the merging parties. In this case, MOFCOM essentially imported Google's public commitment, and allowed Google to provide specific details on how it would implement this commitment after adoption of the decision.

CONCLUSION

There are arguably too few cases to discern clear trends with regard to MOFCOM's approach to IT mergers. What is clear is that IT mergers will be looked at closely in China given the sector's sensitivity. As the cases illustrate, MOFCOM will scrutinize IT mergers, including transactions involving global markets.

The cases also suggest that MOFCOM's approach to horizontal mergers is more developed than in the case of non-horizontal mergers. In both instances market share analyses play an important role in the competition analysis. However, the threshold for intervention may differ in the case of non-horizontal mergers.

The analysis will focus on competition concerns but also on how a given transaction might adversely affect the China context – in Seagate/Samsung and Western Digital the HDD market, and in Google/Motorola smart mobile devices and smart mobile operating systems. It remains to be seen whether MOFCOM will continue to be receptive to behavioral remedies in particular in the IT sector as a basis for clearing problematic transactions. This seems likely given its power under the AML to impose remedies to mitigate identified concerns.

Chinese Enforcement Against Abuses of Dominance Ramps Up

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The first three years under the Chinese Anti-Monopoly Law ("AML") have been dominated by merger control decisions mainly involving foreign companies, and cartel investigations mainly involving domestic Chinese ones.

However, the spotlight recently has begun to shift towards the third major area of anticompetitive activities under the AML: abuses of dominant market position. Several prominent matters have been reported in late 2011, most notably an investigation by price regulator the National Development and Reform Commission ("NDRC") into price discrimination in the provision of broadband internet services by state monopoly telecom companies; another NDRC investigation into refusals to deal involving dominant distributors of an important pharmaceutical precursor, and; a civil AML lawsuit filed against leading search engine Baidu. The AML prohibits such conduct by firms with dominant market positions, subjecting them to penalties that include potential fines of between 1 and 10 percent of annual turnover.

This article focuses on the recent NDRC investigations to project future consequences for abuse of dominance cases brought under the AML.

A. BROADBAND INTERNET INVESTIGATION

In November 2011, NDRC announced that it was investigating China Telecom and China Unicom, two of the country's major telecommunications operators, over suspected price discrimination in the broadband internet market. NDRC indicated that the two operators were using their dominant market position—together they reportedly have as much as 90 percent of the broadband market—to charge competitors higher fees for broadband access than those offered to non-competitors. NDRC alleged that this price discrimination resulted in harm to consumers, such as lower-quality interconnection between networks and internet access speeds that are only one-tenth of those available in the United States, the United Kingdom and Japan. NDRC also stated that "effective competition" in the market could lower prices nearly 40 percent over 5 years.

This case is particularly noteworthy because it is the first widely-reported case of Chinese antitrust regulators enforcing the AML against Chinese state-owned enterprises ("SOEs"). Yet SOEs have been the targets of AML cases in the past. In 2010, a tying case involving local SOE Hubei Salt Company resulted in an order by the Hubei Provincial DRC requiring the company to cease abusing its legal monopoly position in salt to harm consumer interests, apparently through activities including tying.[1] Moreover, several SOEs, including several state telecom companies, have been sued by private plaintiffs in AML litigation over the past three years.

The China Telecom and China Unicom investigation generated further interest because a senior NDRC official stated in an interview on state television that the 1 to 10 percent fine would be based on the revenues generated only from the companies' broadband access services businesses, rather than the companies' total revenues across all businesses.

In December, China Telecom and China Unicom were reported as announcing that they would raise their broadband speeds and would reduce broadband service charges substantially (that is, by 35 percent) over the next 5 years. The companies also stated that they have applied to NDRC to settle their investigations pursuant to commitments made by the companies to correct their practices. Under the AML, law enforcement authorities can decide to end anti-monopoly investigations if the companies in question promise to take concrete actions to correct their practices in a given period as approved by the authorities.

B. BLOOD CONTROL MEDICATIONS

On November 14, 2011, NDRC announced fines of nearly RMB 7 million (USD 1.1 million) against two private pharmaceutical companies in Shandong Province for various abuses of dominant market position, reportedly including refusals to deal and the imposition of higher prices through threats to withhold supply. The case involved actions taken to increase the price of promethazine hydrochloride, a key raw material for a cheaply-priced and widely-used hypotensor, Compound Reserpine Tablets ("CRT"). CRT is categorized as a type of basic medicine in China, payment for which is fully covered by the national social insurance policy, so the decision noted that these increased costs were directly borne by society. The fines are notable for being the highest amounts imposed by NDRC (or any other antitrust enforcement agency) under the AML and the first imposed for anticompetitive conduct including abuse of dominant position.

According to reports, Shandong Weifang Shuntong Pharmaceutical Company ("Shuntong") and Shandong Weifang Huaxin Pharmaceutical Trading Company ("Huaxin") entered into exclusive distribution agreements with the only two producers of promethazine hydrochloride in China, by which those producers agreed not to sell promethazine hydrochloride to other distributors. (NDRC's investigation revealed that Shuntong and Huaxin were actually controlled by the same group of people.) After becoming the sole source of promethazine hydrochloride in China, the two companies then pressured most major CRT producers to increase prices for CRT from RMB 1.3 per bottle to RMB 5-6 and to "rebate" to Shuntong and Huaxin RMB 1 per bottle of that price, under threat of ceasing all supply to the producers of promethazine hydrochloride. When rejected by the CRT producers, Shuntong and Huaxin increased the price of promethazine hydrochloride approximately fifteenfold, forcing many CRT producers to suspend production.

See, e.g., http://jjs.ndrc.gov.cn/gzdt/t20101115_380421.htm.

C. THE BAIDU CASE

Beyond administrative enforcement, the volume of AML litigation against large companies — mainly for abuse of dominance — continues to be substantial. Most such cases have been filed against domestic companies.

A recent case was filed in Beijing against Baidu, China's leading search engine, by its competitor Hudong.[2] Hudong accused Baidu of using its dominant market position to negatively impact search results related to its competitors. A public hearing was held in November but no public report of a judgment has been issued. Hudong had reportedly filed a complaint with SAIC earlier, requesting an investigation. This case is similar to earlier ones filed against Baidu for discrimination against competitors in search results, and most were resolved with findings that the plaintiffs had failed to establish Baidu's market dominance and/or that Baidu had apparent justification for its actions.

Separately, Baidu filed a complaint in a Beijing court against the CEO of Hudong for defamation relating to his public statements against Baidu. The Haidian court ordered Hudong and its CEO to publish a statement of apology and pay RMB 120,000 as compensation to Baidu.

D. SOME OBSERVATIONS

These cases illustrate a few points, mainly procedural, about the emerging trend of administrative investigations of abuses of dominance under the AML:

- The broadband internet case shows (consistent with other cases in the context of anticompetitive agreements) that NDRC will allow companies to utilize the commitment mechanism to end investigations by agreeing to alter their conduct and/or compensate complainants.

- NDRC's press releases are very brief and provide little visibility into the legal reasoning and evidentiary burden of proof in individual cases.

- It remains unclear what penalties will be imposed in practice for abuse of dominance and other AML conduct violations, although statements by NDRC officials seem to indicate that fines lower than 10 percent of annual turnover across all businesses may be imposed in some cases.

- Compared to litigation, NDRC enforcement appears to be more aggressive and faster for both investigation and decisions. The Hubei Salt Company case required only three months, while the pharmaceutical precursor case took roughly five months, and the broadband internet case appears to be well along the way toward resolution after approximately six months.

- Many NDRC investigations, including in the cartel area, appear to focus on products in which there is a substantial public interest, such as salt, foods, telecoms, and inputs for popular medicines.

- NDRC's decisions, in contrast to some published court decisions, do not appear to be as strict or detailed on issues such as market definition and findings of dominance.

- NDRC enforcement may originate from media reports (the Hubei salt case), customer complaints (the pharmaceutical case), and competitor/customer complaints (the China Telecom investigation).

See, e.g., http://finance.sina.com.cn/chuangye/internet/20111102/092810738833.shtml; http://old.nbd.com.cn/newshtml/20111102/20111102105556973.html.

Recent developments in civil litigation under China's Anti-monopoly Law

Margaret Wang and Richard Hughes

I. INTRODUCTION

Civil litigation is a key tool for businesses as they seek to protect their interests and remain competitive. So it is unsurprising that the right to launch a civil antitrust action has been exercised with increasing regularity since it became available to businesses in China on August 1, 2008 under China's first comprehensive antitrust law, the Anti-monopoly Law ('AML').

Over the past four years, private antitrust litigation in China has undergone some interesting developments. As the AML entered into effect, numerous cases were filed in the years that followed, but the majority of cases were unsuccessful. The first half of 2012 has seen an unprecedented number of antitrust cases being filed in courts, leading to a revival of interest in this area of law among the media and the public. This trend coincided with the publication of important guidance by the Supreme People's Court ("SPC"), which sets out the fundamental principles (on issues such as standing) of antitrust litigation, and which contains a number of measures intended to facilitate a greater number of successful actions.

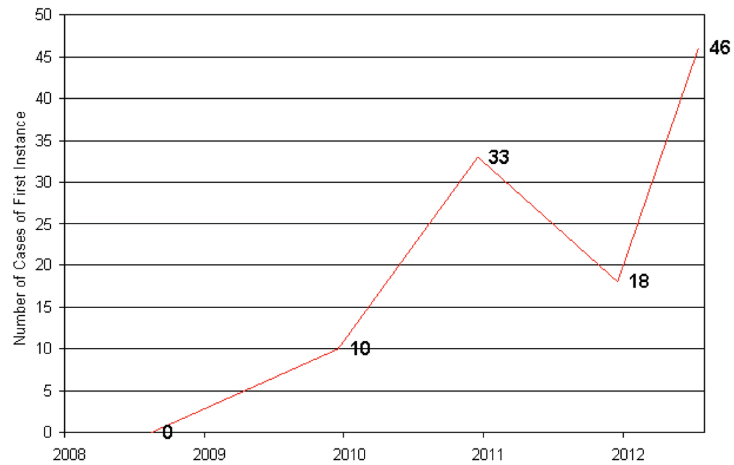
Courts are also becoming increasingly sophisticated in their reasoning (as seen in a recent antitrust challenge against Johnson & Johnson alleging unlawful resale price maintenance) and the use of expert witness evidence (for example in the Qihoo v Tencent abuse of dominance case). At the same time, appetite for bringing private antitrust actions also appear to be on the increase, with the first half of 2012 recording the highest number of cases filed to date since the AML came into effect.

This article summarizes the key developments in the fast-moving Chinese antitrust litigation landscape.

II. BACKGROUND STATISTICS ON ANTITRUST LITIGATION IN CHINA

At a recent seminar in Beijing, Mr. Jin Kesheng, Vice President of the Intellectual Property Tribunal under the Supreme People's Court, provided statistics outlining the number of civil actions accepted by the courts of first instance under the AML to date. As can be seen from the graph in Figure 1, the number of civil claims under the AML has followed an upwards trajectory over the last four years, with a noticeable decline in 2011 followed by a surge in activity in the first half of 2012.

Figure 1: Civil antitrust litigation cases, 3Q2008-1H2012



Source: Speech by Mr. Jin Kesheng, International Seminar on Antitrust Law in the Internet Industry

In addition to the statistics, the SPC also provided some feedback on the qualitative aspects of the cases filed to date. In a press release published on May 8, 2012, the SPC noted that the quality of many of the initial cases brought before the courts has been low, which has resulted in a 'relatively low success rate' for plaintiffs. This view was repeated by Mr. Jin Kesheng at the recent seminar at Peking University, in which he noted that many early cases were tentative efforts brought by legal practitioners seeking to explore the procedure and boundaries of private antitrust litigation and to attract public attention. The number of such "test cases" has decreased in the subsequent years and, more recently, higher-quality cases that raise substantial competition issues are now regularly being brought before the courts.

Interestingly, and according to the SPC, many of the cases concern abuse of dominance rather than anti-competitive agreements.

III. THE LEGAL BASIS AND PROCEDURE FOR CIVIL CLAIMS

The legal basis for private antitrust actions lies in Article 50 of the AML. Article 50 provides that where a business operator's 'monopolistic conduct' 'causes a loss' to another business operator, the infringing operator shall 'assume civil liability' and thus may be sued in a civil action. This right was expressly affirmed by the SPC, in October 2007, by the inclusion in its published list of approved causes of civil action of the rights to pursue claims against anti-competitive agreements, or abuse of dominance.

The legal basis for private antitrust actions has been supplemented by a number of procedural and substantive guidance issued by the SPC. As China's highest court, the SPC oversees the lower courts and its guidance binds all courts below it. A brief description of the relevant SPC guidance in relation to private antitrust actions is set out below.

In the days leading up to the effective date of the AML, on July 27, 2008, the SPC issued a notice, 'On the study and implementation of the Anti-monopoly law of the People's Republic of China' ('SPC AML Implementation Notice'). This notice assigns jurisdiction of AML civil cases to the IP Tribunals and provides that parties must meet the standard set under Article 108 of the Civil Procedure Law (which governs, amongst others, who may be adjoined to a civil case) to be adjoined to a civil case under the AML. This is an important decision, given that IP Tribunals are generally regarded as the most advanced and sophisticated courts in China, as IP judges are generally all legally trained and have had substantial experience in dealing with foreign-related and complex disputes.

In May 2012, the Supreme People's Court published a long-awaited judicial interpretation, the 'Provisions of the Supreme People's Court On Several Issues Concerning the Application of Law in the Trial of Civil Dispute Cases Arising Out of Monopolistic Conduct' ('Judicial Interpretation'), that has further refined and delineated the procedure for actions under the AML and provided some helpful mechanisms designed to assist plaintiffs in making antitrust claims.

The Judicial Interpretation reaffirms the rights of natural persons, legal entities and organizations, to file civil claims under the AML. It confirms that AML actions may be filed as either a stand-alone claim or as a follow-on action. The Judicial Interpretation also clearly specifies that the Intermediate People's Courts (being the second level courts) are to be the courts of first instance in civil antitrust cases, although the SPC retains discretion to grant jurisdiction to the Basic People's Courts on a case-by-case basis. Geographical jurisdiction is in line with the Civil Procedure Law. This means that in the case of a claim of abuse of dominance, the case must be filed in the jurisdiction where the defendant is domiciled; where a case involves a contractual agreement, jurisdiction would lie in the place where the contract was performed.

Under the Judicial Interpretation, in actions pertaining to anti-competitive agreements, where the conduct concerned constitutes a hardcore infringement as prohibited under Article 13(1-5) of the AML, the burden of establishing that the agreement in question did not have any anti-competitive effect is reversed from the plaintiff to the defendant.

In dominance cases, the plaintiff bears the burden of proof in proving that the defendant is dominant and that the behavior was abusive, but the defendant bears a burden to prove that their behavior was fair if they mount a defense. The Judicial Interpretation also helpfully provides facilitative measures for plaintiffs by expressing permitting plaintiffs to adduce evidence of public statements made by allegedly dominant companies to substantiate the finding that they are in fact dominant. While evidence of this nature may be rebutted by the defendant company alleged to hold a position of dominance, this would nevertheless likely go some way to assisting plaintiffs in passing one of the fundamental hurdles in establishing dominance.

Furthermore, parties may introduce expert witnesses to provide opinions on evidence in court, or to provide written evidence in the form of market surveys or other reports.

The Judicial Interpretation brings clarity to a number of fundamental procedural aspects of private claims under the AML. The relaxation of the burden of proof on the plaintiff and the strengthening of the procedural rules for case handling may lead to an increase in the consistency and frequency with which plaintiffs are able to enforce their rights under the AML within the judicial system.

IV. RECENT HIGHLIGHTS IN PRIVATE ANTITRUST LITIGATION

In recent months, several interesting cases have featured in the Chinese courts that bring to light current practices as applied by litigants in resolving their disputes.

1. Qihoo v Tencent - Abuse of Dominance in the High-Tech Industry

As noted above, the majority of civil cases under the AML concern abuse of dominance claims. Of these cases, the most high-profile case is that of Qihoo v Tencent, which was filed by Qihoo 360 against Tencent in Guangdong in October 2011.

Following Tencent's entry into the PC security software sector, Qihoo 360 released two stand-alone software applications that were targeted at QQ, Tencent's flagship instant messaging application. These two applications, '360 Privacy Protector' and 'Koukou Bodyguard', alerted users that QQ was 'scanning' private user files and enabled users to alter certain functionality of QQ. Tencent responded by blocking all users of Qihoo 360's products from using QQ by issuing a public statement stating that its QQ instant messaging product would be unavailable on all devices that installed Qihoo 360's security software, and requested that its users uninstall Qihoo 360's software on the basis that it disrupted certain features of QQ.

Qihoo 360 is claiming damages of RMB 150 million on the basis that Tencent has allegedly abused its position of dominance in the market of online instant communications services by:

- forcing consumers to choose between QQ and Qihoo's 360 antivirus software, alleging that this amounted to prohibited abusive exclusive dealing; and

- abusive "bundling" of Tencent's QQ safety software with Tencent's QQ instant messaging product without justification.

In April, 2012, the first public hearing of this case was held in the Guangdong Higher People's Court in which it considered a number of key issues, which were: market definition, whether Tencent held a position of dominance, and whether Tencent's conduct constituted an abuse of its dominance and liability.

Both parties instructed experts to give evidence, with Qihoo 360 adducing economic evidence by engaging a British economist, and Tencent adducing evidence given by industry experts on the impact of Tencent's conduct on the development and outlook of the Internet sector.

The court held over the hearing, and a judgment is expected to be rendered in the near future. This case is interesting in that it is the first in which a plaintiff has introduced evidence from an expert witness.

2. Antitrust counterclaim against Microsoft

Another interesting case was recently reported to involve Microsoft by way of a counterclaim. The plaintiff's Hong Kong headquarters had been negotiating with Microsoft to allow it to use an existing Microsoft software license in its mainland China operations. These negotiations failed. In 2010, Microsoft asked the local PRC authorities to investigate the plaintiff's mainland China offices, which were found to be using illegal copies of Microsoft's software. The plaintiff was fined. Microsoft then launched a civil action in the local courts in Nansha, seeking damages of RMB 5mn and for the plaintiff to purchase a set number of copies of the software in question.

In November 2012, the plaintiff filed a counter suit in the Nansha district people's court, accusing Microsoft of abuse of dominance on the grounds that:

- it forced the plaintiff to purchase copies of Microsoft software, thereby squeezing out competitor software companies; and

- the higher cost of Microsoft software in mainland China as compared to Hong Kong constitutes price discrimination

As the Nansha court, a Basic People's Court, does not have the jurisdiction to adjudicate on anti-monopoly cases, it will convene a full court to consider the application of the countersuit and, if it finds that the countersuit is established, will transfer the case to the Guangzhou Intermediate People's Court.

3. First antitrust litigation in relation to an anti-competitive vertical agreement

In the first case concerning a vertical agreement to reach court in China, the AML claim against Johnson & Johnson, concerning its distribution arrangements in China, was initially reported in February 2012. The plaintiff, Ruibang Yonghe Technology and Trade Co. Ltd. (***Ruibang***), had been Johnson & Johnson's distributor of surgical products in the Beijing region for more than 15 years.

The distribution agreement contained a term that imposed on Ruibang a minimum resale price of the surgical suture products. The dispute arose when Johnson & Johnson removed Ruibang's distribution rights for certain hospitals after it discovered that Ruibang had charged its hospital customers prices lower than those stipulated under the agreement. Ruibang claimed that the agreement violated the AML as it contained a minimum resale price term, which is expressly listed as an example of a prohibited "monopoly agreement" under the AML. Ruibang sought RMB 14.4 million in damages against Johnson & Johnson.

On May 18, 2012, the Shanghai Intermediate People's Court delivered its judgment finding in favor of Johnson & Johnson. The Court found that Ruibang failed to establish that the agreement in question had given rise to an anticompetitive effect. The Court's approach, while not binding on subsequent court judgments (given China operates a civil law system) nor on the PRC antitrust regulators, suggests that the Court would not find an infringement for resale price maintenance on a per se basis, but would, instead, require evidence that the agreement had given rise to an anti-competitive effect.

