CPI's Asia Column Presents:

Yutai: A Landmark Case on Resale Price Maintenance in China — The Divergence in Public and Private Enforcement is Now Institutionalized

By Jet Deng, Ken Dai and Rangi He[1]

Special thanks will go to the intern Elsa Zhong for her contribution to this article and she is currently studying law the University of Sydney Law School, Australia.

CPI COMPETITION POLICY INTERNATIONAL

February 2018

1. Introduction

On December 21, 2017, a long-anticipated judgment of the second instance of *Yutai v. Hainan Provincial Price Bureau* was handed down by Hainan High People's Court.[2] It was previously anticipated that this judgment could terminate the five-year long divergence in the approach towards resale price maintenance ("RPM") adopted by NDRC (National Development and Reform Commission[3]) and the courts.

As the antitrust agency responsible for the public enforcement against RPM in China, NDRC adopts the "prohibition + exemption" approach[4] against RPM. By far, NDRC has prohibited around 18 RPM cases and imposed significant fines on the companies committing RPM (the record fine on a single company is USD $55.12 million（CNY 350.06 million）, which was imposed on Mercedes-Benz in 2015[5]). On the other hand, there is no public record of successful exemption case to date.

By contrast, the plaintiffs who brought RPM cases against their suppliers before the courts could hardly win, actually the plaintiffs never won a single case up to the date. This is mainly because the courts adopted the rule of reason approach towards RPM, which requires the plaintiffs to prove the RPM's effect of eliminating or restricting competition. So far, the private enforcement against RPM is very limited due to such burden of proof imposed on the plaintiff side.

Different approaches adopted by NDRC and the courts have led to a dual-mode regulatory scheme clouded with administrative and legal uncertainties. Hence, such difference, divergence and tension need to be addressed.

For the first time, the administrative litigation (judicial review) case of *Yutai* provided the courts with a precious opportunity to terminate the dual-mode regulatory scheme and to decide on the one and only approach towards RPM. However, after the first and the second instance, the *Yutai* case failed to play the role of the Terminator but instead effectively institutionalized the divergence.

2. The Divergence between the Public and Private Enforcement against RPM

Article 14 of the *Anti-Monopoly Law of the People's Republic of China* ("AML") prohibits vertical monopoly agreements, which include RPM among trading partners that fix the price of goods sold or limit the minimum price at which goods can be sold to third parties.[6] This prohibition seemed clear and non-controversial at the time when it was submitted to the National People's Congress for review

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[1] Jet Deng, partner at Dentons Beijing office; Ken Dai, partner at Dentons Shanghai office; Rangi He, senior associate at Dentons Beijing office.

[2] See the judgment (second instance before Hainan High People's Court) of *Yutai* at http://wenshu.court.gov.cn/content/content?DocID=23889d51-88d8-4e87-aaa4-a85c01845f73&KeyWord=%E9%94%90%E9%82%A6.

[3] In this article, NDRC refers to both itself and its branches at the provincial level (such as Hainan Provincial Price Bureau).

[4] Similar to the *per se* rule, the "prohibition + exemption" approach does not require assessment and proof of anti-competitive effect; unlike the *per se* rule, this approach provides opportunity of exemption (namely, Article 15 of the AML). However, since it is quite difficult to meet the conditions of Article 15 in practice, RPM is effectively *per se* illegal under the "prohibition + exemption" approach.

[5] See NDRC's penalty decision on Mercedes-Benz at http://mp.weixin.qq.com/s/HGyY0pSGXkh346IdgvVX4w.

[6] Article 14 of the AML (adopted August 30, 2007, at the 29th Meeting of the Standing Committee of the 10th National People's Congress, effective August 1, 2008).

and adopted on August 30, 2007.[7] However, under the combined influence of both the US[8] and the EU's regulation of the RPM and a lack of prescribed and detailed modes of analyzing RPM in the AML itself, the approach towards RPM adopted by NDRC and the courts diverged in the course of public and private enforcement of the AML.

