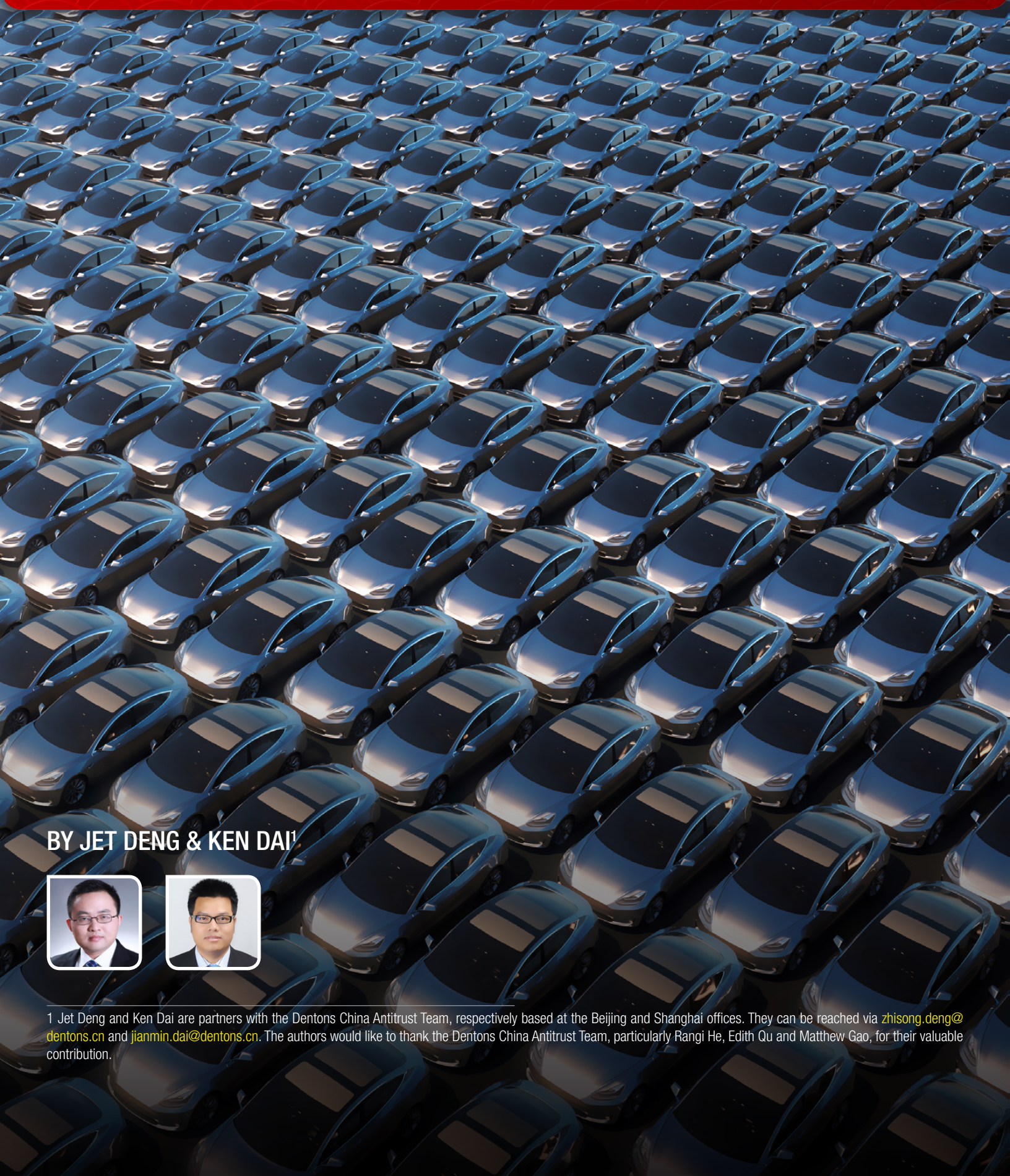


ANTITRUST ENFORCEMENT IN THE CHINESE AUTOMOBILE INDUSTRY: OBSERVATIONS AND FUTURE PERSPECTIVES



BY JET DENG & KEN DAI¹



¹ Jet Deng and Ken Dai are partners with the Dentons China Antitrust Team, respectively based at the Beijing and Shanghai offices. They can be reached via zhisong.deng@dentons.cn and jianmin.dai@dentons.cn. The authors would like to thank the Dentons China Antitrust Team, particularly Rangi He, Edith Qu and Matthew Gao, for their valuable contribution.