Importantly, the Court also set out a non-exhaustive list of relevant factors to be considered in determining whether an agreement that contained a resale price maintenance clause contravened the AML. These included the market share of the product subject to the pricing restrictions, the state of competition in both the upstream and the downstream markets, and the effect of the clause on the volume of the product supplied and on price.

Although Ruibang did not succeed in making its claim, it is the first court case in China concerning vertical arrangements, which are very common in China and continue to be a mainstay of multinationals' strategies in ensuring a wide distribution of their products. The case also demonstrates Chinese courts' growing sophistication in handling antitrust disputes as the judges demonstrate an understanding of the factors that are likely to be of relevance in considering the impact on competition when examining a vertical arrangement.

What next for civil antitrust litigation in China?

Private antitrust litigation in China has begun to flourish in recent times, as demonstrated by the increase in the number of cases filed in the courts so far in 2012. Courts and litigants alike have begun to demonstrate a greater degree of sophistication in analyzing antitrust claims, and parties are now beginning to explore the use of expert evidence in advancing their cases. No doubt the publication of the Judicial Interpretation will encourage this trend, if it has not already done so. Taking all these factors in their totality, it is expected that the growing trend in AML litigation will continue.

With the newly strengthened ad clarified guidelines set down in the Judicial Interpretation, combined with the increasing awareness of businesses of their rights under the AML, it is likely that this increase in the quantity and quality of private antitrust litigation in China is set to continue.

China's Current Approach to Vertical Arrangements Under the Anti-Monopoly Law

Margaret Wang*

I. INTRODUCTION

Traditionally in competition law, vertical arrangements (where parties to the transaction or agreement in question are active up and downstream of each other) are normally subject to a lower level of scrutiny compared with horizontal arrangements. Some jurisdictions have even taken the policy decision not to subject vertical arrangements to the reach of competition law. For instance, the United Kingdom until recently had in place an exemption for vertical agreements. This approach is also proposed under the hotly anticipated Hong Kong Competition Bill.

The position in China is, however, different. Under the Chinese Anti-monopoly Law ("AML"), the legislation expressly seeks to regulate agreements involving undertakings operating at different levels of the value chain, and this is reinforced in regulatory guidance. The merger control provisions make no distinction as to horizontal, vertical or conglomerate mergers, and in practice, the Ministry of Commerce ("MOFCOM") has indeed imposed remedies in two cases involving vertical mergers.

This article summarizes the extent to which vertical arrangements have been scrutinized by antitrust regulators, and instances where they have been challenged in the private sphere.

II. MOFCOM'S APPROACH IN VERTICAL TRANSACTIONS

Under the AML, transactions involving mergers or acquisition of control or decisive influence are notifiable if they meet specified turnover thresholds. In the four years since the AML has taken effect, the antitrust merger control regulator, MOFCOM, has been actively enforcing the merger control provisions. Based on statistics released in December 2011, MOFCOM had examined, in total, just over 400 cases since August 2008. MOFCOM is required to publish its decision only in cases where it has intervened. To date, there have been no fewer than two instances of MOFCOM imposing conditions on vertical transactions in a total of 13 intervention decisions.

Although MOFCOM's public decisions are typically concise and tend not to elaborate or explain the reasoning, it is possible to discern a trend of MOFCOM's maturing approach in relation to vertical transactions, as outlined below.

A. First case: the GM-Delphi decision (September 2009)[1]

The GM-Delphi transaction is the first vertical merger on which MOFCOM imposed conditions. The global automotive manufacturer General Motors ("GM") proposed to acquire the car parts business and four U.S. sites of Delphi Corporation ("Delphi"). The transaction had already been cleared unconditionally by the U.S. and the European Commission. However, MOFCOM imposed a set of behavioral remedies on the parties, requiring Delphi to continue to supply car parts to Chinese car manufacturers on a non-discriminatory basis, and GM to continue to source car parts from various suppliers and not to favour Delphi unreasonably.

In reviewing vertical transactions, antitrust agencies in more mature jurisdictions such as the U.S. and the EU would normally be concerned with foreclosure effects—namely, whether the merged entity would be able and have an incentive to foreclose its competitors or customers upstream or downstream by virtue of its dominant position in one or more of the relevant markets.

Yet in reviewing this transaction, MOFCOM simply alleged that GM and Delphi had a "leading position" in both global and Chinese automotive and car parts markets, respectively. MOFCOM did not justify its concerns by reference to any alleged dominant market position of either or both of the parties (for example, by citing the parties' market shares, the position of their competitors, and other prevailing competitive conditions in the markets). The decision also contains no evidence or analysis that would show that GM and Delphi had the ability and incentive to foreclose their respective competitors or customers other than by referring to the "post-concentration relationship and the common interests between the parties." The decision provides no discussion on the effect that any such foreclosure could have on the relevant markets.

Therefore while MOFCOM's approach in the GM-Dephi transaction was in line with the internationally accepted theory of harm for vertical transactions, nevertheless (at least on the face of the decision), such theory has not been fully expounded upon, nor supported by, evidence.

B. Second case: the Tiande-Henkel decision (February 2012)[2]

Less than three years after the GM-Delphi decision, MOFCOM intervened again in another vertical transaction.

A green field joint venture ("JV") was to be established between Tiande Chemical Holding Limited ("Tiande"), a manufacturer of ethyl products, and Henkel Hong Kong Holding Limited ("Henkel"), a maker of monomer products and one of Tiande's important customers. The JV would involve a vertical integration of Tiande and Henkel's activities, as Tiande would supply the upstream ethyl products, an essential ingredient to the production of monomer products by the JV. Together, the JV and Henkel would consume 25 percent of Tiande's production capacity of the key upstream ethyl products.

The approach adopted by MOFCOM in this decision indicates remarkable maturity. As elaborated in the published decision, MOFCOM was concerned that Tiande, being one of the only two ethyl suppliers in the global market and having a strong global market share of 40 to 50 percent, could alter its supply strategy and discriminate against or "foreclose" other downstream competitors of the JV.

1 MOFCOM Announcement No.76 of 2009.

2 MOFCOM Announcement No.6 of 2012.

To resolve its concerns, MOFCOM imposed behavioral remedies that required Tiande to continue to supply ethyl to all downstream customers on a fair, reasonable and non-discriminatory basis. It also ordered Tiande not to sell ethyl at an unreasonably high price or supply to the JV on terms that are more favorable.

C. Other instances where vertical arrangements have been scrutinized in the context of merger reviews: Novartis-Alcon[3]

In addition to the GM-Delphi and Tiande-Henkel decisions, MOFCOM has also taken into account existing vertical arrangements that parties have outside of the transaction in question when assessing its impact. An example of this is the merger of two pharmaceutical giants, Novartis and Alcon, which was conditionally cleared in the EU, Canada and Australia, upon divestment of various businesses.

The Novartis-Alcon case involved key overlaps in China in ophthalmic anti-infective and anti-inflammatory compounds, and contact lens products. While the extent of overlap between the parties in contact lens products in China was not problematic in and of itself (the merging parties having a combined market share of almost 20 percent in China), MOFCOM was concerned with an existing vertical distribution relationship between Novartis and a leading contact lens products player, Hydron, which enjoyed a position of more than 30 percent market share. MOFCOM came to the view that the exclusive distribution arrangements may eliminate or restrict competition through coordination between Hydron and the merged entity over price, volume and sales territories of contact lens products. MOFCOM therefore required Novartis to terminate these exclusive vertical arrangements within 12 months.

D. Conclusion on MOFCOM's approach to vertical transactions

In conclusion, the fact that MOFCOM has imposed conditions on at least two occasions involving vertical transactions demonstrates that such transactions do not escape scrutiny. A comparative analysis of the two vertical decisions also shows MOFCOM's growing maturity in applying the theory of harm (although this may also partly be explained by MOFCOM's growing willingness to be more elaborate in its public decisions).

III. BEHAVIOURAL ENFORCEMENT IN RELATION TO CONDUCTS WITH A VERTICAL DIMENSION

A. A changing tide? NDRC's investigation into two telecommunications operators[4]

In Chinese competition law, much of the limelight has been focused on merger control. MOFCOM has been extremely active in reviewing transactions, as well as publishing interventions decisions and numerous final and draft guidances. In contrast, the non-merger antitrust authorities—the National Development and Reform

3 MOFCOM Announcement No.53 of 2010.

4 China Telecom, China Unicom Face Monopoly Probe, Wall Street Journal, 9 November 2011: http://online.wsj.com/article/SB10001424052970204358004577027283900972206.html

Commission ("NDRC") and the State Administration for Industry and Commerce ("SAIC")—have not been as active, both in terms of the profiles of cases they have taken on and the number of guidances they have published.

Since the AML came into effect, the NDRC and SAIC have begun to prosecute companies engaging in predominantly hardcore horizontal arrangements such as price-fixing and market allocation. These prosecutions largely concern small-scale activities at local levels, and these cartels often involve trade associations playing facilitative roles. Additionally, the levels of fines are not very high, with the highest imposed in relation to such horizontal arrangements being around RMB 1 million.

Of the various guidances that the NDRC and the SAIC published in January 2011, none provide any further detail or clarification on the authorities' attitude or approach towards vertical arrangements, be it in the context of agreements (such as resale price maintenance), or in the context of abuse of dominance involving vertical elements. Then in November 2011, the NDRC announced that it was in the process of an abuse of dominance investigation into two state-owned companies, China Unicom and China Telecom, the country's two vertically integrated fixed-line operators.

The NDRC investigation is reportedly concerned with allegations of price discrimination in China's downstream broadband access market, of which, according to the NDRC, China Unicom and China Telecom account for over two-thirds, thereby holding a dominant market positions. The NDRC found that the two companies charged rival downstream internet services providers ("ISPs") fees for broadband access that were higher than those for non-rivals. NDRC alleged that such behavior constitutes "price discrimination."

What is not apparent from public sources is the extent to which the NDRC has considered the conduct from a vertical perspective. Under the PRC sector regulations, China Unicom and China Telecom are the only two operators that are permitted to operate networks connected to the internet backbones in China. Any ISPs wishing to provide broadband internet connection services in China must first seek access from either China Unicom or China Telecom.

In other jurisdictions, such as Europe, such conduct involving pricing of a key upstream input on terms that are unfavorable to downstream competitors would normally be considered a possible instance of abusive margin squeeze, as opposed to price discrimination. Examples of margin squeeze include the European Deutsche Telekom case[5] and the TeliaSonera case.[6] Both of these cases involved downstream pricing by incumbent telecommunications operators that sought to price in such a manner as to squeeze out downstream rivals.

While the NDRC has yet to conclude its investigation into China Unicom and China Telecom's pricing conduct in relation to their provision of access to the internet backbone, the case highlights the fact that the behavioral antitrust regulators such as the NDRC are now ready and willing to take on more high-profile and

5 European Commission Case C-280/08 P: Deutsche Telekom AG v Commission.

6 European Commission Case C-52/09: Konkurrensverket v TeliaSonera Sverige AB.

technically complex cases, including those involving vertical elements, which are traditionally considered to be a more difficult area to tackle. Therefore, vertically integrated companies with significant market presence in the upstream product market, or those who supply products or services that can be characterized as essential inputs need to pay heed to possible antitrust risks associated with their conduct involving downstream enterprises.

IV. PRIVATE ENFORCEMENT IN RELATION TO VERTICAL ARRANGEMENTS

A. Ruibang v. Johnson & Johnson[7]

As mentioned above, the AML contains an express prohibition against vertical agreements that fix resale prices or set minimal resale prices on products with respect to third parties. There is also a catch-all prohibition in relation to all vertical arrangements that may have the effect of eliminating or restricting competition.

To date, no known public enforcement actions have been taken in relation to any resale price maintenance arrangements. Furthermore, the NDRC and the SAIC generally do not scrutinize vertical arrangements if the undertakings concerned do not have substantial market presence of at least approximately 30 percent of market share in the relevant market. Companies with operations in China have therefore been able to derive some comfort from the NDRC or SAIC's generally understood position, and have not had to revise their go-to-market models which, for many companies (particularly multinational companies wishing to gain market presence rapidly), involved appointing distributors for their products.

Thus the widely-reported February 2012 litigation against Johnson & Johnson ("J&J") concerning its distribution arrangements in China may serve as a wake-up call to companies with a network of distributors to take a more cautious approach when it comes to their supply arrangements in China.

The case involved a claim by Johnson & Johnson's distributor alleging that the terms of its exclusive distributorship constituted unlawful resale price maintenance. The plaintiff, Ruibang Yonghe Technology and Trade Co., Ltd. ("Ruibang"), had been Johnson & Johnson's distributor of surgical products in the Beijing region for more than 15 years. The distribution agreement imposed a minimum resale price of the products on Ruibang. The dispute arose when J&J cancelled Ruibang's distribution rights for certain hospitals after discovering Ruibang was charging its hospital customers prices lower than those stipulated under the agreement. Ruibang therefore challenged the legality of the agreement based on the AML.

A number of key arguments were raised during the trial. In particular, Ruibang argued that Johnson & Johnson had violated the prohibition on monopoly agreements under the AML by unlawfully restricting Ruibang's ability to sell the products to its customers at a price below the stipulated minimum resale price, the purpose of which was to restrict competition. Ruibang sought RMB 14.4 million in damages for the harm resulting from its cancelled distribution rights.

7 Press release published by Shanghai No.1 Intermediate People's Court in February 2012: http://www.a-court.gov.cn/platformData/infoplat/pub/no1court_2802/docs/201009/d_880113.html (in Chinese). A short report of this case can be found in English at: Antitrust a buzz word at China's parliamentary meeting, Fin. Times (Mar. 16 2012), available at http://www.ft.com/cms/s/2/5f49ace4-6f6e-11e1-9c57-00144feab49a.html.

Johnson & Johnson's first key responses was that the claim was not valid because the distribution agreement was terminated before the AML took effect. The second key response, and the more interesting one, was that even if the distribution agreement had breached the AML, Ruibang was a participant in the infringement and therefore not entitled to bring such a claim. This line of argument was very similar to that pleaded in ***Courage v Crehan***[8] in Europe.

The court has yet to render its judgment. However, the case demonstrates an increased risk profile associated with vertical arrangements. Businesses in China are becoming increasingly aware of the use of competition law claims as a sword in advancing one's commercial interests. In addition, companies with extensive distribution arrangements in China can no longer take the view that challenges would be unlikely, given that the high-profile ***Ruibang v Johnson & Johnson*** case may register on the radar screens of distributors across China and possibly whet their appetite in making similar claims. The risk of private action is further amplified by the combination of the relatively modest cost of litigation in China, as well as the promulgation by the Supreme People's Court on May 8, 2012 of a set of judicial interpretations that seek to encourage more private AML actions.

V. CONCLUSION

While the body of competition law in China is still relatively young, there have been some interesting decisions taken by regulators in relation to vertical arrangements, be it vertical mergers such as the case of GM-Delphi, or investigations into conduct involving vertical elements such as the abuse of dominance investigation against China Unicom and China Telecom. A review of these decisions and investigations reveals that the approach taken in relation to vertical issues is largely in line with the internationally accepted theory of harm. It is also notable that vertical arrangements have also come under attack in private courts, even though no private litigation has resulted in a successful claim to date.

Given the pace with which regulators are maturing in their application of the law, as well as the growing enthusiasm of private litigants in using competition law as a sword to advance their interests, it is likely that the level of scrutiny over vertical arrangements will not abate. As the jurisprudence in this area develops, and as Chinese regulators gain more experience in reviewing vertical arrangements, it is anticipated that they will be able to apply the theory of harm by reference to the factual matrix with greater confidence, and hopefully with a higher degree of predictability that follows international norms.

8 Case C-453/99 [2001] ECR I-6297.

Judicial Practice Under Code of Conducts in China's Anti-Monopoly Law

Susan Ning[1*]

It has been three and a half years since China's Anti-Monopoly Law ("AML") was enacted. Although still in its initial stage, the code of conduct under the AML has been gradually developed and widely recognized. The administrative agencies, including the National Development and Reform Commission ("NDRC") and the State Administration for Industry and Commerce ("SAIC"), and the judicial branch, specifically the Supreme People's Court, have been working to become more deeply involved and have made significant progress. The most recent and notable development is the Supreme People's Court "Prov isions of the Supreme People's Court on Several Issues Concerning the Application of Law in the Trial of Civil Dispute Cases Arising from Monopolistic Conduct" ("Supreme Court Provisions"[2]). This article reviews the latest judicial practice under the current code of conduct of the AML, and the challenges presented by these new developments.

I. THE EXISTING CODE OF CONDUCT UNDER THE AML

Chapter 2 and Chapter 3 of the AML concern the regulation of monopoly agreements and abuse of market dominance activities, respectively. Under Chapter 2, companies are prohibited from engaging in horizontal agreements including price fixing, output restriction, market segmentation, restriction on purchasing or developing new technology, and joint boycotts, as well as vertical agreements including fixing resale price and fixing the minimum resale price. Under Chapter 3, companies having dominant market positions are prohibited from engaging in abusive conduct, including selling commodities at an unfairly high price or buying commodities at an unfairly low price, selling below cost, refusal to deal, designated dealing, bundling, and discrimination. The AML has also empowered the antitrust enforcement agencies to determine other conduct that they deem to be anti-competitive.

The AML has established a dual model comprised of administrative law enforcement and judicial review of the antitrust code of conduct. According to the government agencies' functional division effected by the Chinese State Council, NDRC is in charge of monopoly agreements and abuse of market dominance activities related to price issues, while SAIC is in charge of the monopoly agreements and abuse of market dominance related to non-price issues.

1 * King & Wood Mallesons.

2 On March 3, 2012, the Provisions of the Supreme People's Court on Several Issues Concerning the Application of Law in the Trial of Civil Dispute Cases Arising from Monopolistic Conduct, as adopted at the 1539th Session of the Judicial Committee of the Supreme People's Court on January 30, 2012, was issued and will come into force on June 1, 2012. The Provisions include rules of jurisdiction, burden of proof, rules of evidence, use of expert witnesses, and remedies regarding antitrust litigation under the AML.

In addition to the administrative enforcement efforts made by NDRC and SAIC, private litigation has also played an important role. Individual consumers and corporations alike are starting to realize that the AML can be used as a powerful device to protect their rights against cartels and monopolies. Specifically, consumers and corporations have the right to institute legal proceedings for civil disputes under Article 51 of AML by asserting that their rights were infringed by a monopoly agreement or an abuse of a dominant market position.

Under Article 53 of the AML, if a party is dissatisfied with the decision made by the authority for enforcement of the AML regarding monopoly agreement and abuse of dominance, it may apply for administrative reconsideration,[3] or it may file an administrative appeal of the decision to the court.[4] However, the AML has yet to clarify the jurisdictional relationship between the administrative agencies and the courts. It is currently unclear which branch has proper jurisdiction to investigate and to review monopoly conduct when there is overlap. Theoretically, it would appear that NDRC, SAIC and the courts may operate independently of one another in the application of the code of conduct under the AML.

II. NEW DEVELOPMENTS IN JUDICIAL PRACTICE

In addition to the recent publication of the Supreme Court Provisions, the new development in judicial practice under the code of conduct in the AML is the expansion of practicing scope and the enrichment of evidentiary procedures in relevant antitrust civil actions.

A. Civil cases involving vertical monopoly agreements

In contrast to cases decided by administrative agencies,[5] within the judicial branch, abuse of dominance cases outnumber cartel cases, and almost all published cartel cases are related to horizontal agreements. Only recently has there been a civil case involving a vertical monopoly agreement. On February 3, 2012, Shanghai First Intermediate People's Court heard the first case involving a vertical monopoly agreement in China. Beijing Ruibangyonghe Technology and Trade Company ("BRTTC") filed suit against Johnson & Johnson for violations found in a price agreement drafted by the latter. BRTTC alleged that Johnson & Johnson restricted BRTTC's minimum resale price to third parties. Specifically, BRTTC alleged that Johnson & Johnson coerced BRTTC into maintaining a minimum resale price by threatening suspension or termination of the agreement, and through other methods. As a result of these and other price-fixing behavior, Johnson & Johnson is suspected of engaging in vertical monopoly. At the first instance, the court overruled the plaintiff's claim on May 18, 2012 on the grounds that the plaintiff failed to provide evidence of the defendant's market share and the competition status in the relevant market, and that the evidence was not sufficient to prove monopoly conduct and the direct connection between the damage and the alleged vertical agreement.