2.1 Public Enforcement

In the first few years after the AML came into force, NDRC mainly focused on the legislation of supporting rules, and its enforcement was not very active.[9] The turning point came in 2013 when NDRC started the antitrust wave against RPM. Since then, RPM have become the main target of NDRC's enforcement activities, accounting for over 40% of the economic monopoly cases probed by NDRC between 2013 and 2017.

To date, NDRC has investigated around 18 RPM cases, and it expressly established the "prohibition + exemption" approach after its first two RPM cases.

On February 22, 2013, NDRC issued two announcements for its first RPM sanction against two liquor makers – *Moutai* and *Wuliangye*.[10] Since the court had previously adopted the rule of reason in the first widely-known private enforcement case[11] against RPM in the *Rainbow v. Johnson & Johnson* (first instance) on May 18, 2012, antitrust practitioners were eager to find out whether NDRC would adopt the same approach. However, NDRC's two announcements were short (without full text of the decisions) and quite different:

- the announcement for *Moutai* simply said that Moutai committed RPM and violated Article 14 of the AML;

- while in the announcement for *Wuliangye*, after a similar short description of the violation of Article 14, it contained a brief analysis of the anti-competitive effects of the RPM from the perspective of elimination of intra-brand competition, restriction of inter-brand competition, and harm caused to the consumers' interests.

Only with these two announcements, it was still unclear whether NDRC adopted the *per se* rule or the rule of reason.

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[7] Literature on the legislative process of the AML shows that the draft AML "expressly prohibits" RPM. See http://www.npc.gov.cn/npc/zt/2006-06/24/content_1382613.htm and http://www.npc.gov.cn/npc/oldarchives/newcwh/zgrdw/common/zw.jsp@hyid=0210029&label=wxzlk&id=370732&pdmc=flzt.htm.

[8] Particularly, the US Supreme Court dropped the long-standing *per se* rule and adopted the rule of reason for RPM in its decision on the *Leegin* case on June 28, 2007.

[9] Jet Deng and Ken Dai, China's Antitrust Regime Is Ushering In A New Era – Amendment To The Anti-Monopoly Law And Drafting Of Six Antitrust Guidelines.

[10] See news on the liquor case at http://www.chinanews.com/cj/2013/02-22/4588648.shtml and http://www.chinanews.com/cj/2013/02-22/4588651.shtml. Also, see Moutai's announcement at http://static.sse.com.cn/disclosure/listedinfo/announcement/c/2013-02-22/600519_20130223_1.pdf and Wuliangye's announcement at http://disclosure.szse.cn/finalpage/2013-02-23/62145581.PDF.

[11] Actually, before *Rainbow v. Johnson & Johnson*, there had been another civil litigation on RPM in 2011 (*Weizhong v. Xilanger*), where Nanjing Intermediate People's Court also required the plaintiff to prove the anti-competitive effect of RPM. However, the judgment of this case was not publicized and aroused little attention. See the case summary of *Weizhong v. Xilanger* at http://www.docin.com/p-1002464382.html.

Later on August 7, 2013, NDRC announced its second RPM sanction against nine infant formula companies.[12] The announcement was also a brief one without a full text of the decision, but it slightly described the anti-competitive effects of the RPM on the intra-brand competition, inter-brand competition and consumers' interests. Hence, some observers commented that NDRC also adopted the rule of reason, which had been reinforced by the *Rainbow v. Johnson & Johnson* (second instance) on August 1, 2013.

NDRC itself did not clarify its approach to the public until an article was published in the name of Mr. Xu Kunlin, the former Director General of NDRC, on October 31, 2013.[13] Mr. Xu explained that NDRC adopts a "prohibition + exemption" approach, which reflects the framework of the AML, according to Article 14 which prohibits RPM and Article 15 which provides conditions of exemption, and it is not necessary to put a label of *per se* rule or rule of reason on the approach against RPM in China. Additionally and more importantly, Mr. Xu also clarified that in the enforcement against RPM, NDRC should have an attitude of attaching importance to the economic analysis of RPM, analyzing its harm caused to the competition and consumers' interests and studying the nature and gravity of the violation, which will be the main factors for imposing the final penalty.