CPI ANTITRUST CHRONICLE

MARCH 2020

CPI Talks...

...with DG Zhenguo Wu



CPI Talks...

...with Brent Snyder



Antitrust Regulation in the Digital Economy: Industry Developments and The Amendment of the Anti-Monopoly Law

By Chenying Zhang



Enforcement of the AML in China's Digital Economy – From the Perspective of the Overall Regulatory Environment

By Wei Han & Yajie Gao



Agency Investigation of Abusive Conduct in China: The *Eastman* Case

By Vanessa Yanhua Zhang & John Jiong Gong



High-Profile Merger Filings in 2019: An Analysis of Conditionally Approved Concentrations

By John Yong Ren, Wesley Zhining Wang & Martha Shu Wen



A Brief Analysis of Standards for Resale Price Maintenance Regulations Under the PRC Anti-Monopoly Law

By Kate Heyue Peng, William Ding, Lingbo Wei, Weimin Wu & Chi Pan



Antitrust Enforcement and Litigation in The Semiconductor Industry in China (Patterns and Updates)

By Wei Huang & Bei Yin



Antitrust Enforcement in the Pharmaceuticals and Medical Products Industry in China

By Michael Han & Joshua Seet



A Retrospective of Chinese Antitrust Enforcement in the Chemical Industry

By Josh Yi Xue & Yikai Yang



Antitrust Enforcement in the Chinese Automobile Industry: Observations and Future Perspectives

By Jet Deng & Ken Dai



Antitrust Enforcement and Litigation in China's Internet Industry

By Zhan Hao, Song Ying, Lv Hongjie & Wei Fei



The Science of China's Frand Rate-Setting

By He Jing



Visit www.competitionpolicyinternational.com for access to these articles and more!

CPI Antitrust Chronicle March 2020



I. INTRODUCTION

The automobile sector has always been a focal point of both public and private antitrust enforcement in China since the country's Anti-Monopoly Law ("AML") came into force in 2008. As one of the largest items of expenditure for ordinary families in China, automobiles can have substantial impact on resource allocation between different products and services. Thus, artificially high prices (or low-quality automobiles and after-sales services) can do significant harm to consumer welfare. In 2019, antitrust enforcement in the Chinese automobile industry penalized two RPM practices, among other things. This article will provide an update on these new cases, and recap other recent representative cases in the Chinese automobile industry. The authors aim to assist stakeholders in the Chinese automobile industry to be better prepared to handle antitrust matters, especially because, as of 2020, there will be several significant developments, including further opening-up to foreign investors in the Chinese automobile industry, more opportunities in the electric vehicle business, and more stringent antitrust rules due to upcoming guidelines for the automobile industry and amendments to the AML.

II. PUBLIC ENFORCEMENT: IS THE NEXT WAVE OF ENFORCEMENT COMING?

Nearly six years has passed since China fined four BMW dealers and twelve Japanese auto parts makers for price fixing in August 2014. These were the first two enforcement cases by Chinese antitrust authorities in the automobile industry (one relating to a domestic cartel and the other to a global cartel). The latter case involved a staggering fine of CNY 1.24 billion, which set a record for Chinese antitrust enforcement at that time. The following two years witnessed aggressive enforcement by Chinese antitrust authorities in the industry, penalizing dozens of companies. Since then, it seems that the automobile industry has become less high-profile in terms of public enforcement. Yet, recent practice shows that the authority may have the automobile industry on its radar again, hence sparking the question: is the next wave of enforcement approaching?

III. 2019 HAS SEEN INTENSE ENFORCEMENT IN THE AUTOMOBILE INDUSTRY

In 2019, three major decisions were issued by the Chinese antitrust authorities in the sector. This shows that the automobile industry is still one of the main areas of focus for the Chinese regulator.

A. The Toyota Case (2019)

On December 27, 2019, in what was perhaps the final enforcement action of the year, China's top antitrust authority, the State Administration for Market Regulation ("SAMR"), issued a decision against Toyota Motor (China) for resale price maintenance ("RPM") agreements operated between 2016 and 2018. Specifically, the SAMR's Jiangsu branch found that the undertaking concerned restricted the displayed prices of Lexus cars on online platforms, and limited the sales prices of certain models. These practices prevented intra-brand competition, restricted dealers' rights to set prices independently, and as a result impeded inter-brand competition in the car market, damaging consumer welfare. In light of the anti-competitive effects of the practices, and the undertaking's cooperation during the investigation, the regulator imposed a fine of CNY 87.6 million, 2 percent of the company's 2016 sales in the Jiangsu area.