3 Administrative reconsideration is analogous to an appellate decision rendered by an administrative agency. If a party is dissatisfied with the initial decision by the administrative agency, it may appeal the decision for reconsideration.

4 An administrative appeal is an initiation of a new administrative action rather than an appeal of court decision.

5 Between NDRC and SAIC, cartel enforcement still prevails over dominance abuse enforcement.

B. Enrichment of evidentiary procedures for plaintiffs

On April 18, 2012, the Guangdong Higher People's Court held the first court hearing for an abuse of dominance action filed by Qihoo (the owner of the 360 antivirus software) against Tencent (the operator of QQ instant messaging software) under the AML. Qihoo accused Tencent of abusing its dominance in the market for online instant communications services and claimed damages of RMB 150,000,000. There were four issues in this case: market definition, dominant position, abusive conducts, and legal liabilities. The court divided the hearing into four sessions, dedicating one session to each issue. The court focused its attention mainly on market definition, dominant position, and abusive conduct. Expert witnesses played a crucial role at the hearings and each issue was debated extensively by counsel from both parties. The hearings lasted for more than eight hours and attracted immense public attention. Ultimately, no judgment was entered.

This case is distinguished from previous cases by being the first AML litigation where the plaintiff, Qihoo, engaged in in-depth analysis and presented ample evidence, including an economic report, to prove the defendant's dominant position. The engagement of outside professionals has been affirmed by the recently issued Supreme Court Provisions in Articles 12 and 13, which stipulated that litigants may employ expert witnesses and professional agencies in trial. With the Supreme Court's affirmation, involvement of professionals—such as economists, industry experts and scholars in antitrust private litigations—is expected to become increasingly prevalent in the near future.

III. TRENDS AND CHALLENGES IN JUDICIAL PRACTICE

The newly-issued Supreme Court Provisions regarding antitrust civil actions under the AML is a big step for the judicial litigation development of the AML. The Supreme Court Provisions not only provided procedural guidelines for private antitrust litigation, but also clarified issues relating to burden of proof, acceptable forms of evidence and methods for evaluating evidence. The new guidelines provided by the Supreme Court Provisions will give both consumers and corporations an effective method of preventing and restraining illegal monopolistic behavior and safeguarding their interests. Under these new Supreme Court Provisions, there will likely be more cases related to the abuse of dominance, as well as monopoly agreements.

However, many of the current cases are still pending, and the courts have been hesitant in making any drastic changes, adopting a cautious approach to applying the AML. One possible explanation of this phenomenon is the numerous deficiencies currently found in the code of conduct itself. For instance, uncertainties regarding how to calculate market share, how to establish a dominant market position and how to prove anti-competitive effect still need to be resolved, either by enacting more specific rules of implementation, or through judicial precedents.[6] After all, the AML is still in its developing stages. Moreover, judges have generally expressed concerns with the potentially profound effects a judgment may have on the future operations of companies, although it would be a pity to see judges refraining from making a sound decision in accordance with the AML because of this caution.

6 Judicial precedents are not binding on the courts in China but can be used as a secondary source to understand judicial practice.

Upon the promulgation of various implementation rules,[7] both the NDRC and SAIC have gradually picked up their momentum in the enforcement of the AML. For example, the NDRC attracted significant public attention when it imposed a fine of more than RMB 6.8 million on two pharmaceutical companies for violations of the AML.[8] A recent high-profile case involved the investigation of China Telecom and China Unicom, the two largest State-owned telecommunications operators, for their alleged abuse of dominance in the broadband Internet access market[9]. The promulgation of the Supreme Court Provisions will enable the judicial branch to play an increasingly important role in civil actions under the AML.

As administrative enforcement and judicial practice continue to develop, the potential discrepancy between the administrative agencies and the court regarding their jurisdiction of investigating and reviewing the same monopoly conduct may become a real problem in the future. Determination of the proper jurisdiction for investigation and review of a questionable monopolistic conduct has been a major concern. Due to the ambiguous relationship between the administrative agencies and the courts, coordination between the two branches remains a challenge.

One of the main concerns regarding the interaction between the administrative agencies and the judicial courts in AML antitrust cases is the treatment of previous administrative decisions in the judicial courts. Specifically, whether the administrative decision should be admitted as evidence in judicial courts, and if so, how much weight should they bear in judicial trials. While the Supreme Court took a positive stand on that issue, giving significant weight to previous administrative decisions in subsequent judicial proceedings, in its initial draft of the Supreme Court Provisions,[10] the final version is silent on the matter. This further indicates courts' cautious attitude towards AML cases. Unless these issues are properly resolved, there will continue to be controversy surrounding the application of the AML and the future of antitrust litigation.

Further attention must be directed toward proper coordination of judicial proceedings with administrative proceedings. Potential problems may arise when the administrative agency resumes investigation following the conclusion of court proceedings. In cases of simultaneous judicial proceedings and administrative investigation,

7 NDRC and SAIC promulgated three substantive rules and two procedural rules that refined the aforesaid regulations in order to implement the regulations of AML. The substantive rules are Provisions on Anti-price Monopoly (promulgated by the NDRC in 2010), Provisions on Prohibition of Monopoly Agreements and the Provisions on Prohibition of Abuse of Market Dominance (promulgated by the SAIC in 2010). The procedural rules are Procedural Provisions on Investigating Monopoly Agreements and Abuse of Market Dominance (promulgated in 2009 by the SAIC) and Procedural Provisions on Administrative Enforcement of Anti-price Monopoly (promulgated in 2010 by the NDRC).

8 On November 14, 2011, the NDRC imposed a fine of RMB 6,877,000 and 152,600 against two pharmaceuticals companies and confiscated their illegal income for controlling an active pharmaceutical ingredient (API) of Compound Reserpine Tablets (复方利血平原料药).). The resulting price hike led to production halts in several pharmaceutical enterprises.

9 The parties have proposed several remedies to address the NDRC's concerns. The parties are said to have reached a settlement with the NRDC, despite the lack of official reports on this matter to date.

10 According to Article 11 of Provisions of the Supreme People's Court on Several Issues concerning the Application of Law in the Trial of Monopolistic Civil Dispute Cases (Draft), facts confirmed by a decision of the anti-monopoly law enforcement authority affirming the existence of monopolistic conduct need not be further proved in court with additional evidence, unless it can be rebutted by evidence proving to the contrary from the opposing party.

there might be potential conflicts between the administrative decision and the court's ruling. In order to properly resolve these issues, a balance must be made between the discretionary power of administrative agencies against the advantages of judicial practices, such as greater transparency[11] and more predictable[12] limitations for the review period.

11 Compared to administrative agencies, courts are more selective in the cases they accept due to formal procedures governing which cases should be heard. In addition, investigations by the administrative agencies are often closed-door. Their decisions, even if published, provide very limited visibility into their reasoning process.

12 The administrative agencies typically take several months to investigate and review cases. However, there is no formal time guideline for the agencies. In contrast, courts observe formal procedural rules that set specific timeframes in which cases must be resolved.

Antitrust Litigation in China – A Step Forward

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The legal basis for private antitrust civil litigation in China is Article 50 of China's Anti-Monopoly Law (the "AML"), which provides that "[w]here the monopolistic conduct of an undertaking has caused losses to another person, it shall bear civil liability according to law." Since the AML entered into force on August 1, 2008, Chinese parties believing themselves to have been harmed by anti-competitive conduct have had more success in getting the attention of Chinese courts than of Chinese antitrust authorities. Chinese courts have reportedly accepted 61 antitrust cases and ruled on 53, although the courts have so far generally ruled in favor of the defendants.[2] By contrast, China's anti-monopoly enforcement authorities (the "AMEAs") have been relatively inactive in non-merger enforcement of the AML. The National Development and Reform Commission ("NDRC") and the State Administration for Industry and Commerce ("SAIC") have issued very few decisions regarding domestic cartels and have publicly reported only three abuse-of-dominance investigations.[3]

The legal framework for Chinese antitrust litigation took a significant step forward on June 1, 2012, when the judicial interpretation (the "Judicial Interpretation") of China's Supreme People's Court (the "SPC") regarding private civil litigation under the AML took effect. This is the first SPC judicial interpretation addressing the AML.

I. BACKGROUND

In China, four levels of courts can hear civil disputes in the first instance: basic people's courts, intermediate people's courts, high people's courts, and the SPC.[4] The jurisdiction of these courts depends mainly on the

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2 See Press Release of the SPC (May 8, 2012), available at: http://www.court.gov.cn/xwzx/xwfbh/twzb/201205/t20120508_176702.htm.

3 All of the three investigations (i.e., refusal to deal by two pharmaceutical companies, discriminatory treatment/margin squeeze by China Telecom and China Unicom, and tying by Wuchang Salt) were carried out by NDRC or its provincial agencies. None of the three investigations involved multinational companies. A fine was imposed in only one case (the refusal to deal by two pharmaceutical companies).

4 See Articles 18–21 of the Civil Procedural Law.

subject matter of the dispute, the complexity and impact of the dispute, and the amount in controversy. Appeals are heard by the next higher level court.

When the AML was first adopted, it was unclear which level of courts would have first-instance jurisdiction over civil claims for damages. The SPC classified civil claims under the AML as "intellectual property rights civil disputes" (later renamed "intellectual property rights and competition disputes").[5] As a result, subject to any special procedural rules, AML cases could in theory be heard in the first instance by 92 designated basic people's courts, as well as by intermediate people's courts and high people's courts, depending mainly on the amount in controversy.[6]

As mentioned above, AML civil litigation in China is also subject to special procedural rules adopted by the SPC, such as the Judicial Interpretation.[7] Drafting of the Judicial Interpretation began in 2009. A preliminary version of the Judicial Interpretation was published for comment on April 25, 2011 (the "2011 Draft"). The final Judicial Interpretation is less detailed than the 2011 Draft, particularly with regard to discovery and the interaction between court proceedings and investigations by the AMEAs. As discussed below, the Judicial Interpretation, among other things, changes the allocation of first-instance jurisdiction over civil litigation under the AML.

II. SUMMARY OF THE JUDICAL INTERPRETATION

A. Jurisdiction

As noted, the Judicial Interpretation modifies the allocation of first-instance jurisdiction over AML civil litigation (Article 3). High people's courts will have no jurisdiction over AML civil lawsuits in the first instance. Certain intermediate people's courts[8] will continue to have jurisdiction over such lawsuits, alongside the SPC-ap-

5 See SPC, Notice on Causes of Action in Civil Cases (issued on February 4, 2008 and effective as of April 1, 2008) (listing "anti-monopoly related disputes" under Item Sixteen, "Unfair Competition and Antitrust Disputes," in Section Five, "Intellectual Property Rights Disputes"), available at: http://www.law-lib.com/law/law_view.asp?id=249663. The 2008 notice was further amended in 2011. See SPC, Notice on Causes of Action in Civil Cases (issued on February 18, 2011 and effective as of April 1, 2011) (renaming Section Five as "Intellectual Property Rights and Competition Disputes," and distinguishing between unfair competition disputes and antitrust disputes by splitting the previous Item Sixteen into two items: Item Fifteen, "Unfair Competition Disputes," and Item Sixteen, "Antitrust Disputes"), available at: http://www.court.gov.cn/xwzx/fyxw/zgrmfyxw/201103/t20110320_18959.htm.

6 See SPC, Circular on Adjusting Standards for Various Levels of People's Courts to Have Jurisdiction in the First Instance over Intellectual Property Rights ("IPR") Civil Cases (issued on January 28, 2010 and effective as of February 1, 2010), available at: http://rmfyb.chinacourt.org/paper/html/2010-01/29/content_3343.htm; and SPC, Standards for Basic People's Courts to Have Jurisdiction in the First Instance over [General] IPR Civil Cases (issued on January 28, 2010 and effective as of February 1, 2010), available at: http://www.court.gov.cn/qwfb/sfwj/tz/201002/t20100222_1512.htm. The SPC also issued a circular providing that the tribunals responsible for IPR cases should also be responsible for antitrust civil lawsuits, whether or not IPR related. See SPC, Circular on Carefully Studying and Implementing the AML (issued on July 28, 2008).

7 See SPC, Circular on Adjusting Standards for Various Levels of People's Courts to Have Jurisdiction in the First Instance over IPR Civil Cases (issued on January 28, 2010 and effective as of February 1, 2010), Item 5, available at: http://rmfyb.chinacourt.org/paper/html/2010-01/29/content_3343.htm (dealing with jurisdiction over special IPR civil cases, such as those involving antitrust, patents, or recognition of well-known trademarks).

8 Article 3 of the Judicial Interpretation provides that the intermediate people's courts having jurisdiction over antitrust

proved basic people's courts. It remains to be seen which of the 92 basic people's courts that have first-instance jurisdiction over general IPR civil disputes will be approved by the SPC to exert first-instance jurisdiction over AML civil litigation.

B. Standing

The Judicial Interpretation defines private civil antitrust litigation as: (i) damages claims arising from anti-competitive conduct (usually tort claims) and (ii) disputes arising from anti-competitive provisions of agreements, charters of associations, ***etc.*** (contractual claims or otherwise) (Article 1). To qualify as "damages" under category (i), three conditions must be satisfied: (a) the damages must be actual damages; (b) there must be a causal link between the anti-competitive conduct and the damages; and (c) the damages must be of a type that the AML is intended to prevent.[9] It is unclear whether a plaintiff under category (ii) has standing regardless of whether she has suffered "damages."

The Judicial Interpretation eliminated the 2011 Draft's express grant of standing to both direct purchasers (who bought a product directly from the defendant) and indirect purchasers (who operate further downstream). Nevertheless, Article 1 implies that indirect purchasers have standing to sue and certainly does not expressly prohibit standing for indirect purchasers.[10]

C. Relation to Administrative Proceedings

The Judicial Interpretation reiterates that a plaintiff may bring either a stand-alone or a follow-on action after an AMEA has determined that the activity in question violates the AML (Article 2). The 2011 Draft contained one exception to this rule: against certain entities involved in specified abuses of administrative power

civil litigation in the first instance include the intermediate people's courts of the capital cities of the provinces and autonomous regions, the intermediate people's courts in the municipalities directly under the control of the central government, the intermediate people's courts of the cities specifically designated in the state plan, and the intermediate people's courts designated by the SPC.

9 See Interview of the responsible justice at the IPR tribunal of the SPC (May 9, 2012), available at: http://www.chinacourt.org/article/detai l/id/516688.shtml.

10 The people's courts may take a relatively broad approach to standing in antitrust civil cases. See Interview of the responsible justice at the IPR tribunal of the SPC (May 9, 2012) (stating that anyone having sufficient evidence to prove one of the two types of private antitrust litigation cases under Article 1 has litigation standing), available at: http://www.chinacourt.org/article/detail/id/516688.shtml. The SPC has stated that "as long as the conditions exist to accept a lawsuit under Article 108 of the Civil Procedural Law and under the AML, the people's courts should duly accept the case and adjudicate according to law." See the SPC, Circular on Carefully Studying and Implementing the AML (issued on July 28, 2008). The referenced conditions under Article 108 of the Civil Procedural Law are: "(i) the plaintiff must be a citizen, legal person, or an organization having a direct interest in the case; (ii) there must be a specific defendant; (iii) there must be a concrete claim, a factual basis, and a cause of action; and (iv) the lawsuit must be within the scope of civil lawsuits acceptable by the people's courts and within the jurisdiction of the people's court to which the lawsuit is filed." The referenced condition under the AML is that "the monopolistic conduct of an undertaking has caused losses to another person." See Article 50 of the AML.

under Articles 32 and 36 of the AML, only follow-on civil claims were allowed.[11] This exception is omitted in the Judicial Interpretation, suggesting that such claims may be brought as stand-alone actions.

In addition, the 2011 Draft permitted courts to adjudicate a case even if an AMEA had investigated the case without finding any anti-competitive conduct, and it gave courts discretion to suspend a case pending the results of an AMEA's investigation. The Judicial Interpretation drops these provisions but does not prohibit courts from adjudicating cases where an AMEA has investigated and found no violation.

Finally, the 2011 Draft stated that plaintiffs may establish a rebuttable presumption of an antitrust violation based on other non-appealable judgments, rulings or AMEA decisions. Again, the Judicial Interpretation is silent on this issue. However, this issue is partially addressed in Article 9 of the SPC's Rules on Evidence in Civil Litigation, which provides that a party does not need to prove facts verified by non-appealable court judgments and rulings, unless there is contrary evidence that is sufficient to rebut those facts.[12]

D. Burden of Proof

The Judicial Interpretation deleted the general provision in the 2011 Draft that the plaintiff bears the burden of proving the existence of the alleged monopolistic conduct, loss, and causal link between the infringement and the damages complained of. Instead, Articles 7-9 detail the allocation of the burden of proof for horizontal agreements and abuse of dominance.[13] While similar to the 2011 Draft, the Judicial Interpretation may slightly increase plaintiffs' burden of proof.

1. Anti-Competitive Agreements

Like the 2011 Draft, Article 7 of the Judicial Interpretation allows defendants to prove that horizontal agreements to fix prices, limit output, divide markets, restrict the purchase or development of new technology or jointly boycott transactions had "no anti-competitive effect." It remains unclear whether the requirement that a defendant prove the absence of "anti-competitive effect" means that the defendant bears the burden of proving no antitrust damages/injury on plaintiffs during the damages phase of a trial or, more generally, indicates that defendants may show that an agreement was not illegal because it had "no anti-competitive effect." In many jurisdictions, including the United States and the EU, such horizontal agreements are considered ***per se*** illegal,

11 Article 32 of the AML provides that "[a]dministrative departments and other organizations authorized by laws or regulations to perform the function of administering public affairs may not abuse their administrative power to require, or require in disguised form, units or individuals to deal in, purchase or use only the commodities supplied by the undertakings designated by them"; Article 36 of the AML provides that "[a]dministrative departments and other organizations authorized by laws or regulations to perform the function of administering public affairs may not abuse their administrative power to compel undertakings to engage in monopolistic conducts that are prohibited by this law."

12 See SPC's Rules on Evidence in Civil Litigation, available at: http://www.court.gov.cn/bsfw/sszn/xgft/201004/t20100426_4533.htm.

13 Although the Judicial Interpretation does not address the question, a claim for antitrust damages arising from anti-competitive concentrations should also be possible under Article 1 of the Judicial Interpretation. However, litigation against administrative departments and other organizations authorized by laws or regulations to perform the function of administering public affairs for damages arising from abuses of administrative power would likely be treated as administrative litigation, which may be brought under the State Compensation Law.

regardless of their effect, though in U.S. civil litigation plaintiffs must still establish that they were injured in fact by the anti-competitive conduct and, during the damages phase of a trial, the approximate level of damages resulting from the ***per se*** illegal agreement.

Plaintiffs retain the burden of proof to show harm from vertical agreements to maintain resale prices. The SPC has stated that most vertical agreements will not create competition problems (unless both the suppliers and the purchasers have market power), so plaintiffs should bear the burden of proof when challenging vertical agreements.[14] The SPC's view is consistent with the AMEAs' (SAIC and NDRC). AMEA officials have reportedly indicated on a number of occasions that vertical agreements are not an enforcement priority.

2. Abuse of Dominance

As in the 2011 Draft, in most abuse-of-dominance cases, the plaintiff must prove that the defendant has a dominant position in the relevant market and that the defendant abused that dominance (Article 8). If this is established, the defendant bears the burden of proving an acceptable justification. The Judicial Interpretation drops the 2011 Draft's rebuttable presumption of dominance when the defendant operates in a relevant market without effective competition and transaction counterparties are highly dependent on the defendant's products or services.

The Judicial Interpretation retains the 2011 Draft's rebuttable presumption of dominance when the defendant is a public utility enterprise or holds an exclusive position according to law. However, the Judicial Interpretation requires that this presumption be established based on "specific facts of the relevant market's structure and its competition landscape."