Based on the "prohibition + exemption" approach, NDRC do not need to assess and prove the anti-competitive effect of RPM, and it may straightly decide that the companies violated the AML based on the pure presence of the RPM arrangement, as it did in a series of automobiles cases and other cases. The table below lists NDRC's achievements against RPM:

	Time of Decision	Relevant Product	Fine (and percentage accounting for the companies' relevant revenue)
1	Feb 2013	Liquor	1) Moutai: USD $38.89 million (1%) (CNY 247 million) 2) Wuliangye: USD $31.82 million (1%) (CNY 202 million)
2	August 2013	Infant formula	1) BIOSTIME: USD $25.65 million (6%) （CNY 162.9 million） 2) MeadJohnson: USD $32.1 million (4%) (CNY 203.76 million) 3) Dumex: USD $27.09 million (3%) (CNY 171.99 million) 4) Abbott: USD $12.18 million (3%) (CNY 77.34 million) 5) Friesland: USD $7.6 million (3%) (CNY 48.27 million) 6) Fonterra: USD $703,712 (3%) (CNY 4.47 million) 7) Wyeth: no fine due to leniency policy

[12] See NDRC's announcement at http://xwzx.ndrc.gov.cn/xwfb/201308/t20130807_552992.html. Also, see BIOSTIME's announcement at http://www.hkexnews.hk/listedco/listconews/SEHK/2013/0807/LTN20130807016_C.pdf and BEINGMATE's announcement at http://disclosure.szse.cn/finalpage/2013-08-07/62913167.PDF.

[13] See http://www.ceh.com.cn/xwpd/2013/10/255896.shtml.

			8) BEINGMATE: no fine due to leniency policy 9) meiji: no fine due to leniency policy
3	December 2013	Pasteurized milk	1) TianLu: investigation suspended due to commitment mechanism
4	May 2014	Lens	1) Essilor: USD $1.38 million (2%) (CNY 8.7902 million) 2) Nikon: USD $265,238 (2%) (CNY 1.6848 million) 3) Carl Zeiss: USD $278,286 (1%) (CNY 1.766 million) 4) Bausch + Lomb: USD $580,916 (1%) (CNY 3.69 million) 5) Johnson & Johnson: USD $573,882 (1%) (CNY 3.6437 million) 6) HOYA: no fine due to leniency policy 7) WEICON: no fine due to leniency policy
5	August 2014	Auto	1) Chrysler: USD $5 million (6%) (CNY 31.682 million)
6	September 2014	Auto	1) FAW-Volkswagon: USD $39.17 million (6%) (CNY 248.58 million)
7	May 2015	Auto	1) Mercedes-Benz: USD $55.14 million (7%) (CNY 350.06 million)
8	September 2015	Auto	1) Dongfeng-Nissan: USD $19.42 million (3%) (CNY 123.3 million)
9	April 2016	Auto tire	1) Hankook: USD $342,768 (1%) (CNY 2.1752 million)
10	August 2016	Home appliance	1) Haier: USD $1.95 million (3%) （CNY 12.348 million）
11	December 2016	Medical device	1) Medtronic: USD $18.67 million (4%) （CNY 118.52 million）
12	December 2016	Auto	1) SAIC General Motors: USD $31.8 million (4%) (CNY 201.756 million)
13	December 2016	Pasteurized milk	1) Bright Dairy: USD $311,633 (1%) (CNY 1.978 million)
14	December 2016	Medical device	1) Smith & Nephew: USD $116 925 (6%) (CNY 742,148)
15	February 2017	Fish feed	1) Yutai: USD $31,506 (RPM not implemented) (CNY 200,000)

			2) Other six companies: totaling USD $141,831 (CNY 900,000)
16	March 2017	Broadband	1) China Unicom: no specific figure (1%)
17	December 2017	Headset	1) GN Netcom: USD $363,402 (3%) (CNY 2.306 million)
18	December 2017	Turbo oil	1) Eastman: USD $373,535 (5%) (CNY 2.37 million)

However, with the attitude of attaching importance to the economic analysis of RPM, NDRC gradually added more detailed analysis of the harm caused by RPM in recent decisions. For example, in NDRC's decision on *Medtronic*, NDRC substantially assessed the RPM's harm caused to the intra-brand competition, inter-brand competition, and the consumers' interests.[14] Nevertheless, such attitude will not change NDRC's "prohibition + exemption" approach.

With regard to the "exemption" of RPM, no record of such exemption exists so far.[15] The companies may in principle rebut the presumption of illegality of RPM in accordance with policy considerations listed in Article 15 of the AML. Aspects of these policies include improving technological advancement, enhancing operational efficiency and assist the growth of small-and medium-sized enterprises (SMEs).[16] In order to facilitate companies to understand and apply for the exemption, NDRC has drafted antitrust guidelines on the conditions and procedures of the application for exemption.[17] The drafted guidelines are now in the process of being reviewed by the Anti-Monopoly Commission under the State Council and will likely be enacted in 2018.

2.2 Private Enforcement

In contrary to the public enforcement, Chinese courts have been applying an analytical rule of reason approach towards RPM. In this approach, existence of monopoly clauses in agreements does not directly establish illegality. Instead, priorities of the analysis are given to the economic effects caused by the alleged illegal conduct. *Rainbow v. Johnson & Johnson*[18], the first widely-known example of private antitrust litigation involving RPM, laid the foundation of this approach by a thoroughly-reasoned judgment in 2013. The framework of the analysis was subsequently followed in *Gree* Case in 2016[19], where the RPM arrangement was held to be legal.

The plaintiffs in both *Rainbow v. Johnson & Johnson* and *Gree* are downstream distributors, and the defendants are upstream suppliers. Based on the judgments in these civil litigations, two main elements distinguish the courts' rule of reason from NDRC's "prohibition + exemption" approach:

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[14] See NDRC's decision at http://jjs.ndrc.gov.cn/fjgld/201612/t20161209_829716.html. Also, see NDRC official's article on this case at http://mp.weixin.qq.com/s/oIMLRzoO2O9_ICoeCNuGCA.

[15] Junqi Hao, Introspecting and Weighing: Analytical Mode for RPM under the AML.

[16] Article 15 of the AML.

[17] See the draft antitrust guidelines at http://jjs.ndrc.gov.cn/fjgld/201605/t20160512_801559.html.

[18] See the judgment (second instance before Shanghai High People's Court) of *Rainbow v. Johnson & Johnson* at http://wenshu.court.gov.cn/content/content?DocID=effe7905-b647-11e3-84e9-5cf3fc0c2c18&KeyWord=%E9%94%90%E9%82%A6.

[19] See the judgment (first instance before Guangzhou Intellectual Property Court) of *Gree* at http://wenshu.court.gov.cn/content/content?DocID=f9d94f5a-c0b9-4720-8789-a7f50cf3eb9a&KeyWord=%E4%B8%9C%E8%8E%9E%E5%B8%82%E6%A8%AA%E6%B2%A5%E5%9B%BD%E6%98%8C%E7%94%B5%E5%99%A8.

(1) RPM itself does not violate Article 14 of the AML, unless it has the effect of eliminating or restricting competition; and

(2) The plaintiffs shall bear the burden to prove that the defendants' RPM practice has the effect of eliminating or restricting competition.