E. Discovery

Given the lack of discovery procedures in China, particularly as compared to the United States, the 2011 Draft offered plaintiffs several options for gathering necessary evidence. For example, as mentioned above, plaintiffs could rely on non-appealable decisions by AMEAs. In addition, the court could compel defendants to submit relevant evidence under some circumstances. The 2011 Draft also implied that plaintiffs may be given access to leniency application files. All of these measures have been dropped in the final Judicial Interpretation. It remains to be seen how non-appealable AMEA decisions will be treated in civil proceedings and whether plaintiffs will be able to access AMEA's files relating to applications for leniency.[15]

14 See Interview of the responsible justice at the IPR tribunal of the SPC (May 9, 2012), available at: http://www.chinacourt.org/article/detail/id/516688.shtml. Interestingly, not long after the Judicial Interpretation was published, the first judgment in China regarding a vertical agreement under the AML was handed down (Beijing Rainbow Medical Equipment & Supplies Company ("Rainbow") v. Johnson & Johnson ("J&J")). On May 18, 2012, the Shanghai First Intermediate People's Court ruled for J&J in its dispute with Rainbow regarding resale price maintenance ("RPM"). J&J had terminated its distributor Rainbow for violation of J&J's RPM policy and for operating outside its authorized area. The court ruled against Rainbow because the latter did not prove (i) the anti-competitive effect of J&J's RPM (considering factors such as market shares, competitive landscape, the supply situation, and price fluctuation), (ii) Rainbow's antitrust damages, or (iii) the causal link. Under the Judicial Interpretation, if Rainbow brought an action under the second category of antitrust civil litigation ("a dispute arising from anti-competitive provisions of agreements, charter of associations, etc.") it remains unclear whether it would need to prove items (ii) and (iii).

The 2011 Draft also provided that public disclosure by listed companies and admissions by defendants could be regarded as ***prima facie*** evidence of dominance.[16] Although the Judicial Interpretation is less detailed in this regard than the 2011 Draft, it states that plaintiffs may rely on information publicly released by defendants (Article 10). If such information is sufficient to prove a dominant position, the court may rule based on this evidence.

In addition, the Judicial Interpretation drops the 2011 Draft's prohibition on the use of plaintiffs' commitments in AMEA investigations to presume the existence of an antitrust violation. It is now unclear whether courts may use defendants' commitments to infer the existence of monopolistic conduct.

F. Expert Witnesses

Under the Judicial Interpretation, parties are limited to two expert witnesses each (Article 12),[17] but they are not limited to economic experts or industry experts as indicated in the 2011 Draft. Additionally, the court may appoint independent experts to conduct market research or economic analysis on specific issues (Article 13).

G. Validity of Contracts

The 2011 Draft contained a controversial provision to the effect that a technology contract (or its relevant clauses) that had not been found to have violated the AML could still be voided if the court decided that the contract "unlawfully monopolizes technologies or impedes technology development" under Article 329 of the Contract Law. The Judicial Interpretation drops this provision, possibly signaling that the SPC recognizes that contracts violating Article 329 of the Contract Law do not necessarily run afoul of the AML. The Judicial Interpretation (Article 15) retains the general provision that contracts or charters of industry associations violating the AML shall be declared void by the courts.H. Statute of Limitations

Although the Judicial Interpretation deletes the explicit provision that the statute of limitations for AML cases is two years, it limits damages to two years (Article 16), the general statute of limitations in civil cases.[18]

15 Article 46 of the AML allows a company to seek immunity or a reduction in sanctions by reporting anti-competitive agreements to the AMEA and providing the AMEA with important evidence of the agreements. NDRC and SAIC implementing rules provide further details about their respective leniency programs. These two programs are not completely consistent with each other and leave many important questions unanswered.

16 See Article 9 of the 2011 Draft (providing that public disclosure by listed companies, admissions by defendants, and market research, economic analysis, monographic studies, and statistics provided by qualified independent third parties can be regarded as prima facie evidence for the purpose of proving dominance).

17 It is reported that in the April 18, 2012 Qihoo 360 v. Tencent trial before the High People's Court of Guangdong Province, both parties engaged two expert witnesses to testify. Qihoo 360 also engaged an expert economist to present an economic report.

18 See Article 135 of the General Principles of the Civil Law (providing that unless provided otherwise by law, the statute of limitations on application to a people's court for protection of civil rights shall be two years).

III. CONCLUSION

The Judicial Interpretation provides important guidance on antitrust civil litigation in China and should increase the consistency of the Chinese courts' application of the AML. However, the Judicial Interpretation is ambiguous on a number of issues, including indirect purchaser standing, plaintiffs' discovery rights, the interaction between court and AMEA proceedings (particularly whether a court may or should stay its proceedings during an AMEA's investigation), plaintiffs' access to leniency application documents, and the calculation of damages. The ambiguity on discovery issues is particularly striking, as one of the Judicial Interpretation's aims is to promote private enforcement of the AML by levelling the playing field between plaintiffs and defendants. Nevertheless, unless and until the AMEAs become more active in non-merger areas, private antitrust civil litigation will continue to play a prominent role in AML enforcement.

Evidence Rules in Private Antitrust Litigation in China

Dr. Hao Zhan[1*]

Since the enactment of China's Antimonopoly Law ("AML"), more private antitrust actions have been brought before Chinese courts. The majority of these cases concern monopoly agreements and abuse of market dominance. Plaintiffs include competitors in the relevant market, consumers, and the parties who transact with the business operators; defendants include business operators and trade associations. Actions include contractual and tortious disputes.

In April 2011, the Supreme Court of China published a consultation draft of the provision on the application of the laws on the trial of civil antitrust disputes (the draft judicial interpretation). It remains to be seen as to how many articles in this draft will become the juridical interpretation to be issued formally. The draft, containing only 20 articles, covers a broad spectrum of matters relevant to private antitrust litigation such as jurisdiction of courts, limitation of acting period, burden of proof, and evidence.

One of the most striking issues covered by the draft judicial interpretation is the evidence rules. This article expands upon the critical aspects of evidence rules in private antitrust litigation in China that would be affected by the proposed draft.

I. ADMISSIBLE EVIDENCE

Article 63 of the Civil Procedure Law provides that evidence shall be classified as follows:

- Documentary evidence;
- Material evidence;
- Audio-visual reference material;
- Testimony of witnesses;
- Statements of the parties;
- Expert conclusions; and
- Records of inquests.

1 Grandall Law Firm

Any of the above–mentioned evidence must be verified before it can be taken as a basis for ascertaining a fact. It is noteworthy that the draft juridical interpretation (Article 13) provides that the parties may apply to the court to have economics or trade experts provide explanations on technical issues. The parties may apply to the court to appoint, or the court on its own initiative may appoint, independent organizations or professional experts to carry out market investigations or compile economic analysis reports on technical issues. Although evidence from experts has been mentioned in previous laws and juridical interpretations, this is the first time that civil procedure rules in China have provided specific rules on expert evidence.

II. EVIDENCE PROTECTED BY LEGAL PRIVILEGE

Confidentiality between a client and a lawyer is not recognized by the Chinese Lawyer Law, the Civil Procedure Law, nor related regulations. Such evidence is therefore not protected by legal privilege, regardless of whether the advice comes from external legal counsel or in-house counsel. Some scholars and experts believe that legal privilege will be codified into law, but this is not yet on the legislative agenda.

Trade secrets are also not privileged in China. Article 17 of the Provisions of the Supreme People's Court on Evidence in Civil Procedures expressly provides for collecting trade secrets as one of the grounds for a party to apply to the court to obtain evidence. Trade secrets are thus clearly discoverable under Chinese laws. Specific rules are in place to contain the use of trade secrets in court proceedings. Article 120 (2) of the Civil Procedure Law states that a case involving trade secrets may be heard in a court closed to public if the party requests so.

However, the draft judicial interpretation proposes more extensive protection to trade secrets in private antitrust actions. It proposes to allow parties to apply to the court to take effective steps to protect trade secrets, such closing the hearing from the public, restricting or forbidding duplication of evidence, limiting the presentation of evidence to the legal representatives of the parties, and ordering the parties to enter into undertakings for confidentiality.

III. EFFECTIVENESS OF THE EVIDENCE IN CRIMINAL PROCEEDINGS AND LENIENCY

The evidence or findings in criminal proceedings can be relied upon by plaintiffs in parallel private actions. According to the Civil Procedure Law, facts verified by a valid judgment in other litigation—including criminal, civil and/or administrative litigation— are accepted automatically in civil litigation, unless the defendant can provide sufficient evidence to rebut it.

Until now, there has been no detailed leniency regulation in China. Article 46 of the AML briefly addresses leniency policy: when a business operator voluntarily provides the antimonopoly law enforcement authority with crucial evidence and information relating to monopoly agreements, the authority can lower or waive the punishment meted out to the business operator. Specific details on the operation of Article 46 have been included in regulations issued by the enforcement authority, such as those contained in Articles 11, 12, and 13 of the

Regulations of the Industrial and Commerce Administrative Authority regarding the prohibition on monopoly agreement activity, issued by the State Administrative of Industry and Commerce in December 2010.

However, the draft judicial interpretation contains no provisions on how the leniency rule would apply in private antitrust litigation. The only reference to the rule is contained in Article 14 of the draft, proposing that information and evidence provided by leniency applicants that has not been made public may be protected by the court using the same measures for evidence in antitrust litigation that contains national or trade secrets or privacy of the individual.

Public Enforcement Against Cartels in China

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China's Anti-Monopoly Law ("AML") is entering its fourth year since taking effect on August 1, 2008.[3] Regulations, rules, and cases are still in development and it is expected that these outcomes will further shape antitrust law not only in China, but overall antitrust practice around the world.

Cartelization has long been recognized as classic monopolistic behavior. China, too, acknowledges the problem in Chapter II in the AML. Article 13 prohibits horizontal monopoly agreements, while Article 14 prohibits vertical monopoly agreements. The two administrative agencies handling public enforcement against cartels, the National Development and Reform Commission ("NDRC") and the State Administration for Industry and Commerce ("SAIC") investigate some cartel cases, although not all of the results of these investigates are disclosed to the public.[4]

I. PUBLIC ENFORCEMENT VERSUS PRIVATE ENFORCEMENT

China is a civil law jurisdiction and, as such, a statute is the primary source of law with respect to pursuing anti-cartel actions. The AML itself contains only 57 articles. Therefore, antitrust enforcement in China relies heavily on the implementing rules for public enforcement by administrative agencies and the judicial interpretations for private enforcement by the Supreme People's Court.

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3 The AML was enacted by the National People's Congress, China's top legislative body, on August 30, 2007.

4 In the Chinese governing system, a San Ding (三定, meaning "three points" or "three decisions") is a document approved by the State Council that sets out the duties of the administrative organ, its departments and the staffing. According to the San Ding, there are three ministries that serve as AML enforcement authorities: the Ministry of Commerce ("MOFCOM") reviews mergers, while the NDRC and SAIC handle cartels and investigations into abuse of dominance. The NDRC reviews cases involving pricing issues and SAIC handles those without pricing issues.

Both the NDRC and SAIC promulgated their Implementing Rules for anti-cartel enforcement by end of 2010.[5] The Supreme People's Court's Judicial Interpretation is still in the draft stage.[6] This partially explains why public enforcement against cartels by the administrative agencies prevails over private enforcement by courts.[7]

It should further be noted that China lacks the culture, incentives, and litigation mechanisms that encourage private actions, such as triple damages and class action lawsuits in the United States. Thus it is more likely for the administrative agencies to play a leading role in AML enforcement, and this is also the case with anti-cartel enforcement.

II. CASE ANALYSIS

When comparing the levels of enforcement activity between the NDRC and the SAIC, the NDRC is the more aggressive body. At the end of 2011, the NDRC announced a total of four investigations against cartels. The SAIC, on the other hand, announced only one case.

The NDRC conducted three cartel investigations in 2010: two agricultural products cases (the Rice Noodle Case[8] and the Green Bean Case[9]) and a cartel case involving a trade association. It is unsurprising that the NDRC's first two cases involved price hikes of agricultural products, given the central government's history of dedication to price stability for necessary goods and the great pressure of inflation at that time. It is also noteworthy that for the first two cases, NDRC relied on the Price Law more than the AML to reach its decisions. Although the Price Law has largely given way to the AML due to substantial overlap, the NDRC has been the authority to enforce the Price Law since 1997, and NDRC officials are more familiar with the Price Law than the AML.

The NDRC's investigation against price cartels in the paper making industry in 2011[10] marks a turning point where the agency began to rely more on the AML than on the Price Law. In 2010, the Paper Making Trade Association of Fuyang City in Zhejiang Province held five member meetings to coordinate the price increase for

5 The NDRC issued the Anti Price Monopoly Rules and the Rules on the Administrative Procedures for Law Enforcement Against Price Monopoly on December 29, 2010. They came into effects on February 1, 2011. SAIC issued three Rules on December 31, 2010, namely, Rules on Prohibition of Abusing Dominant Market Position, Rules on Prohibiting Monopoly Agreements, and Rules on Prohibiting Abusing Administrative Powers. These three Rules took effect on February 1, 2011.

6 The Supreme People's Court issued the Draft Judicial Interpretation for public comment in April 2011. It is expected to be promulgated in 2012. See http://www.court.gov.cn/gzhd/zqyj/201104/t20110425_19850.htm (text in Chinese).

7 Judge Zhu Li from the Supreme People's Court noted in his speech (presented in Beijing at the 2011 Forum on Anti-Monopoly Civil Litigation in China, organized by the Competition Law Centre of UIBE and T&D Associates on June 25, 2011) that China's judicial system as a whole accepted around 70 civil AML actions by the middle of 2011. Most of these cases were alleged as abuse of dominance cases, and a few involved cartel allegations.

8 See http://news.xinhuanet.com/fortune/2010-03/30/content_13271788.htm (text in Chinese).

9 See http://www.chinanews.com/cj/2010/07-17/2408374.shtml (text in Chinese).

10 See http://www.chinanews.com/cj/2011/01-04/2764453.shtml (text in Chinese).

packing papers. Such behavior was found by the NDRC to constitute a price cartel. The trade association was fined 500,000 RMB, the upper limit of such a fine under Article 46 of the AML.

In 2011, the NDRC conducted a high-profile investigation of abuse of dominance against China Telecom and China Unicom, two giant state-owned enterprises. At the same time, the NDRC announced an investigation decision for a cartel case. Two medicine distributors in Shandong province were found guilty of jointly controlling the supply of a medicine's raw materials, and then raising prices of the medication.[11] The NDRC in this investigation referred only to the AML, without any mention of the Price Law.

The SAIC, compared to the NDRC is relatively low-profile. The authority announced only one case against cartel. In 2009, a trade association for the concrete industry in Lianyungang city of Jiangsu province organized its 16 member companies to enter into an agreement to coordinate the concrete supply in the city and prohibit any sales without permission of the association. The SAIC fined the trade association 200,000 RMB and also fined five of the 16 member companies.[12]

III. COMPARING THE NDRC WITH THE SAIC

Two factors contributed to the NDRC's high-profile investigation, especially in 2011. First, the Chinese central government approved the NDRC's request to expand its AML enforcement team in July 2011. The Price Supervision and Inspection Department handles AML enforcement in the NDRC, and was subsequently renamed as the Price Supervision and Inspection and Anti-Monopoly Bureau. Following this restructuring, the NDRC added twenty more officials to its quota.

Second, the NDRC is a powerful ministry under the State Council. Although its stature has been steadily diminishing as reforms move forward, the NDRC is arguably the politically most powerful of the three agencies (MOFCOM, SAIC and NDRC). The NDRC is the successor to the State Planning Commission that was set up in 1952 to run China's economy. The NDRC is also responsible for the enforcement of the Price Law.

Yet the role of the SAIC should not be understated. SAIC only had one case to announce, but the agency has fulfilled its responsibilities using closed-door investigations. SAIC is a smaller ministry in terms of size and official numbers. However, it has much experience handling unfair competition cases, and is the only agency that enforces the Anti-Unfair Competition Law in China.

III. THE FUTURE OUTLOOK

As the two authorities handling anti-cartel enforcement, the NDRC and the SAIC promulgated the implementing rules. However, both agencies intentionally avoided the issue of vertical agreement. In the *Anti Price Monopoly Rules*, NDRC simply duplicated Article 14 of the AML, unlike the further clarification it provided to

11 See http://www.ndrc.gov.cn/xwfb/t20111114_444330.htm (text in Chinese).

12 See http://www.antimonopolylaw.org/article/default.asp?id=2837 (text in Chinese).

other behavior, such as horizontal agreements and abuses. In the ***Rules on Prohibiting Monopoly Agreements***, the SAIC did not pen a single word on vertical agreement, even as it created four articles to address the specific categories of horizontal agreements. Vertical agreements were mentioned in the previous draft version of the implementing rules, but were eventually removed.

Moreover, the four cartel investigations by the NDRC and the sole cartel investigation by the SAIC involve horizontal agreements; there has yet to be brought a single case of vertical agreement. Vertical agreements continue to occupy a complex and controversial area for China AML enforcement, and we expect this issue to be clarified slowly in the coming years. Such clarification would possibly be taken via future revisions to the implementing rules of the NDRC and the SAIC.

Another angle with which to observe enforcement of the AML is that four of the five NDRC investigations were against cartels, as was the SAIC's one announced case. Even when taking unannounced cases into account, cartel enforcement still prevails over dominance abuse enforcement. Such a phenomenon may be explained by the fact that Chinese companies and individuals are still learning and exploring the new law, and the higher burden of proof poses obstacles for the administrative agencies and potential plaintiffs.

Chinese agencies and companies are becoming more familiar with the AML, and as abundant experiences from foreign jurisdictions such the U.S. and the EU are introduced into China, it is safe to predict that more cartel investigations will occur in China. The more controversial area of vertical agreements may also enter into the scope. With the addition of 20 officials, the NDRC's antitrust team is now the same size of that of MOFCOM; the NDRC is poised to continue playing an aggressive role in China's anti-cartel enforcement in the coming years.

With more limited human resources[13] than their western counterparts, the AML enforcement agencies' capacity of public enforcement is highly constrained. There will be more private actions brought before courts, and after the Judicial Interpretation by the Supreme People's Court is promulgated in 2012, cartel players will be facing challenges from competitors and consumers in addition to the administrative agencies. It will be interesting to observe potential conflicts in procedure between the courts and administrative agencies, and their eventual resolution.

13 MOFCOM's antitrust team is comprised of about 30 people; the NDRC amounts to the same number after its expansion, and the SAIC has fewer than ten officials.

Recent Amendments to Hong Kong's Competition Bill

Ping Lin[1*]

Jingjing Zhao[2**]

I. INTRODUCTION

After more than a decade of policy study and two rounds of public consultation, the Hong Kong Government submitted its Competition Bill for the Legislative Council's ("LegCo") approval in July 2010. The Bill marked a giant step toward establishing a comprehensive competition law in Hong Kong.

Although widely regarded as well-crafted legislation by international experts, the Bill received strong criticisms from within Hong Kong, particularly from small and medium-sized enterprises ("SMEs"). They raised the following arguments:

(a) The general prohibition against anticompetitive agreements is difficult to understand and comply with;

(b) The payment requirement of infringement notice may place a significant burden on SMEs;

(c) The *de minimis* arrangements should be laid down in the law to give more certainty to SMEs;

(d) The penalty cap of 10 percent of global turnover for each year in which the contravention has occurred is too severe; and

(e) Large companies may use private action to harass SMEs.

In response, the Government introduced six major changes to the Bill at the LegCo Bills Committee meeting on October 25, 2011.

II. DISTINGUISHING BETWEEN "HARDCORE" AND "NON-HARDCORE" VIOLATIONS

The Government proposed to distinguish "hardcore" violations from "non-hardcore" ones. The former category was to be defined as price-fixing, bid rigging, market allocation and output control. The latter group included violations of the first conduct rule prohibiting anticompetitive agreements and concerted practices.

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III. FINES AND INFRINGEMENT NOTICE MECHANISM

The original infringement notice mechanism provided that the Competition Commission could require an infringing party to pay up to HK $10 million (approximately U.S. $1.28 million) in addition to admitting and ceasing the infringement. To address the SMEs' concern of having to pay financial penalties even in a settlement, the Government proposed to remove the Commission's right to impose the fine.