For element (1), the courts took the view that since Article 13(2) of the AML defines monopoly agreements as agreements, decisions or other concerted practices which eliminate or restrict competition, RPM should only be illegal when it has the effect of eliminating or restricting competition.

For element (2), the courts held that plaintiffs bear the burden of proof in vertical agreements. The burden of proof under the *Civil Procedural Law* ("CPL")[20] will be reversed only by express terms under laws, regulations or judicial interpretations. Since the Supreme People's Court's *Provisions on Several Issues concerning the Application of Law in the Trials of Civil Dispute Cases Arising from Monopolistic Conducts* ("SPC Provisions", adopted on January 30, 2012 and effective on June 1, 2012) has no specific reference to vertical agreements,[21] the general principle that "the burden of proof is upon the party who claims" under the CPL shall apply.

When assessing whether Johnson & Johnson's RPM had eliminated or restricted competition in the medical suture market, Shanghai High People's Court did not refer to the factors listed in the Article 15 of the AML. Instead, it considered the following factors: the competitiveness of the market, the market position of the related companies, the intention for having the RPM program and the effect of the RPM on competition in the market. It is worth noting that the effect of the RPM on competition is based on pricing theories instead of on empirical evidence of actual harm related to sales volume. The position in *Rainbow v. Johnson & Johnson* could have been strengthened if empirical evidence could be taken into account. This selection of evidence arguably clips the potential value of rule of reason approach in gaining practical experience in utilizing RPM for consumer welfare to its full potential.[22]

In view of the above, there is divergence in the approaches adopted by the courts and NDRC stems from their different understanding of the relationship between Article 13(2) and Article 14 and their different inclination in weighing the value of pro-competitive and anti-competitive effects of RPM.

3. The *Yutai* Case

On February 28, 2017, NDRC fined seven fish feed producers (including Yutai) for RPM. Yutai was found that in 2014 and 2015, it signed agreements with its distributors where it required them to sell its fish feed at its guide price; if this requirement was not fulfilled, it was entitled to reduce its profit shares to the distributors. After investigation, NDRC concluded that these arrangements constituted RPM conduct and thus violated Article 14 of the AML. On the other hand, NDRC also found that the RPM was not actually implemented by the distributors. Then according to Article 46 of the AML, NDRC imposed a penalty of USD $31,518 (CNY 200,000) on Yutai. For this decision, Yutai brought an administrative action against NDRC in court.

The court of first instance rejected the approach adopted by NDRC and held that an additional

[20] Article 64 of the CPL.

[21] Article 7 of the SPC Provisions.

[22] *Leegin*, 551 U.S. at 898.

analysis of the effect of the alleged RPM arrangements should have been added (i.e., the same approach adopted by the courts in *Rainbow v. Johnson & Johnson*). It was decided that Yutai did not in effect restrict or eliminate competition in the market. This decision, however, was overruled on appeal.[23]

In the second instance, Hainan High People's Court did not follow the approach adopted in the civil litigation cases of *Rainbow v. Johnson & Johnson* and *Gree*, where the courts held that RPM itself does not violate Article 14 of the AML unless it has the effect of eliminating or restricting competition. Using wording cautiously, Hainan High People's Court took the view that there is no basis to make "eliminating or restricting competition" a constitutional requirement for antitrust agencies in determining vertical monopoly agreements. The reasons provided by the court to support its position may be summarized as follows:

(1) Article 1 of the AML specifies the legislative purposes of the AML, which include not only restraining but also preventing monopolistic conducts. Hence, the antitrust agencies should also take actions to prevent monopolistic conducts.

(2) Literally, Article 14 explicitly prohibits RPM as monopoly agreements. Also, it empowers the antitrust agencies to determine other monopoly agreements, indicating that the antitrust agencies enjoy certain discretion in the antitrust regime.

(3) Article 46 prescribes different types of fine for monopoly agreements that are implemented and not implemented. Hence, the antitrust agencies have the power to sanction monopoly agreements that are not implemented.

Hainan High People's Court further held that after the antitrust agencies have determined the vertical monopoly agreements in accordance with Article 14 of the AML, such determination will be inapplicable only when the offenders, who bear the burden of proof, provide evidence to prove that they meet the conditions of Article 15 of the AML. In other words, the court confirmed that NDRC is entitled to the "prohibition + exemption" approach.

Moreover, in responding to Yutai's reference to the approach adopted in *Rainbow v. Johnson & Johnson*, Hainan High People's Court made a distinction between the civil litigation and the administrative litigation. The court opined that in the framework of civil litigations alleging RPM, the plaintiffs must prove actual damage caused by the alleged illegal conduct, which requires that the plaintiffs first prove the conduct having effect of eliminating or restricting competition. However, in the *Yutai* case, these prerequisites are not necessary, considering that the RPM committed by Yutai was not implemented. Hence, it is not necessary for NDRC to prove the RPM has the effect of eliminating or restricting competition.

4. Conclusion

As a landmark case, *Yutai* had a chance but failed to end the five-year long divergence in the approaches adopted by the courts and NDRC against RPM. The seeming convergence realized in this

[23] See the judgment (second instance before Hainan High People's Court) of *Yutai* at http://wenshu.court.gov.cn/content/content?DocID=23889d51-88d8-4e87-aaa4-a85c01845f73&KeyWord=%E9%94%90%E9%82%A6.

case is actually conditional in two aspects:

(1) The convergence occurred in an administrative litigation (judicial review) case, and the court respected NDRC's "prohibition + exemption" approach. However, for civil litigations, the court mentioned that the plaintiffs still need to prove the anti-competitive effect for claiming damages.

(2) NDRC did not need to prove the effect of eliminating or restricting competition in this case, as the RPM arrangement was not implemented. However, *Yutai* is not clear on whether this is still the case where RPM is implemented.

With these conditions, *Yutai* effectively institutionalized the divergence between the courts and NDRC, resulting in a "one country, two systems" in the approach towards RPM in China. It would not be surprising if the courts and NDRC continue their different approaches in private and public enforcement in the future. In that case, more *Yutai* like cases may come out again.

Currently, China is in the process of amending the AML,[24] and one of the main tasks is to address the divergence at the legislation level. It is hard to say which approach will prevail in the end, but many scholars take the view that the "prohibition + exemption" approach is more consistent with China's current situation and its market than the rule of reason approach.[25] These are the reasons so far: First, due to the relatively low level of economic freedom compared to that of developed western countries, the market in China by itself is incapable of correcting the error costs created by false negatives in which conduct that is actually anticompetitive failed to be condemned. [26] To avoid such error costs and to strengthen the openness in the market in the present time of economic transformation, it is preferable to mistakenly condemn an antitrust conduct. Second, considering the limited resources available to administration departments, a bright-line prohibition subject to exceptions in public enforcement branch is less costly and more efficient to administer than a standard requiring a case-by-case assessment of the competitive effects. Third, it is observed that RPM investigations of companies are motivated by multiple reasons.

In view of the above and from a practical perspective, *Yutai* has clarified the boundary of antitrust risk for RPM in China. As the practitioners the authors would like to recommend that companies should still be careful to arrange RPM, even if the arrangement may ultimately benefit the consumer and such positive effect may be taken into account in a private litigation. Previously people may contemplate that NDRC's decision might be challenged before the courts, now from *Yutai*, companies can perceive that the standard of compliance should be aligned with NDRC's approach, which would likely be respected by the courts in administrative litigations.

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[24] See a news published by the Ministry of Commerce (in Chinese), http://fldj.mofcom.gov.cn/article/xxfb/201711/20171102673084.shtml

[25] Junqi Hao, Introspecting and Weighing: Analytical Mode for RPM under the AML.

[26] Frank H. Easterbrook, The Limits of Antitrust , 63 Texas L. R. 1 (1984).