Additionally, infringement notice would not be applied to cases involving non-hardcore breaches of the first conduct rule. Instead, a "warning notice" will be issued to request the relevant undertaking(s) to cease the infringement within a specified period, and only continued infringement after the warning period would attract legal consequences.

IV. "DE MINIMIS" FRAMEWORK

To provide greater certainty to SMEs, the Government proposed to introduce a "***de minimis***" framework into the Bill in the form of an exclusion from the first conduct rule for all agreements among undertakings with a combined turnover not exceeding HK $100 million in the preceding financial year. This threshold was adopted because (1) it is easier to determine turnover than market share, which requires a definition of the relevant market for each and every agreement; and (2) the average annual business turnover of SMEs has been steady throughout 2005 to 2009 at about HK $11 million, according to government statistics. However, exclusion would not apply to "hardcore" anti-competitive activities, because these activities almost always have an "appreciable adverse effect on competition." The threshold can be amended through subsidiary legislation when circumstances change.

As for the abuse of a substantial degree of market power prohibited by the second conduct rule of the Bill, a similar ***de minimis*** arrangement is adopted, with a threshold of HK $11 million.

V. MAXIMUM PENALTY

In the original Bill, the maximum penalty in relation to a "single contravention" was 10 percent of the turnover of the undertaking concerned, for each year in which the contravention occurred.

The statutory maximum is now capped at 10 percent of the undertaking's total local turnover (deriving from all businesses, not only those relating to the contravention) for each year of infringement, but only up to a maximum of three years. If the infringement lasted for more than three years, the three years of infringement with the highest sales would be chosen.

VI. PRIVATE ACTIONS BEFORE THE COMPETITION TRIBUNAL

The Bill originally provides that in addition to public enforcement by the Competition Commission, the special court of Competition Tribunal would also hear damages claims brought by private parties, with or without a determination of infringement in prior public enforcement.

The Government proposed to remove the right altogether. As a result, private actions can only be carried out following a successful prosecution brought by the Commission. The government may restate stand-alone private actions "in a few years' time," once the business community acquires more experience with the new competition regime.

VII. MERGERS EXCLUDED

Lastly, although the specific merger rule in the original Bill is confined to M&A transactions relating to telecommunications licensees, the broad wording of the conduct rules made it possible for them to be used to challenge M&A activity in other sectors. The government has now expressly excluded mergers from the scope of application of the conduct rules.

VIII. CONCLUSION

Following the Government's release of the amendment proposal, LegCo's Bills Committee held a public hearing to invite comments on the amendments.

The SMEs mostly welcomed the changes, but many Councilors expressed concerns that the proposed turnover threshold under the second conduct rule was too low and that many SMEs would in practice exceed this threshold.

A similar concern was expressed regarding the proposed ***de minimis*** threshold under the first conduct rule. The Government refused to raise these thresholds, stating that its proposal was already more lenient than the regime in other jurisdictions where no ***de minimis*** rules exist for abuse of dominance rules. The Government also refused to replace the proposed "substantial degree of market power" test by the "dominance" test, re-stating its position that the former is more appropriate for Hong Kong, given its small and geographically concentrated economy to tackle anticompetitive conduct in oligopolistic markets.

Taken together, the six proposed amendments may have been too big a concession. The perceived benefits will undoubtedly come at a cost. The reduction in the maximum penalty and the removal of the stand-alone private action will significantly lower the deterrence effect of the law, which may in the end hurt the SMEs (and consumers) who are frequently victimized by anticompetitive conduct of their upstream suppliers and dominant rivals in the markets.

One controversial issue not touched upon in this round of amendment is the Competition Bill's exclusion of quasi-governmental statutory bodies, many of which are engaged in economic activities and compete with private undertakings. The Government is supposedly reviewing the 500-strong local statutory bodies in order to come up with a list of those not benefiting from the exclusion, yet the release of this list has been postponed many times. When it is eventually released, the list will certainly be subject to close public scrutiny before the Competition Bill is expected to pass into law in July 2012.

A Competition Law for Hong Kong

Marc Waha

Julienne Chang[1*]

The Competition Ordinance 2012 was adopted by the Hong Kong Legislative Council on June 14 and signed into law by the Chief Executive on June 21.[2] The Ordinance represents a major milestone on the way towards comprehensive competition policy reform in Hong Kong. It establishes a Competition Commission with wide-ranging investigative powers and a Competition Tribunal that can apply severe sanctions. Many forms of competition restrictions that were hitherto tolerated are prohibited under the law.

But the adoption of the Ordinance, while a significant step, is not the last one. The Ordinance will enter into force at a date to be set by the Secretary for Commerce. The Administration has indicated that the institutional provisions would take effect first to allow for the establishment of the new authorities, with the substantive provisions of the Ordinance becoming effective later, presumably after initial enforcement guidelines are issued by the Competition Commission. The Commission is required to consult the public on proposed guidelines. As a result, it would be surprising if the new competition regime were to become effective before 2014.

A brief description of the tortuous legislative history may shed some light on the challenges ahead for the Competition Commission. This is the focus of our first section. The following sections describe the scope of the Ordinance and its enforcement mechanisms.

I. A DIFFICULT GENESIS

The introduction of cross-sector competition law was first proposed within the Legislative Council in the 1990s.[3] Nearly 20 years of debate, expert reports, public consultations, hearings, and bills committee meetings ensued. The process concluded with a final five-day flourish of plenary debate in the Legislative Council, and the Competition Ordinance was adopted a little after 10:00 P.M. on June 14. Rarely has a competition law statute generated so many discussions.

1 * Norton Rose Hong Kong.

2 An Ordinance to prohibit conduct that prevents, restricts or distorts competition in Hong Kong; to prohibit mergers that substantially lessen competition in Hong Kong; to establish a Competition Commission and a Competition Tribunal; and to provide for incidental and connected matters; Ordinance No 14 of 2012, Hong Kong Official Gazette (June 22, 2012), p. A1323.

3 See Motion for the adoption of legislation on fair trade, moved by Dr. Law Cheung-kwok, Official record of proceedings of the Hong Kong Legislative Council of May 29, 1996, with a discussion of a similar motion introduced in 1992 by the Honorable Fred Li.

Behind the political folklore lie real issues worthy of debate. Why would Hong Kong, an economy consistently rated as among the world's most competitive, need to adopt legislation and create dedicated institutions to preserve market competition? Is the primary goal of the Ordinance to enhance allocative efficiency in the Hong Kong markets, or is it to ensure that Hong Kong consumers get a fairer share of economic efficiencies, in a context where many goods and services produced in Hong Kong are exported and consumed abroad?

The original Competition Bill introduced by the Government in July 2010 provided few answers to these questions. It contained extremely detailed provisions on procedure and institutions but very little detail on substance. Unfortunately, the legislative debate did not add much clarity. Most of the arguments heard during the Bills Committee meetings related to the impact of the law on small and medium enterprises ("SMEs") and on the appropriate level of sanctions. Government representatives did explain the Administration's policy intent on a few matters, but overall the legislation that was ultimately adopted fails to embody a clear economic policy.

This of course is nothing new to competition law practitioners, who have long had to deal with the very broad principles-based provisions of competition legislation elsewhere. The loose wording of the US Sherman Act and of the relevant articles in the EU Treaties has allowed major shifts in competition policy over time. The Hong Kong law is in this respect very similar to that adopted in other jurisdictions, as it leaves a large degree of flexibility to courts and enforcers in setting competition policy.

The lack of a clear articulation of policy objectives is nevertheless unfortunate. Different economies may justify different objectives and legal tests.[4] Many of the jurisdictions that have introduced competition law in the last two decades did so at the time their markets were deregulated and their economies were transitioning towards market-based principles. Policy objectives in this context were relatively straightforward, and these jurisdictions could rely on foreign (mainly EU) precedent when interpreting their regimes. In contrast, Hong Kong has for a long time been an open market economy largely free of government intervention, and there are no signs that the markets where the State's influence is strong (such as land supply) will be deregulated soon. In other jurisdictions, adopting competition law meant less market regulation. In Hong Kong the adoption of the Competition Ordinance is perceived as an increase in regulation.

The original Hong Kong context may therefore have warranted the inclusion of clear guiding principles in the Ordinance. The lack of clarity in this regard leaves a number of important questions open, and it will be up to the Competition Commission to set a path for Hong Kong's competition policy.

II. PERSONS SUBJECT TO THE COMPETITION ORDINANCE

In line with EU law, the Ordinance applies to "undertakings." Any entity engaged in economic activity, regardless of its legal status or the way in which it is financed, is subject to the Ordinance.

4 See Thomas K. Cheng, Convergence and Its Discontents: A Reconsideration of the Merits of Convergence of Global Competition Law, 12 Chi. J. Int'l L. 433 (2012).

The Ordinance contains a patchwork of exclusions and exceptions mainly benefiting SMEs and statutory bodies. However, as a consequence of the way they are structured, virtually no undertaking—including SMEs and statutory bodies—can afford to completely ignore the provisions of the Ordinance.

A. Statutory Bodies

Section 3 of the Ordinance excludes all statutory bodies from the scope of the substantive provisions of the law, except for those statutory bodies listed in a separate regulation that will be adopted by the Chief Executive in Council. Under current proposals, the Government will adopt a regulation that would subject the activities of six statutory bodies to the Ordinance, out of a total of 581 such bodies in Hong Kong. Despite the exclusion, the Administration stated during the legislative debate that it will ensure that these bodies would still be required to act consistently with the principles underlying the competition rules.[5]

Rather mystifyingly, the Ordinance abandons the notion of undertaking in favor of a legalistic approach: only those persons that are incorporated as a statutory body will be excluded. This peculiar approach suggests that statutory bodies must comply with the substantive provisions of the Ordinance as soon as they engage in economic activity through a private law subsidiary. The approach is similar to that under the Singapore Competition Act, and Government-owned entities in Singapore know that the exclusion only affords limited protection.[6]

B. Small and Medium Enterprises

Sections 5 and 6 of Schedule 1 exclude certain conduct by undertakings whose turnover remains below certain thresholds. These exclusions are, however, partial—some hardcore conduct is never excluded—and are in some cases impractical (for example, the exclusion from the prohibition on restrictive arrangements only applies when the combined turnover of all undertakings involved is below the threshold).

C. Other Specified Persons

Finally, pursuant to section 4 of the Ordinance, the Chief Executive in Council may also disapply the substantive provisions in relation to a "specified person" or "persons engaged in specified activities." The Ordinance does not provide any criteria for such exclusion, despite calls for more guidance from several Legislative Councilors during the review of the Bill.

5 See Gregory So Kam-leung, Secretary for Commerce and Economic Department, Speech, Official record of proceedings of the Hong Kong Legislative Council (June 6, 2012).

6 See Section 33(4) of the Competition Act. The first decision of the Competition Commission of Singapore finding an abuse of dominance concerned a government-linked company, SISTIC. At the time of the hearing, SISTIC was owned 65 percent by the Singapore Sports Council (SSC) and 35 percent by The Esplanade Co. Ltd. (TECL). TECL was a public company limited by guarantee and owned by the Ministry of Information, Communications and the Arts. SSC was a statutory board under the oversight of the Ministry of Community Development, Youth and Sports. See Notice of Infringement Decision issued by the Competition Commission of Singapore - Abuse of a Dominant Position by SISTIC.com Pte Ltd, June 4, 2010, Case number: CCS 600/008/07. SISTIC in its appeal (which was rejected on May 28, 2012) did not contest the finding that it was subject to the Competition Act.

III. THE SUBSTANTIVE COMPETITION RULES

The Ordinance introduces two of the traditional three pillars of a competition law regime: a prohibition on restrictive agreements and a prohibition on the abuse of market power.

Despite its full title ("An Ordinance […] to prohibit mergers that substantially lessen competition in Hong Kong") and references to "the merger rule," the Ordinance does not introduce a comprehensive merger control regime. Rather, it modernizes the existing rules for review of concentrations involving telecommunications carrier licensees. Merger activity in other sectors of the economy is clearly out of scope. Section 4 of Schedule 1 expressly keeps mergers out of reach from enforcement of the two conduct rules, although it is not clear whether ancillary merger restrictions such as non-compete covenants are also excluded.

A. The First Conduct Rule: The Prohibition on Restrictive Agreements

The Ordinance adopts in section 6 a general prohibition on anticompetitive agreements and concerted practices between undertakings as well as decisions of an association of undertakings which have the object or effect of preventing, restricting or distorting competition in Hong Kong. The rule applies irrespective of whether the conduct took place in Hong Kong or abroad, as long as its object or effect is to prevent, restrict, or distort competition in Hong Kong.

While the substantive legal test under the first conduct rule is the same for all conduct, the enforcement focus is expected to be on serious anticompetitive activity, which the Ordinance defines as price-fixing, market sharing, output restrictions and bid-rigging. This is because of specific procedural rules that will apply to non-serious anticompetitive conduct.

The first conduct rule does not distinguish between horizontal and vertical arrangements. The Administration stated during the legislative process that, in its view, vertical restrictions would only raise competition issues when they involve suppliers with market power or when a supply agreement is entered into among competitors.[7] It will be up to the Competition Commission to set the policy in this regard.

B. The Second Conduct Rule: The Prohibition on the Abuse of Market Power

Section 21 of the Ordinance provides that an undertaking that has a substantial degree of market power in a market must not abuse that power by engaging in conduct that has as its object or effect the prevention, restriction or distortion of competition in Hong Kong. Again, the rule applies irrespective of whether the conduct took place in Hong Kong or abroad.

It is noteworthy that the Ordinance refers to the substantial degree of market power test rather than the more commonly used dominance test. After arguing for a while that there was little difference between the two

7 See Draft Guidelines on the First Conduct Rule, ¶ 2.5, Commerce and Economic Development Bureau, CB(1)2336/10-11(01), May 2011.

tests, the Government representatives stated that the Administration wished to retain a lower market power threshold in the Ordinance, as several sectors of the economy—mainly food retail markets—have an oligopolistic structure.[8] While intent on adopting a low threshold, the Secretary for Commerce mentioned during his final policy address that a market share of 40 percent may be indicative of a substantial degree of market power, and that undertakings with a market share below 25 percent should benefit from a safe harbor as they would be unlikely to possess market power.[9] Despite these policy statements, the law itself does not provide guidance on the meaning of "a substantial degree of market power," and it will be up to the Competition Commission to form a view.

Section 21 provides an illustrative list of conduct that may constitute an abuse of market power: predatory behavior towards competitors; and limiting production, markets or technical development to the prejudice of consumers. The law provides no example of exploitative abuse.

In a bizarre twist, Schedule 8 of the Ordinance introduces a new specific rule for exploitative abuses in the telecommunications sector for licensees in a dominant position. The specific reference to exploitative abuses in this ad hoc provision may suggest that these are not meant to be captured under the general abuse of market power regime under section 21. Again, it will be up to the Competition Commission to provide guidance on these questions.

C. Exemptions and Exceptions

Sections 31 and 32 of the Ordinance list the only two real exemptions in the law: the Chief Executive in Council may (but has no obligation to) exempt certain agreements or conduct on public policy grounds or to avoid conflict with international obligations. The Chief Executive in Council retains relatively broad discretion whether to grant exemptions under these sections.

All other causes for exclusion, which are listed in Schedule 1, are designed as exceptions: parties must benefit from the exclusion as soon as specified conditions are met. Parties may therefore self-assess whether the conditions for exclusion are met. These five exclusions are as follows:

neither of the conduct rules applies to conduct if it is made to comply with a binding Hong Kong legal requirement;

neither of the conduct rules applies to undertakings entrusted with the operation of services of general economic interest insofar as these rules would obstruct the performance of these services;

the first conduct rule does not apply to agreements that enhance economic efficiency, when certain conditions (including that a fair share of benefits accrues to consumers) are met;

8 See Responses to outstanding issues arising from previous meetings, ¶ 11, Commerce and Economic Development Bureau, CB(1)1450/11-12(02), March 2012.

9 See So Kam-leung, supra note 4.

the first conduct rule does not apply to agreements and concerted practices between undertakings or decisions by associations where the aggregate annual turnover of the undertakings involved does not exceed HKD200 million, except where the conduct qualifies as serious anticompetitive conduct; and

the second conduct rule does not apply to undertakings whose annual turnover is below HKD40 million.

While the Ordinance does not expressly exclude competition restrictions that are not appreciable, the Competition Commission may well consider that restrictions involving undertakings with small market shares will not be caught by the conduct rules. Further, despite the lack of an express efficiency exclusion under the second conduct rule, undertakings with market power are also expected to be able to rely on an objective justification defense.[10] The Competition Commission will provide guidance on these questions in its guidelines.

Overall, save for the turnover-based exclusions in favor of SMEs, the regime is broadly in line with the law in the EU or in Singapore.[11]

IV. ENFORCEMENT

The Ordinance establishes two enforcement bodies: the Competition Commission and the Competition Tribunal. The former is to investigate and bring cases before the latter, which will hear and make the final decisions.

10 See Draft Guidelines on the Second Conduct Rule, ¶ 6.4, Commerce and Economic Development Bureau, CB(1)2618/10-11(01), June 2011.

11 In Singapore, the section 34 prohibition does not apply to the matters specified in the Third Schedule to the Competition Act by virtue of section 35. These are (i) an undertaking entrusted with the operation of services of general economic interest or having the character of a revenue-producing monopoly, insofar as the prohibition would obstruct the performance, in law or fact, of the particular tasks assigned to that undertaking; (ii) an agreement to the extent to which it is made in order to comply with a legal requirement, that is any requirement imposed by or under any written law; (iii) an agreement which is necessary to avoid conflict with an international obligation of Singapore, and which is also the subject of an order by the Minister; (iv) an agreement which is necessary for exceptional and compelling reasons of public policy and which is also the subject of an order by the Minister; (v) an agreement which relates to any product to the extent to which any other written law, or code of practice issued under any written law, relating to competition gives another regulatory authority jurisdiction in the matter; (vi) an agreement which relates to any of the following specified activities: the supply of ordinary letter and postcard services by a person licensed and regulated under the Postal Services Act; the supply of piped potable water; the supply of wastewater management services, including the collection, treatment and disposal of wastewater; the supply of scheduled bus services by any person licensed and regulated under the Public Transport Council Act; the supply of rail services by any person licensed and regulated under the Rapid Transit Systems Act; and cargo terminal operations carried out by a person licensed and regulated under the Maritime and Port Authority of Singapore Act; (vii) an agreement which relates to the clearing and exchanging of articles undertaken by the Automated Clearing House established under the Banking (Clearing House) Regulations; or any related activities of the Singapore Clearing Houses Association; (viii) vertical agreements other than vertical agreements as the Minister may by order specify; (ix) an agreement with net economic benefit; (x) any agreement that is directly related and necessary to the implementation of a merger; and (xi) any agreement (either on its own or when taken together with another agreement) to the extent that it results, or if carried out would result, in a merger.

A. The Competition Commission Investigates and Provides Guidance

The Commission is a new authority comprising between five and 16 members appointed by the Chief Executive for a renewable three-year term.

One of the Commission's principal tasks is to investigate possible infringements. It has wide-ranging investigation powers, including the power to order the production of documents and other information, and to hear relevant persons. It can also conduct surprise on-site inspections ("dawn raids") after obtaining a warrant from the Court of First Instance. It may also conclude leniency agreements granting beneficial treatment in return for a person's cooperation in an investigation.

The Commission is also vested with some remedial powers: it can put a violation to an end by accepting commitments from investigated parties or by sending warning notices.

The Commission is tasked with providing guidance through the adoption of guidelines or the issuance of individual guidance decisions on whether conduct benefits from an exclusion or an exemption. The Commission can also adopt block exemption orders, on application or of its own motion, if it is satisfied that a particular category of agreements enhances economic efficiency.

Finally, it has an advocacy role, i.e., it must promote public understanding of competition law and the adoption of compliance mechanisms by businesses.

B. Different Procedures Depending on the Seriousness of the Alleged Infringements

During the legislative process, many SMEs argued that the indiscriminate treatment of all anticompetitive conduct in the Bill would represent a significant burden, as there was no guarantee in the statute that an inadvertent breach of a less serious nature would not attract a heavy fine.

To assuage these concerns, the enforcement regime ultimately retained in the Ordinance distinguishes between serious and non-serious anticompetitive conduct:

if the alleged infringement amounts to one of the four types of serious anticompetitive conduct under the first conduct rule or if an infringement of the second conduct rule is alleged, the Commission may either directly bring proceedings in the Tribunal, or first issue an infringement notice, offering not to bring those proceedings on condition that the defendant makes a commitment to comply with requirements of the notice;

if, on the other hand, the alleged infringement does not amount to serious anticompetitive conduct under the first conduct rule and if no infringement of the second conduct rule is alleged, the Commission must first issue a warning notice requesting the relevant undertaking to cease the relevant conduct; should the undertaking fail to rectify the anticompetitive conduct in compliance with the warning notice, the Commission may bring proceedings against that undertaking, but only in respect of the period after the warning notice has been issued.

C. The Competition Tribunal Hears Cases, Imposes Remedies and Grants Follow-on Damages

The Competition Tribunal is a new court established by the Ordinance. The existing judges of the Court of First Instance will sit as a specialized jurisdiction, following specific procedures likely to be less formal than in civil cases.

A range of remedies is available to the Tribunal for contravention of a competition rule. These include a maximum pecuniary penalty of 10 percent of the local turnover of the infringing undertaking for each year of infringement (up to a maximum of three years), damages, interim injunctions and director disqualification orders for a maximum duration of five years.

Persons who have suffered loss or damage as a result of a contravention of the conduct rules will have a right of action before the Competition Tribunal. However, proceedings may only be brought after a contravention has been established. It is not entirely clear whether parties to a contractual dispute could invoke a violation of the Ordinance without first having to wait for a decision from the Competition Commission or the Competition Tribunal.

V. CONCLUSION

Once the new authorities will have been established, the Competition Commission will prepare guidelines for public comment. As many policy questions remain open, one may expect significant debate to occur in the context of these consultations. It may well be that the initial guidelines will only provide a high-level direction. The enforcement model nevertheless provides a good framework for authorities to develop competition policy without making companies bear too many of the costs resulting from the remaining uncertainties.

As was the case in many other competition law jurisdictions, it will take time before a clear policy emerges under the Ordinance, and even longer before its effects are felt on the Hong Kong markets.

Hong Kong's First Economy-Wide Competition Law: A Review of the Law and the Challenges Ahead

Margaret Wang*

I. INTRODUCTION

Traditionally seen as averse to regulation, perhaps best exemplified by the maxim "small government, big market," Hong Kong has finally joined the growing ranks of Asian jurisdictions that formally regulate competition across all sectors of the economy. After two rounds of heated public consultations and a long legislative passage, Hong Kong's first economy-wide competition law, the Competition Bill ("the Bill"), was formally signed into law, on June 22, 2012.

The Competition Ordinance ("the Ordinance") imposes behavioral competition law provisions and prohibits anti-competitive conduct by multiple undertakings and unilateral anti-competitive conduct by a single undertaking. The merger control regime will remain confined to transactions involving telecommunications carrier licensees for now, although it is anticipated that the merger control regime may be extended in a few years. A Competition Commission ("the Commission") equipped with investigatory powers will shortly be established, while adjudicatory powers will be vested in a specialist Competition Tribunal ("the Tribunal"). The Ordinance is expected to come into effect in one to two years' time, while the Commission and the Tribunal will be constituted well before then to begin the substantial amount of preparatory work necessary to enforce the Ordinance.

This article will examine the key provisions of the Ordinance, the extent to which aspects of its implementation are unclear, and consider the challenges with enforcing the law.

II. CONTEXT UNDER WHICH THE ORDINANCE WAS ADOPTED

The Hong Kong regulatory context in which the Ordinance was adopted is significant for practical as well as academic reasons. It informs us on the manner in which the Ordinance will likely be interpreted, as well as the enforcement priorities of the Commission.

Hong Kong has largely been a laissez-faire economy that emphasizes introducing rules that allow free entry of goods and services; the origin of such free trade principles can be traced back to its origin on the world map as a trading port. Since the 1970s, focus gradually began to shift on transforming the city-state into a financial center, and after the handover to China in 1997, Hong Kong's eyes quickly focused on becoming the gateway to

China. Despite these changing policy objectives, Hong Kong has consistently focused on making it an attractive place to do business by passing laws and policies that allow ease of cross-border trading, as exemplified by the lack of foreign investment restrictions and low corporate and personal taxes. Laws and regulations were introduced to facilitate these objectives, and to ensure the integrity of the financial and banking systems.

It was not until 1995 that the issue of Hong Kong's domestic competition policy first came to bear, when the last Governor of Hong Kong, Chris Patten, asked his business council to consider the issue of a competition policy for Hong Kong. This resulted in the establishment of the Competition Policy Advisory Group ("Compag") in 1997, an independent statutory body whose role is to investigate alleged anti-competitive conduct. Compag has proven to be largely ineffective as it has no legal powers of enforcement.

Separately, in the context of the Government's continuing bid to deregulate the telecommunications market, competition provisions were introduced in the telecommunications and broadcasting sectors in 2000. These sectoral rules were administered by the Telecommunications Authority and the Broadcasting Authority, with the former having accumulated a body of case law and issued guidance on the manner in which these rules are to be enforced.

Momentum continued to gather for a general, economy-wide competition law for Hong Kong. This culminated in two rounds of well-participated public consultations in 2006 and 2008, with the Competition Bill being introduced into the Legislative Council for deliberations in 2010 and its final adoption in June 2012, just a few weeks before the Bill would have lapsed.

The slow and deliberate manner in which Hong Kong's competition policy evolved may suggest a degree of reticence on the part of the public and certain parts of the Government about a competition law that applies to the entire domestic economy. The public debate that took place during the public consultations as well as during the legislative passage of the Bill clearly unveiled anxiety in the business community about a general competition law. Such concerns resulted in a number of special features of the Ordinance, like the introduction of certain turnover-based exemptions for small and medium sized enterprises ("SMEs") who lobbied against the Ordinance. In addition, private enforcement is now limited to follow-on actions (private actions for damages that require a prior regulatory infringement decision) and stand-alone private actions are not permitted. As a further concession, the merger control regime will regulate only transactions involving telecommunications carrier licensees.

It remains to be seen whether the Commission's enforcement approach will reflect the more conservative approaches taken by the government. The recent change of the government (the new Chief Executive, C.Y. Leung, was only sworn in on July 1, 2012), whose election campaign was largely focused on grassroots issues such as the availability of supply of public housing, suggests increased support for a more active enforcement regime than would have been the case under the previous government led by Donald Tsang, himself a tycoon.

III. CONDUCT PROHIBITED BY THE COMPETITION BILL

Despite the quirks of the new law, the Ordinance has adopted the internationally prevalent "three pillar" model of competition law and introduces the following three prohibitions: (a) the First Conduct Rule, which is concerned with anti-competitive conduct involving two or more separate undertakings; (b) the Second Conduct Rule, which is concerned with anti-competitive conduct of a single firm that abuses its "substantial degree of market power"; and (c) the Merger Rule, which seeks to regulate transactions that involve telecommunications carrier licensees.

A. The First Conduct Rule: Prohibition of Multi-party Agreements, Concerted Practices and Decisions

The First Conduct Rule is concerned with multi-party agreements, concerted practices and decisions that have the object or effect of preventing, restricting or distorting competition in Hong Kong. The First Conduct Rule is largely in line with the equivalent prohibition against anti-competitive agreements such as the Article 101 prohibition under the TFEU. There are some key elements to note:

The First Conduct Rule applies to "undertakings," defined as "any entity, regardless of its legal status or the way in which it is financed, engaged in economic activity, and includes a natural person engaged in economic activity." The key phrase "economic activity" is elaborated on in draft papers issued by the government during the legislative process that was compiled to show the Bills committee (the LegCo body responsible for scrutinizing the bill) what may be included in the regulatory guidance that the Commission is required to issue. In these Leg-Co Draft Guidelines, references to "economic activity" is elaborated as "any activity consisting in offering goods or services on a market and which could, at least in principle, be carried on to make profits." This term seems to encompass all businesses and business people.

Such a definition of "undertakings" is very much consistent with international norms. The notion of undertakings is also consistent with the basis on which the Government has introduced exclusions from application of the Ordinance for certain statutory bodies. Statutory bodies are excluded from the application from the Ordinance on the basis that their primary function is not to engage in economic activity. Under the Ordinance, statutory bodies may still be subject to its prohibitions if they are expressly listed in a separate piece of secondary legislation. Of the 581 statutory bodies, there are currently six that will be subject to the Ordinance.

The second key concept, "agreement," is interpreted by the Ordinance as "any agreement, arrangement, understanding, promise or undertaking, whether express or implied, written or oral, and whether or not enforceable or intended to be enforceable by legal proceedings," thus capturing all formal and informal agreements between undertakings.

As to what might amount to an infringement of the First Conduct Rule, the Ordinance makes express reference to four types of agreements that would constitute "serious anti-competitive agreement"—namely, price-fixing, market allocation, fixing or limiting purchase/supply markets, and bid-rigging—but does not specify the other types of agreements that may be captured by the prohibition. "Serious anti-competitive agreement" was in fact introduced quite late during the legislative passage to address concerns by SMEs that serious infringement actions could potentially be taken against them by the Commission. The government's response was to introduce a turnover-based exemption for SMEs whereby the First Conduct Rule would have no application if the combined turnover of the undertakings to an agreement that would have otherwise infringed the rule does not exceed HK$ 200 million. Nevertheless, the Government also specifically provided a carve-out from the exemption by explicitly stating that if any such agreement should constitute a serious anti-competitive agreement then no exemption would be available. This position is consistent with those taken by other jurisdictions where such agreements are regarded as the most egregious forms of anti-competitive arrangement, and in some places, have been likened to a "cancer on society" and treated as a per se infringement of the law.

Aside from those four types of agreements referred to as serious anti-competitive agreements, the Ordinance does not provide any indication as to the other types of arrangements that may give rise to an infringement. Helpfully, the LegCo Draft Guidelines provide an indicative, non-exhaustive list of horizontal agreements to which the First Conduct Rule could potentially apply. Aside from the more egregious types of anti-competitive agreements (e.g., collusive tendering), these Guidelines also make references to more commonplace business arrangements such as joint purchasing or selling, information sharing and the setting of technical or design standards.

It is anticipated that an effects analysis would be required before infringement can be established. Like many other jurisdictions, it is also anticipated that enforcement efforts would initially focus on those more serious anti-competitive agreements as these are typically considered to be the most harmful to competition. That has certainly been the track record in the relatively short history of the sector-specific competition law regime under the Telecommunications Ordinance, in which the Telecommunications Authority carried out investigations into hardcore price-fixing arrangements, and no cases have ever been brought against these other business cooperations that may have an anti-competitive effect.

As for vertical agreements, the view taken by the government throughout the debate and also in the LegCo Draft Guidelines is that these agreements are, in general, less likely to give rise to competition issues. However, the LegCo Draft Guidelines do note that vertical agreements that seek to limit access to the market for competing suppliers or that seek to limit competition between competitors could give rise to competition concerns. The Commission is required by the Ordinance to carry out a public consultation to issue guidelines on how it proposes to enforce the First Conduct Rule, and it is expected that the Commission will clarify how it proposes to treat vertical agreements, and whether it would be prepared to issue a block exemption in relation to such agreements. It will therefore be important for businesses to keep monitoring developments in this aspect of enforcement.

The Ordinance provides for exclusions from the prohibition for private undertakings, which can be obtained pursuant to a prior Commission decision or by way of self-assessment. There are several available exclusion grounds, including economic efficiency, on the basis that the agreement was made to comply with legal requirements and to carry out operations of general economic interest. The bar has been set quite high before an undertaking can apply for a prior Commission decision, as the Ordinance requires that the application involve a novel issue that has broader application than just the undertakings concerned. Therefore one would expect that in the majority of cases, companies would need to assess their own situation to see if they can make use of the relevant exemption. Given the lack of detail around what these grounds of exclusion cover, it would be important for companies to monitor available guidance from the Commission, relevant pronouncements made by the Telecommunications Authority (on the issue of efficiency only), and guidance in other jurisdictions such as the European Union.

Significantly, the Commission has the power to issue block exemptions, which are exemptions for specified categories of agreements. Examples of EU block exemptions are motor vehicles and research & development. Businesses should bear in mind that the issuance of a block exemption will open for public consultation, so it will be key to keep a close watch on developments and to participate in the process as much as possible in order to put forward views and have them be taken into account.

Separately, exemptions may also be awarded by the Chief Executive on public policy grounds, and in order to avoid conflicting with international obligations. However, such exemptions will most likely be invoked only rarely.

B. The Second Conduct Rule: Prohibition of Unilateral Abuse of Substantial Market Power

The Second Conduct Rule deals with abusive actions by an undertaking with significant market power, and it provides that "[a]n undertaking that has a substantial degree of market power in a market must not abuse that power by engaging in conduct that has as its object or effect the prevention, restriction or distortion of competition in Hong Kong."

As is the case elsewhere, a breach of the Second Conduct Rule would only be found where: (i) an undertaking has a substantial degree of market power and (ii) that undertaking has abused its market power with an anti-competitive object or effect.

The notion of what constitutes a "substantial degree of power in a market" is partially defined in the Ordinance. It involves considering the following factors: market share, power to make pricing and other decisions, barriers to entry in the relevant market, and any other factors that may be included in future guidelines to be issued by the Commission.

What is interesting about the Ordinance is that Hong Kong has deliberately opted to adopt a lower threshold than dominance, which is commonly adopted in most other competition law statutes. In fact, in papers issued by the government in April 2012, it was expressly proposed that a market share of as low as 25 percent could give rise to the application of the Second Conduct Rule. While market share is not the only factor that the Commission would use to determine whether an undertaking enjoys a position of a substantial degree of market power, such a low threshold could nevertheless capture a larger number of undertakings than is the case elsewhere. For example, Europe sets an indicative presumption of dominance at a 40 percent market share, and China's rebuttable legal presumption of dominance is a 50 percent market share). This issue is particularly acute for the Hong Kong domestic economy, as it is not large and has fewer players in each sector. It is therefore possible that, unlike other jurisdictions where there are traditionally fewer abuse of dominance cases than there are cases taken under the prohibition against anti-competitive agreements, we could potentially see the reverse situation in Hong Kong.

The second limb of establishing an infringement requires an abuse of a substantial degree of market power. The Ordinance refers, "in particular," to conduct that is exclusionary in nature, and those that limit production, markets or technical development to the prejudice of consumers. Examples given in the relevant LegCo Draft Guidelines of such categories of abusive conduct is also in line with the international norms, which specify that predatory behavior could include predatory pricing (i.e., pricing below cost), tying/bundling, margin squeeze, and refusal to supply.

The currently available guidance in the form of case law by the Telecommunications Authority under the sector-specific competition laws and its published guidance are also consistent with the Second Conduct Rule, and is the way that it is envisaged that it would be enforced. Again, there have been decisions taken under the equivalent rule by the Telecommunications Authority, and this may well mean that when the Commission starts to enforce the Ordinance, it will not shy away from it as some other antitrust authorities have done, at least initially.

Exclusions and exemptions under the Second Conduct Rule are broadly similar to those under the First Conduct Rule, although they differ in that there is no exclusion on the grounds of economic efficiency, nor will the Commission grant block exemptions. As with the First Conduct Rule, there is a de minimis exemption for SMEs and it is set at the lower level of global annual turnover of which it does not exceed HK $40 million.

C. The Merger Rule

The issue of whether the Hong Kong competition law should have a generally applicable merger rule was hotly debated during the public consultation. It was felt that such a rule would bring about high transaction costs, and that Hong Kong was not ready for it. As a compromise measure, it was decided that a merger rule would only be introduced for transactions that involve telecommunications carrier licensees, which is similar (although slightly broader) in scope to the current merger control rules under the Telecommunications Ordinance.

The Merger Rule has limited application and prohibits transactions involving telecommunications carrier licensees that have the effect of substantially lessening competition in a telecommunications market. The intent is to review the operation of the Merger Rule with a view to extending it to transactions in other sectors across the entire economy in a few years' time.

IV. ENFORCEMENT AND ADJUDICATION

A. The Competition Commission

The Ordinance originally called for the Commission having both powers of investigation and adjudication. However, in response to feedback from both the consultation and during the legislative passage, it was ultimately decided that the Commission would only have powers of investigation, with all enforcement actions to be taken in the Tribunal, the adjudicatory body.

The Commission's key role is to investigate conduct that may contravene the Ordinance and to enforce the Ordinance. The Commission's powers are broad, and in accordance with Section 131 of the Ordinance, it may do "all such things as appear to it to be expedient ... in connection with the performance of its functions."

The Commission will be headed by a political appointee, the Chairperson, whose appointment is to be approved by the Chief Executive. The day-to-day operation of the Commission is to be overseen by the Chief Executive Officer.

The Chairperson, as leader of the Commission, will be responsible for the policy direction of the Commission and will decide the approach the Commission takes towards enforcement. It is still unclear as to whether the Commission will adopt a light-touch approach to enforcement or whether it will take a tougher line, as has been the case more recently in the financial services sector in Hong Kong. The appointment of the Chairperson of the Commission is a major decision and will be a good indication as to the approach we can expect to see from the Commission in enforcing the law.

Beyond the political issues, the Commission's effectiveness will also depend on the composition of the staff, both in terms of the number of staff and their experience.

B. The Competition Tribunal

The Tribunal will consist of judges of the Court of First Instance. The Tribunal will hear and determine applications made by the Commission, reviewable determinations, and private actions, among other matters.

The key challenge we envisage for the Tribunal will be the current lack of a competition law regime and the challenges this may pose to the judges sitting on the Tribunal, who may lack direct experience in ruling on competition law matters.

Aside from public enforcement, it is also possible to institute private follow-on damages actions. Initial proposals that permit stand-alone damages actions were eventually rejected, particularly because of SMEs' concerns that larger and well-funded corporations could simply institute actions against them opportunistically.

C. Penalties

Key penalties include fines of up to 10 percent of local Hong Kong turnover of the undertakings concerned for a maximum period of three years, and directors' disqualification orders for up to five years. The Tribunal may also award damages against both undertakings and individuals. Other sanctions the Tribunal may impose include orders for payment of costs and damages, disposal of operations, assets or shares, and declarations that an agreement is void or voidable.

V. CONCLUSION

The introduction of the competition law spells out a watershed moment for Hong Kong, which has traditionally boasted a laissez-faire economy with minimal regulation. Given the lack of experience with competition laws for most businesses in Hong Kong, compliance may be challenging. While the Ordinance largely follows international norms, it does have a number of features that are specific to Hong Kong. Such features include the turnover-based exemptions for SMEs, the adoption of a lower threshold of "substantial degree of market power" rather than dominance, and the express decision not to regulate mergers (save for transactions that involve telecommunications carrier licensees) for the time being.

The next few months will be key, as they will see the establishment of the Commission and the Tribunal. Once these bodies are in place, the Commission will make it a priority to begin public consultation on the preparation of the various guidelines. It will be important for businesses to participate in these processes as much as possible in order to have their views heard. It is crucial for the government to choose the Chairman of the Commission very carefully, as he or she would have significant influence on enforcement position and trends. Based on the experience of other new Asian competition regimes, Hong Kong can expect a period of transition for the Commission to gear up its internal resources and to start to engage with the public on the permissible boundaries under the Ordinance before serious infringement actions are taken. In the meantime, businesses would be well advised to review their business practices with a view to ensure compliance with the Ordinance.

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SOEs and competition policy in China

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Since China's Anti-Monopoly Laws ("AML") bill passed in 2008, competition policy in China is thoroughly analyzed by antitrust practitioners around the world. The rulings by the Chinese antitrust enforcement agencies are often compared with rulings by competition authorities in developed economies. These comparisons may not properly take into account the major distinction of the Chinese economy. Namely, China's economy is still in the transition from a planned economy to a market economy. As such, state owned enterprises ("SOEs") play a much bigger role in China than in developed economies.

Given the important role played by the SOEs, Article Seven of AML provides that:

> *"With respect to the industries controlled by the State-owned economy and concerning the lifeline of national economy and national security or the industries implementing exclusive operation and sales according to law, the state protects the lawful business operations conducted by the business operators therein. The state also lawfully regulates and controls their business operations and the prices of their commodities and services so as to safeguard the interests of consumers and promote technical progresses." In addition, Article Seven of AML stipulates that "The business operators as mentioned above shall lawfully operate, be honest and faithful, be strictly self-disciplined, accept social supervision, shall not damage the interests of consumers by virtue of their dominant or exclusive positions."*

Article Seven of China's AML has received considerable amount of criticism as it does not clearly stipulate which are those industries concerning the lifeline of the national economy and national security. While SOEs dominate in these industries, SOEs are also active in many arguably nonstrategic industries, such as real estate development.

This paper examines the SOEs and their effect on China's competition policy and projects future relations between SOEs and antitrust policy in China.

I. BACKGROUND

Among the major economies in the world, the Chinese economy is the only one that is still in transition from a centrally-planned economy to a market economy. A unique feature of this transitional economy is the overwhelming presence of SOEs. Different levels of government supervise SOEs. The largest SOEs, such as the three big oil companies (Sinopec, China National Petroleum, and China National Offshore Oil), are under the supervision of the State-owned Assets Supervision and Administration Commission (SASAC), whereas the large state owned financial companies, such as the four major national banks (Industrial and Commercial Bank of China, China Construction Bank, Agricultural Bank of China, and Bank of China), are regulated by the China Banking Regulatory Commission.

SOEs are dominant in many strategic industries such as banking, insurance, telecom, transportation infrastructure, oil and gas, and utilities. Table 1 presents statistics of Fortune Global 500 companies in China in 2012. Among the 73 Chinese firms listed on the Fortune Global 500, only five firms are privately owned companies and the highest rank by a private company is 242. On the other hand, 68 SOEs are included in the Fortune Global 500 ranking, among which, 43 SOEs are administered by the SASAC.[1]

Table 1: Statistics of Fortune Global 500 Companies in China in 2012

	Number	Highest rank
SOEs	68	5
Under supervision by SASAC	43	5
Private	5	242
Total	73	

Sources: Fortune magazine's 2012 Global 500. http://money.cnn.com/magazines/fortune/global500/

Table 2 presents the statistics of Top 500 Enterprises in China in 2012. SOEs account for 310 and private companies account for 190 in the ranking. SOEs not only dominate in terms of quantity, but also in size. The top 30 companies are all SOEs. In addition, SOEs are very active in merger and acquisition (M&A) activities. 110 SOEs in the ranking conducted 918 M&A activities, while 44 private companies conducted 193 M&A activities. SOEs accounted for 86 percent of the 1111 reported M&A activities among the top 500 Enterprises in China.

Table 2: Statistics of 2012 Enterprise Top 500 in China

	Number	Top Rank	Merger and Acquisition
SOEs	310	1	918
Private	190	32	193
Total	500		1111

Source: 2012 Enterprise Top 500 in China. http://www.cec-ceda.org.cn/more_new.php?sid=6

Despite its dominant position in the market, and its active role in M&A, very few SOEs are being challenged by the three main AML enforcement agencies, namely Ministry of Commerce ("MOFCOM"), the National Development and Reform Commission ("NDRC"), and the State Administration for Industry and Commerce ("SAIC") since the inceptions of AML in China. For example, MOFCOM has issued a number of rulings regarding M&A, but only one restriction involved an SOE (e.g. GE/ Shenhua case).[2]

1 See SASAC press release at http://www.sasac.gov.cn/n1180/n14200459/n14669156/index.html (in Chinese).

2 See MOFCOM press release at http://fldj.mofcom.gov.cn/ztxx/ztxx.html (in Chinese).

A number of reasons explain this inactivity by the AML enforcement agencies against SOEs. First, Article Seven of the AML provides SOEs with certain legal protections. For example, if a SOE operates in an industry concerning the lifeline of national economy and national security, it cannot be investigated by AML agencies. At this moment, there is no clear definition of strategically important industries in the AML statute.

Second, SOEs have a very deep connection with various levels of government agencies. These deep political connections make it harder for AML enforcement agencies to prosecute anticompetitive practices by SOEs.

Third, the executives of large SOEs are at the vice minister level in the Chinese bureaucratic system, which ranks SOEs above the AML enforcement agencies, such as MOFCOM's antimonopoly bureau. Chinese political culture makes it therefore very difficult for a lower ranked agency to prosecute a higher ranked agency.

II. NEW DEVELOPMENTS

Several recent developments indicate a changing attitude towards SOEs by the AML enforcement agencies. The first widely reported antimonopoly case against an SOE in November 2011, the investigations against China Telecom and China Unicom over suspected price-discriminations in the broadband market, resulted in an announcement by the two companies that they would increase broadband speeds and reduce service charges, in order to settle the investigations by NRDC.[3] These recent developments are encouraging, because it seems that SOEs are under scrutiny by AML enforcement agencies. These changes are mainly driven by the following crucial transformations.

First, the Chinese government recognizes that SOEs need to improve efficiencies in order to improve the overall efficiency in the economy. As China is moving away from a low income country to a medium income country, future growth in the economy will need to come from efficiency gains, rather than from further increases in capital and labor inputs. Thus, improving efficiencies at the SOEs level is critical to sustaining future growth. The main objective of the AML is to increase efficiencies in the economy by promoting competition. Therefore, the government has incentives to use AML to increase competition in the market and to improve the efficiency of SOEs.

Second, public opinion plays an important and increasing role in government decision-making. For example, the investigation by NDRC is prompted by public dissatisfaction with SOEs monopoly in the telecom market, which results in poor service quality and higher prices.

Third, competition between SOEs may lead to increasing roles by AML enforcement agencies in the future. Although, SOEs are all state owned, the management of SOEs enjoy considerable and exercisable power. In addition, SOEs are under supervision by different levels of the government. Hence, competition between SOEs can be very intense sometimes. AML enforcement agencies will therefore face growing demand in the future from competing SOEs to maintain a level of competitiveness.

3 See press release at China Telecom website: http://www.chinatelecom.com.cn/news/02/t20111202_80346.html

Fourth, competition from private and foreign owned firms in China will influence how AML agencies handle SOEs. Private and foreign owned companies are the fastest growing sectors in China. Both private and foreign owned companies have recognized the power of AML in order to protect their own interest.

Fifth, as SOEs become multinational companies, SOEs face examination by competition authorities from other jurisdiction. As part of SOEs growth strategies, more and more SOEs adopt a "go abroad" policy by investing in developed economies around the world. The expansion of SOEs in developed economies will bring SOEs under supervision by foreign competition authorities. For example, the European Union Competition Commission carefully reviewed the proposed acquisition of Elkem AS by China National Bluestar Group Co., Ltd,[4] and the joint venture agreement between Sinochem Group (Sinochem, China) and Koninklijke DSM N.V. (DSM, Netherlands)[5] in 2011. The lessons learnt by SOEs from acquisitions in developed economies will affect their behavior in the domestic market as well.

III. CONCLUSION

China's competition law is a key piece of legislation, which aims to build a market-based competitive economy. At its early stage, China's AML enforcement agencies have been trying to standardize competition policy. At this moment, SOEs have not been aggressively challenged by AML enforcement agencies. However, as market participants gain a growing awareness of AML, SOEs will face increasing pressure from the public and AML enforcement agencies.

Given the speed at which AML enforcement agencies are expanding their capacity and the greater use of AML by market participants, it is likely that antimonopoly cases against SOEs will accumulate.

4 *Case COMP/M.6082 China National Bluestar/Elkem*

5 *Case COMP/M.6113 DSM/Sinochem/JV*

The New Trend of Network Distribution and A Reconsideration of Copyright Protection

Jason Si[1]

Abstract: In recent years, the market for digital content on the Internet has developed at a tremendous pace: Music, videos, and articles have all increased their online presence at fast rates. While advances in Internet distribution technology have brought about great benefits, they have at the same time also created a great number of copyright disputes. This article aims to analyze and explain new technologies and business models and the relevant legal challenges through changes in the methods of distribution and consumption of copyrighted content.

In recent years, along with the widespread adoption of broadband and increase in the ability of the Internet to handle large amounts of data, the market for digital content on the Internet has grown and continues to grow at a remarkable pace. According to the CNNIC's 27th Report on Internet Development, among its ten most-common uses, music, videos, and articles received places 2, 7, and 10 respectively with 79.2%, 62.1%, and 42.6% of respondents' votes. With such data it is obvious that the Internet has already become a vital means of consuming copyrighted content.

Though Internet distribution technology has yielded many benefits, at the same time it has also caused numerous headaches for content rights holders. According to statistics, the number of copyright cases in Beijing and Shanghai these past three years has grown dramatically. Internet copyright cases already hold the largest proportion of IP cases.[2] This article will explore several changes to methods of consuming and distributing copyrighted material in order to explain and analyze the legal challenges brought by these new technologies and business models.

I. MUSIC

From a historical standpoint, the music industry's main modes of distributing and consuming content can be divided into three types: performance rights in giving live performances, the right to reproduce and publish (this is the mode for release of recorded media with which we are familiar), and live streaming on the internet.

1 Zhongnan University of Economics and Law, IP Institute Doctoral Candidate, Director of Tencent Legal Department

2 Chen, Jinchuan: "Increasing number of Internet copyright cases."【EB/OL】【June 3, 2010】, http://ip.people.com.cn/GB/141383/177175/10620601.html

According to statistics, the current retail rate of digital music has increased by 15-20%, whereas the rate of CD sales has decreased by the same proportion. In fact, by the end of 2010 the retail volumes of digital music and CDs were equivalent.[3] It is not difficult to imagine that if this current trend continues, CDs will completely disappear from our lives in the near future.

2. VIDEOS

The distribution of videos and motion pictures can also be divided into three types: theatrical releases, DVDs, and Internet streaming. However, the methods of distributing and profiting from motion pictures are different than those of music. Due to natural advantages in video effects, widespread availability, and social aspects, theatrical releases are the main profitable distribution method for motion pictures. On the other hand, and in common with music, distribution of films and television programs over the Internet is replacing the more traditional DVD distribution channel due to a combination of cost advantage and convenience in storage, update and on-demand streaming.

3. WRITTEN WORKS

The two typical distribution channels of written works are paper media and the Internet. Due to the widespread of e-readers, the development of e-paper technology and the efforts to expand 3G networks, e-reader adoption and technological development are both advancing at an amazing pace. However, this has also put tremendous pressure on traditional distribution of newspapers and other print media; according to authoritative prediction, 90% of traditional print media will be distributed digitally by 2015. [4]

4. SOFTWARE

Traditionally, the software industry's main distribution method was to sell physical discs containing the software, such as CDs. Microsoft is unquestionably the most successful representative of this mode of distribution. The second method is through internet distribution. Under this mode, software is available for download over the Internet and is usually free; the software providers collect profits from selling license keys for either installation or use of the software. Most of the popular antivirus software that we use is operated on this model. The third distribution method is called SAAS (Software as a Service) and it is a creature born of cloud computing. SAAS derives value also from Internet distribution: Software providers don't rely on reproduction or release of software to earn profits but rather upon the providing of the software.

As seen from the remarkable change in the means of distribution and use of the preceding four works, content distribution and consumption models are in the midst of upheaval. Under the influence of modern distribution technology, there is a shift underway from traditional models of selling copies of a copyrighted product to selling the access to the copyrighted product itself. But our copyright laws are unquestionably more suited to

3 "Apple iTunes already accounts for 1/4 of music sales in the US." 【N/OL】World Computers, 2009【2010.06.03】, http://it.icxo.com/htmlnews/2009/08/19/1373083.htm

4 Industry Insight: Digitial Books to Surpass Traditional Press Media, http://news.sohu.com/20041209/n223409501.shtml

the traditional model of selling a physical copy of a work, leading to serious problems in adapting to new technology. This author believes that future revisions to China's Copyright Law should seek to consider and respond to the following issues:

First, broaden the scope of Internet distribution rights: Merge broadcasting rights into information network distribution rights; act in accordance with Article 8 of the Wipo Copyright Treaty and establish the idea of a unified set of rights for supplying a copyrighted work to be distributed over the Internet to consumers. This is to avoid the awkward issue that Article 17 of the Copyright Law has already listed 17 kinds of copyrights but "other rights enjoyed by the copyright holder" still apply to remedy unauthorized network timed rebroadcasts.

Second, on the premise of improving the collective copyright management and the fee collection system for statutory license, print media content that has been reposted on the Internet should be allowed within the scope of statutory license. Unauthorized use of articles or images currently occupies a very large proportion of online copyright cases, but they also have small amount of objective and relatively unambiguous circumstances. With such a large volume of easily-resolved cases still going to trial, there is obviously a tremendous waste of legal resources. By allowing reposting on Internet within statutory license, the number of copyright disputes will decrease dramatically. However, one must also simultaneously accompany this with a reformation of collective copyright management and fee collection systems for statutory license, or else risk severely threatening the natural balance of interests.

Third, incorporate the "Computer Software Protection Regulations" into the national "Copyright Law." This will both codify the specialized nature of software and clarify the granting of protection to object code stored in memory and the converted form thereof; as seen from the discussion of SAAS model above, the copyright protection of the online and service software is severely lacking. Infringing parties can use technological measures to make alteration on software to the same effect to but not by changing source code and object codes at all. If the illegality of these sorts of actions is not confirmed, it will become very difficult for software service providers to continue offering this model in the future.

Fourth, a logical three-step test should be put in place both to make the fair use system more accommodating and to strengthen legal protection to neutral information transmission technology. In legal practice, webpage snapshots, offline downloading, and other new technology are distinctively neutral; their development and application have had a major impact on increasing the efficiency of data transmission. They do not have any necessary conflict with the legal consumption of content. But under current enumerating legislation, it is quite difficult for relevant technologies to be deemed as fair use. The three-step test would use a catchall standard to regulate fair use, thus increasing the ability of the Chinese Copyright Law to accommodate this new technology. This will also have benefits for the wider development of the Internet industry.

Throughout the history of copyright law development, each new development in distribution technology has been accompanied with a lowering of barriers to copying, thus correspondingly decreasing the ability of copyright holders' control over their content. But at the same time, copyright holders have also gained more effective means of distribution as well as new means of deriving value from their content.

The "zero-cost" advantage and the unparalleled convenience and efficiency of Internet release as compared with traditional release methods necessarily make it a means of releasing copyrighted content replacing all others. Therefore, copyright holders should follow the path of history and while simultaneously combating piracy also establish their own authorized pathways for distribution of content over the Internet, to satisfy the demands of vast numbers of consumers for digital content. Otherwise, with so many consumer demands unsatisfied, the fight against Internet piracy will be rather difficult. At the same time, with the changing business models where Internet distribution rights are at the core, the copyright law should also evolve and innovate accordingly to better accommodate and promote the developments of advanced distribution technology.

The Sun Also Sets: Trending Away from Japanese Exceptionalism in Merger Control and Closer to Global Standards

Etsuko Kameoka[1*]

Mel Marquis[2**]

Having endured two lost decades, Japan has little appetite for a third. But as an export-driven country, there are limits to Japan's ability to will itself back to economic health, given limp global demand and bleak forecasts. The implicit medium-term strategy—just staying afloat—seems evident in the Cabinet's decision of June 18, 2010 to pursue a "New Growth Strategy".[3]

One interesting offshoot of the Strategy is a package of merger control reforms, effective July 1, 2011.[4] These took the form of an amendment to the Japan Fair Trade Commission's ("JFTC") notification rules and a revised set of guidelines.[5] The developments highlighted here are: the abolition of the prior consultation system; enhanced procedural transparency; confirmation of greater openness to wider geographic markets, and; early signs of how the reforms seem to be influencing the JFTC's merger practice.

I. THE END OF PRIOR CONSULTATION

Prior to the 2011 merger control reforms, parties to a merger notifiable in Japan had the option of consulting with the JFTC before filing. Such informal consultations presented advantages, such as confidentiality pending discussions with case handlers. This system has now been abolished. From the JFTC's perspective, the

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2 ** European University Institute and University of Verona. The authors are grateful to Tadashi Shiraishi for kindly commenting on a previous draft.

3 For details, see http://www.meti.go.jp/english/policy/economy/growth/index.html;
Randall Jones & Byungseo Yoo, Japan's New Growth Strategy to Create Demand and Jobs, (OECD Economics Department Working Papers, No. 890), available at http://dx.doi.org/10.1787/5kg58z5z007b-en.

4 See JFTC Press Release (14.06.2011), available at http://www.jftc.go.jp/en/pressreleases/uploads/110620.pdf.

5 For translations of the Rules on Applications for Approval, Reporting and Notification ("Notification Rules"), the Guidelines on the application of the Policies Concerning Procedures of Review of Business Combination ("Procedural Guidelines"), and the revised Guidelines on the Application of Antimonopoly Act Concerning Review of Business Combination ("Revised Guidelines"), see http://www.jftc.go.jp/en/policy_enforcement/mergers/pdf/110713.2.pdf; http://www.jftc.go.jp/en/policy_enforcement/mergers/pdf/rules_on_applications.pdf; and http://www.jftc.go.jp/en/pressreleases/uploads/110620attach2.pdf.

main benefit of prior notification was the possibility to obtain information quickly and to head off problems at an early stage, thereby reducing the need to resort later to more drastic measures. This may also have seemed attractive to the parties if it led to quicker approval.[6] In practice, according to the business community, prior consultation sometimes bogged down the procedure and allowed for a *de facto* circumvention of statutory timelines.[7]

It is probably for that reason that the prior consultation system appears to have been used only infrequently in recent years. In 2008, 1008 notifications were filed with the JFTC, yet prior consultation was used in just 28 of those cases.[8] In 2009, prior consultation was used only 24 times as compared to 985 notifications. In 2010, when only 265 notifications were filed, prior consultation was used 13 times. The figures just recited (which do not take account of aborted deals that were never filed) imply that, at least with regard to garden-variety notifications, the impact of the reform may be limited. On the other hand, inasmuch as merging parties generally did avail themselves of prior consultation in large and complex cases, the statistics to some extent belie the qualitative importance of having an additional informal procedural tool.[9]

In the absence of prior consultation, the JFTC will have fewer opportunities to engage in informal, possibly opaque manoeuvring. Moreover, by bringing the procedure more squarely under the more formal framework, the JFTC may be more often obliged to introduce detailed economic analysis when presenting its concerns to the parties. Under the previous system, in cases where competitive concerns were discussed off the record, it was less imperative for the JFTC to build up sophisticated economic evidence to convince the parties and the public.

II. REINFORCED RECOGNITION OF WORLDWIDE MARKETS

The "old" Merger Guidelines of 2007 already envisaged relevant geographic markets wider than the domestic market. Furthermore, the JFTC in fact accepted international markets, as it did, for example, in *Sony/NEC* (2005), a merger of optical disc drive businesses. In the European Union, by comparison, the parties argued for a worldwide market (given low transportation costs, no trade barriers, important trade flows, global product standards and globally active suppliers and customers), but the European Commission left the question open because it did not affect its competitive assessment.

6 From the 1970s to the 1990s, the JFTC resolved competition problems informally and merging parties were quite content to have matters handled confidentially. See, e.g., Toshiaki Takigawa, The Prospect of Antitrust Law and Policy in the Twenty-First Century: In Reference to the Japanese Antimonopoly Law and Japan Fair Trade Commission, 1 Wash. U. Glob. Leg. Stud. Law Rev. 275, 288 (2002). However, following changes made in 2002, general satisfaction with prior consultation seems to have declined.

7 In theory, time should have been running according to "phase 1" and "phase 2" of the prior consultation phase (note: these periods bore no correspondence to the familiar Phase I and Phase II in other jurisdictions). However, the JFTC was criticized for holding up the process, in particular by insisting that submitted documents were incomplete and imposing vast data requirements. See, e.g., Kaori Nakano, The Recent Developments in Merger Inverstigation, 320 Rippo to Chosa [Legislation and Investigation] 79, 81 (2011).

8 JFTC, www.jftc.go.jp/kenkyukai/dk-kondan/110404/188-1.pdf (in Japanese).

9 For the impact of the end of prior consultation, see, e.g., Masahiro Murakami, Review of the merger procedure of 2011, 1357 Hanrei Times 36, 44 (2011).

Nevertheless, perhaps to quell lingering doubts, the revised Merger Guidelines add clarity with regard to when the JFTC will recognize a worldwide or regional (i.e., East Asian) market. According to Section 2.3 (2), such instances include those where domestic or overseas suppliers are selling products in the worldwide (or East Asian) market for almost same price, and buyers are purchasing mainly from worldwide (or East Asian) sellers.

III. MORE PROCEDURAL TRANSPARENCY

The reforms were also designed to achieve more transparent procedures, a seemingly perpetual concern in Japan. Under the new framework, when the JFTC requests a report from the parties, it should indicate the purpose of its request, thus giving the parties a better understanding of what precisely is needed.[10] At the parties' request, the JFTC should also explain its concerns.[11] This was already a matter of informal practice but it is now made explicit. Furthermore, an approval decision (which previously was not announced in written form) should be provided in writing to the parties.[12] Yet another helpful feature, found in the revised Guidelines,[13] is a description of cases falling outside the jurisdiction of the JFTC.

On substantive analysis, the revised Guidelines also provide more detailed explanations of the elements that determine whether a merger will substantially restrain competition. These include, among other things, the supply posture of other producers, competitive pressure from neighboring markets, and competitive pressure exerted by customers.[14]

IV. THE JFTC'S EARLY PRACTICE FOLLOWING THE REFORMS

The impact of the reforms will be felt mostly in mega-mergers and otherwise complex transactions. The news of the moment concerns not a cross-border deal but the NSC/Sumitomo Steel merger, approved conditionally on December 14, 2011 under Japan's revised framework.[15] This is a headline merger of the number one and number three Japanese producers and, if consummated, it will spawn, next to ArcelorMittal, the world's largest steel producer. Notably, the JFTC's new emphasis on speedier procedures played a significant role. Whereas mergers of comparable size might have previously taken up to a year to gain clearance,[16] here approval was granted in just over six months. One hopes that brisk procedures will not be reserved exclusively for cases involving Japanese 'clients' with an industrial policy subtext, although this hope remains to be tested.

10 See supra Note 3, Notification Rules, Article 8; Procedural Guidelines, Section 6(1).

11 Id., Procedural Guidelines, Section 4.

12 Id., Notification Rules, Article 9; Procedural Guidelines, Sections 3, 5 and 6.

13 Id., Revised Guidelines, Section 1.1 (1).

14 Id., Section 4.2.

15 See http://www.jftc.go.jp/en/pressreleases/uploads/2011-Dec-14.pdf. As of this writing, review of the transaction is still pending in certain jurisdictions.

16 See Naoyuki Fukuda citing an unnamed JFTC official, in FTC gives green light to Nippon Steel, Sumitomo Metal merger, ASAHI SHIMBUN, Dec. 15 2011, available at http://ajw.asahi.com/article/economy/business/AJ201112150041.

V. CONCLUSION

Merger control is one area of competition policy, like cartel busting, in which states of convergence matter greatly because its effects redound, in the aggregate, upon both domestic and foreign consumers. Ideas and practices converge, of course, not toward a fictitious **end state** but toward common, indefinite trajectories. The years 2010-2011 have been marked by significant refinements of merger policy in several jurisdictions, partly motivated by the convergence bug, often transmitted through the work of the International Competition Network.[17] The reforms discussed above seem to confirm that Japan, too, is participating in a nascent *ius commune quasi-universalis* — one that must be flexible enough to accommodate, where appropriate, informed divergence and other creative tensions.

17 Many of these developments are discussed in EUROPEAN COMPETITION LAW ANNUAL 2010: MERGER CONTROL IN EUROPEAN AND GLOBAL PERSPECTIVE (Hart Publishing, Philip Lowe & Mel Marquis, eds., forthcoming 2012).

Using Competition Policy to Promote "Shared Growth" in Korea

Seonghoon Jeon[1*]

"Shared Growth," a principle that both large and small companies should grow together, is among the top priorities on the political agenda of all Korean parties. There are many policy instruments to promote shared or mutual growth of large companies and small-medium enterprises ("SMEs"), but the Korea Fair Trade Commission ("KFTC") has played a pivotal role.

In this column, I would like to address the issue of using competition policies to promote shared growth in Korea, with an emphasis on innovation. Even though the recent drive of shared growth by KFTC covers issues larger than innovation, a main focus is to encourage cooperation in research and development ("R&D") between large companies and small-medium enterprises.

I. THE RECENT EMPHASIS ON SHARED GROWTH IN KOREA

Korea's competition law, the Monopoly Regulation and Fair Trade Act, explicitly mandates the balanced development of the national economy and the enhancement of consumer welfare as its two main purposes. Moreover, KFTC enforces a special statute, the Fair Subcontract Transactions Act, to protect SME sellers from large company buyers' abuses. However, shared growth has gained more emphasis recently in Korea, mainly due to the deepened gap between large companies and SMEs in terms of profitability, employment, and R&D.[2]

The Korean government declared that it would drive shared growth policies in September 2010, and KFTC cited improving relationships between large and small companies for shared growth as its top enforcement priority. In addition, the Shared Growth Commission was launched in December of that year. The Commission is a private institution that is formally independent from, but actually supported by, the government.

1 * Dean, School of Economics at Sogang University in Seoul; Commissioner, Korea Fair Trade Commission. This work was supported by the National Research Foundation of Korea Grant funded by the Korean Government (NRF-2010-330-B00091). The preliminary version was presented at the ICC (International Chamber of Commerce) Round Table on Competition and Innovation, The Hague, May 21, 2011.

2 For example, according to the Korea Institute of Industrial Economics and Trade, the mobile division of Samsung Electronics earned operating profits of almost 9 percent of sales, while its 20 parts-suppliers earned less than 2 percent in 2009.

II. REINFORCEMENT OF FAIR SUBCONTRACT TRANSACTIONS ACT

The Fair Subcontract Transactions Act has been the main tool used by KFTC to promote shared growth, by which large-company contractors are required to make proper contracts with, and make proper payments to, SME subcontractors, and are prohibited from exploiting SME subcontractors in various ways. Recently the Act has been reinforced significantly.[3]

The main revisions are (1) expanding the applicable subcontract transactions; (2) making it easier for SMEs to ask for price adjustments reflecting the increase of material costs, and making it more difficult for large companies to reduce prices unreasonably; (3) taking more strict enforcement measures against large companies that steal technology, including treble damages recovery where it is stolen from small subcontractors,[4] and; (4) KFTC may suggest and encourage contractors and subcontractors to make mutual agreements of support and cooperation, which will be the legal basis of the recent drive of shared growth, especially in evaluation of the index of shared growth.

III. THE INDEX OF SHARED GROWTH

The Shared Growth Commission, which is a private institution in appearance but a government-supported one in substance, selected 56 large companies in various industries (including Samsung Electronics and Hyundai Motors) as objects to be evaluated for an index of shared growth.[5]

The index of shared growth will combine two kinds of evaluations: quantitative and qualitative. The quantitative evaluation will examine large companies' efforts for shared growth in terms of the contents and implementations of mutual agreements with subcontractors for shared growth. This evaluation will be conducted by KFTC as its inherited project. The qualitative evaluation, undertaken by the Shared Growth Commission as a newly launched project, reviews SME satisfaction with large companies' efforts for shared growth in terms of fair trade and cooperative subsistence.

The results of index evaluation in terms of grade or ranking will be announced in early 2012. The government will provide those large companies receiving the best evaluations with incentives, such as prizes, tax benefits, R&D projects, procurements, and exemptions.[6]

3 The revision was declared on March 29, 2011; implementation began on June 20, 2011.

4 This particular revision is remarkable in that punitive damages to such an extent are exceptional in Korean civil law.

5 Samsung and Hyundai's sales accounted for 56 percent of GDP in 2009.

6 Details on the government incentives are yet to be fixed.

IV. KEY INGREDIENTS OF MUTUAL AGREEMENTS FOR FAIR TRADE AND SHARED GROWTH

Many large enterprises have recently reached mutual agreements with subcontracting SMEs for fair trade and shared growth, which were usually mediated by KFTC. Two prominent examples of such arrangements are Samsung and Hyundai's agreements with their respective subcontractors.

Nine Samsung group affiliates, including Samsung Electronics, made cooperative agreements for shared growth with 5,200 subcontractors in April 2011. The package of financial assistance amounted to $5.7 billion, among which R&D support comprised $1.7 billion. Samsung agreed to induce its subcontractors to make cooperative agreements with lower-level sub-subcontractors, and provide them with incentives. Moreover, Samsung promised to allow free licenses of its patents, and commit to protecting subcontractors' technologies.

Similarly, six Hyundai group affiliates, including Hyundai Motors, made cooperative agreements for shared growth with roughly 1,600 subcontractors in March 2011. The package of financial assistance amounted to $3.9 billion, with R&D and capacity investments making up $2.3 billion. Hyundai promised to provide 300 R&D support man-powers for its subcontractors.

V. CONCLUSION

I will conclude by remarking on both positive and negative sides of KFTC's recent drive of shared growth. No one objects to the necessity of "shared" growth for sustainable growth as well as stability. At the moment, even large companies regard the drive of mutual agreements for fair trade and shared growth as inevitable, and cooperate with KFTC.

However, there are concerns that too much emphasis on shared growth might distract KFTC from its main tasks of promoting competition such as regulating cartels, mergers and abuses of dominance. Moreover, the drive for shared growth may be transient. It may fade out if economic circumstances improve, or if the next government changes its policy priorities.

Singapore Steps up Competition Enforcement

Chester Toh[1*]

On February 20, 2012, the Competition Commission of Singapore ("CCS") issued a public consultation paper proposing changes to its Guidelines on Merger Procedures. This consultation signals CCS' intention to step up its merger enforcement in a number of ways.

The first is to refine the existing merger notification procedures to make it easier for merging parties to assess whether to notify their transaction under Singapore's voluntary merger notification regime. This is achieved by moving away from the indicative market share thresholds, which require parties to undertake market definition at the notification assessment stage. Under the proposals, merging parties are strongly encouraged to notify their transaction to the CCS if the parties supply goods or services of the same description and their share of supply of such goods or services exceeds 40 percent of the total supply in Singapore. However, one would not be able to apply this bright-line test to vertical or conglomerate mergers for obvious reasons. It is therefore still necessary to conduct a preliminary merger assessment based on the substantial lessening of competition ("SLC") test to determine whether to notify the transaction in Singapore.

Another important aspect of the proposals is introduce a process for merging parties to obtain confidential advice from CCS on whether their proposed transaction is likely to raise concerns. Yet such advice would not be granted as of right. The CCS has full discretion whether to provide the confidential advice, after taking into account amongst others its resources at that particular point in time. Parties seeking such confidential advice should also be aware that the advice would be qualified by the fact that the CCS would not have taken into account views of third parties in providing the advice. There are a number of other criteria to satisfy before parties can take advantage of this process, including demonstrating to the CCS that the merger situation presents genuine issues relating to competition assessment in Singapore. As this confidential advisory mechanism is generally intended to apply to transactions that are not in the public domain save for exceptional circumstances, confidential guidance is unlikely to be commonly sought.

The proposed revisions to the Guidelines also seek to formalize the pre-notification discussions ("PNDs") process. In practice, some have already been approaching the CCS for such discussions before submitting their notifications. PNDs, particularly when used in conjunction with a draft Form M1, allow a notifying party to better manage the clearance process and timelines. For example, the CCS may seek clarification on certain information in the draft Form M1 or identify gaps in the information submitted. The notifying party can also have the op-

1 * Rajah & Tann, Singapore.

portunity to point out information that is not relevant to the particular transaction under consideration. From CCS' perspective, PNDs allow the agency to plan its resource allocation to facilitate a more expeditious merger review process.

The CCS has also spelled out its approach towards market intelligence and surveillance in the revised Guidelines. Aside from monitoring the media for transactions that may potentially raise competition concerns, as a number of its international counterparts do, CCS may also publish a notice on its website indicating that it is in the process of considering whether a non-notified transaction could possibly raise concerns under Singapore merger provisions. Such a move may encourage third parties, particularly those that have not been approached by the CCS for views on the transaction, to provide their feedback on the transaction to the CCS.

Despite being a relatively young agency, CCS has made notable progress in its enforcement efforts since its establishment in 2005. In recent years, there has been a noticeable uptrend in the number of investigations and infringement decisions. Most recently, on March 9, 2012, the CCS issued its proposed infringement decision against two ferry operators plying the Singapore-Batam route. If the CCS proceeds with a final decision against these two operators, this would be its sixth cartel decision and the third in a space of six months. The CCS has stated on a number of occasions that cartels remain its enforcement priority and it is expected to continue focusing on trade associations and certain services sectors with a history of coordinated activities.

Aside from the usual investigatory activities, the CCS has also undertaken eight market studies in the past two years, a stark increase from none in 2009. These market studies covered a broad range of sectors including retail mall rental, healthcare services, retail petrol, pay TV, airport ground handling, concrete and cement, as well as real estate services.

CCS has also recently signalled its intention to conduct a market study into the industrial property sector. Such a market study is a timely one given that prices of multi-user industrial space for 2011 have increased by 27.1 percent, with rentals increasing by 16.2 percent. Industrial property was by far the top-performing real estate sector in Singapore last year. The emergence of industrial property real estate investment trusts ("REITs") coupled with strong demand from retail investors shifting to industrial space in response to residential property cooling measures are possible contributing factors. The move demonstrates CCS' continued emphasis on markets with broader impact on the local economy as the competitiveness of small and medium-sized enterprises ("SMEs") are significantly affected by rising rentals in the industrial property market.

Some commentators have observed that Singapore has not taken an infringement decision against an international cartel so far. There is no doubt that we will see such infringement decisions in due course, some of which may be brought to CCS' attention through its leniency program. However, one should recognize that international cartels have far greater impact on bigger economies. Without similar levels of resources as its larger counterparts in more mature jurisdictions, CCS should be applauded for directing its enforcement efforts towards conduct and behavior that presents significant competitive harm to the local economy. In time to come, CCS will no doubt join the global fight against international cartels, and recent trends suggest that CCS is clearly well placed to do so.

Marching Through the Next Twenty Years: Recent Developments of the Taiwan Fair Trade Law

Andy C. M. Chen[1*]

The year 2012 marks the 20th anniversary of the enactment of the Taiwan Fair Trade Law ("FTL"). Since its inception, the law has undergone five major changes, including the most recent amendments of 2011. Recent developments of the FTL reflect both the experiences of the Taiwan Fair Trade Commission ("TFTC") and its intention to improve the effectiveness of law enforcement.

I. REVISIONS OF SUBSTANTIVE RULES

The most remarkable change effected by the 2011 amendments is the incorporation of the leniency program into the FTL. The program follows the EU model, granting full immunity from administrative fines to the first cartel whistleblower. Cartel leaders or initiators are also qualified for the program.[2] Fines for subsequent informants are proportionally reduced according to the timing of their application. To encourage application, the statutory maximum fine for cartel violations is increased further, to 10 percent of the violators' total sales income from the previous fiscal year.

The other major revision is to hold endorsers in testimonial advertisements to be jointly and severally liable with the advertisers. The revision is evidently a response to the increasingly popular trend of involving celebrities in commercials in Taiwan.

II. INSTITUTIONAL RESTRUCTURES

Under the newly enacted Organizational Law of the Fair Trade Commission, the commissioner is nominated by the Premier and approved by the Congress rather than by the President. By repositioning the TFTC outside the executive branch, the law expects to enhance the independence of the agency.

1 * Associate Professor, Department of Financial and Economic Law, Chung Yuan Christian University; former commissioner of Taiwan Fair Trade Commission (Feb. 2007 to Jan. 2010).

2 The leader and initiator are not excluded because, in practice, verifying the role an applicant plays in a cartel is generally difficult.

Furthermore, the number of commissioners is reduced from nine to seven, with each holding a four-year staggered term. Unlike the current non-staggered three-year term limit, the new law aims to facilitate experience-sharing among commissioners of different sessions.

In recognition of the growing influences of economic theories on competition law, a new Office of Information and Economic Analysis will also be established in early 2012. Comprised principally of staffs with economics and statistics backgrounds, the Office will function both as a "provider" of expert opinions and "check-and-balancer" on economic issues in individual cases.

III. CASE DECISIONS

A. CARTELS

Lifelaw, an online company, and 130 participating lawyers began providing legal services to website and mobile-phone users at prices much lower than those charged for in-person consultations. Upon members' complaints, the Taiwan Bar Association ("TBA") sent letters to participating lawyers, reporting their violations of the Code of Ethics and suggesting their immediate withdrawal from the partnership. In 2010, the TFTC fined the TBA for collusion. The TBA challenged the TFTC's decision for failing to recognize the TBA as a non-commercial organization and its goal of pursuing public interest. The case was later vacated and remanded in administrative appeal proceedings and is currently pending in the TFTC.

Milk became a highly relevant topic toward the end of 2011. The three major milk suppliers, totaling a market share of more than 80 percent,[3] were revealed to be fixing the retail prices of milk. Although the suppliers argued that the price changes were merely suggestive and independently established, the TFTC inferred the existence of a collusive agreement from several "plus factors." Market characteristics, such as homogeneous products, and oligopolistic market structures with high entry barriers and low demand elasticity led the TFTC to conclude that individual price increases on separate dates in September 2011 were simply a means to test competitors' reactions. The real purpose was to reach a consensus to raise prices in October. Despite their very different cost structures, the suppliers failed to justify their nearly universal degree of price increases as independently established.

In the first week of October 2011, the four largest convenience stores in Taiwan raised the prices of freshly brewed coffee containing milk ingredients by exactly five New Taiwan Dollars per cup, irrespective of their sizes. Although analytically identical to the milk cartel case, the definition of a relevant product market in this case was controversial. The TFTC maintained that "coffee brewed and sold at the convenience stores" was an independent market, due in large part to the convenience of one-stop shopping they provided to customers. Regardless of the fact that convenience stores were offering quantity discounts afterwards, such promotions were considered as being implemented to maintain brand loyalty and market power.

3 Wei Chuan Foods Corporation (37.03 percent), Uni-President Enterprises Corporation (29.56 percent), and Kuang Chuan Dairy Co., Ltd. (17.55 percent).

B. MERGERS

Mergers are rarely banned under the FTL. The case on instant noodles in 2010 was a noticeable exception. It involved the acquisition by the leading supplier of instant noodles in Taiwan of the stocks of the second-largest suppliers. Applying in-depth economic analysis, the TFTC directly measured the cross elasticity between instant noodles and several potential substitutes such as snacks or frozen foods. The results revealed low substitutability among those products. Instant noodles, therefore, were treated as a separate relevant market. With the post-merger Herfindahl-Hirschman Index increased by more than 2000, it made the unilateral effect more of a concern in this case. The TFTC was particularly alarmed by the degree of sale diversion from the largest to the second-largest suppliers if the former were to raise its price after the acquisition.

By contrast, the Supreme Administrative Court recently vacated and remanded a merger case banned by the TFTC in 2010. The merging parties were also the leading and second-largest suppliers in the rolled steel markets of Taiwan, with a post-merger market share of more than 50 percent.[4] However, the court was skeptical of the merging firm's ability to raise the prices after the merger. Because steel was a standardized product subject to the World Trade Organization's zero-tariff policy, competition from abroad constrained the merging firm's ability to abuse its market power.

IV. CHALLENGES AHEAD

While the TFTC is becoming more experienced, challenges for the agency loom large. The TFTC must delineate more clearly the boundary between competition and industrial policies in the future. The force of globalization will also further involve the FTL and TFTC in the process of harmonizing international competition law. In marching through the next twenty years, the TFTC should prepare itself for fashioning an enforcement policy capable of balancing these two demanding tasks.

4 Yieh United Steel Corporation (37.52 percent) and Tang Eng Iron Works Co., Ltd (21.21 percentn).