B. The Changan Ford Case (2019)

In June 2019, the SAMR imposed a penalty on Changan Ford, as the undertaking concerned restricted the minimum resale price of vehicles by downstream dealers in the Chongqing area since 2013 by formulating price lists, signing price discipline agreements, and restraining dealers' minimum sales price in auto exhibits (as well as on the online market). According to the SAMR's decision, the alleged conduct prevented franchises from setting prices independently, eliminated and restricted intra-brand competition, damaged fair competition in the relevant market, and prevented consumer benefits. The SAMR therefore imposed a penalty of CNY 162.8 million, 4 percent of Changan Ford's 2018 sales in the Chongqing area.

C. The Heze Automobile Industry Association Case (2019)

Also in 2019, the SAMR's Shandong branch closed an antitrust case relating to monopolistic conduct carried out by the Heze City Automobile Industry Association. The regulator received a tip-off claiming that the association monopolized the local motor show market, restricted competition and damaged the business environment. After inspections, the local authority found that the association concerned restricted its members' rights

to take part in auto shows, and prevented them from competing against each other, through a commitment letter. In its decision, the authority determined that given that the members of the associations concerned are also competitors in the Heze auto resale market, such a commitment letter constituted a monopolistic agreement containing a boycott provision. As a social organization with wide influence in the local market, the association played a role in arranging and implementing the boycott. Based on the facts and evidence, the local authority fined the association CNY 300,000.

In addition to these three cases, an investigation against three German carmakers for restrictions on new emissions cleaning technology is still ongoing.

D. Recap of the Last Wave of Public Enforcement

Apart from the above cases in 2019, Chinese competition regulators have closed 5 cases relating to RPM in the motor resale market between 2014 and 2016:

Year	Auto Makers	Conduct	Amount of Fine	Percentage of Sales
2014	Chrysler	RPM	CNY 31.7 million	3%
2014	FAW-Volkswagen	RPM	CNY 248.6 million	6%
2015	Mercedes-Benz	RPM	CNY 350.0 million	7%
2015	Dongfeng Nissan	RPM	CNY 123.3 million	3%
2016	SAIC General Motors	RPM	CNY 201.8 million	4%

In addition, RPM practices in the auto parts market were also investigated. In 2016, Hankook was fined CNY 2.2 million (1 percent of its relevant sales) for restricting resale prices of auto tires.

It is noteworthy that there is a significant difference between these 2014-2016 cases and the 2019 cases in terms of the basis for the fine. In the past, Chinese antitrust authorities took the “relevant sales” (namely, impacted sales) of the undertakings concerned as a starting point. However, as from late 2018, it used “all sales,” which can lead to heavier penalty.

IV. PRIVATE LITIGATION: FOCUS ON ABUSIVE CONDUCT AND RPM

Private antitrust litigation in the automobile industry frequently involves abuses of dominant positions and RPM practices. In 2016 and 2017, General Motors and Ford both faced allegations of abuse of market power in the after-sale market. In a major follow-on litigation, Shanghai Hankook was sued in 2018 regarding RPM practices between the tire dealer and its distributors.

A. Major Cases in the Past Few Years

The General Motors case (2016) and the Ford case (2017). In the *General Motors case*, Shenzhen Autel Intelligent Technology Company, an auto after-sale service company, and its affiliate brought a suit against General Motors and its three subsidiaries, claiming that General Motors strictly selected trading parties in the after-sale market for General Motors cars and refused to license essential technical information to the plaintiff on FRAND terms. According to the plaintiff, given General Motors’ dominant position in the relevant after-sale market, and the irreplaceability and essentiality of the information concerned to other business operators in the same market, General Motors’ conduct was an abuse of market dominance. On the ground that the defendant’s conduct damaged competition, obstructed other competitors’ from operating in the relevant market, and caused significant damage to them, the plaintiff claimed compensation of CNY 98 million. Subsequently, the defendant filed a petition to challenge the jurisdiction of the first trial court, the Shenzhen Intermediate People’s Court, and argued that the case should be handled by the Shanghai Intellectual Property Court. However, this petition was rejected on first instance and appeal. According to reports, the suit has been closed through a settlement between the parties.

In 2017, the claimants in the *General Motors* case raised similar arguments against Ford, claiming that the U.S. carmaker's refusal to license essential technical information to the plaintiff constituted an abuse, and claimed compensation. Generally, only carmakers hold the complete set of essential technical information needed for repair and maintenance. Therefore, they may face significant risks of being deemed to hold a dominant position. Refusing to license such information on FRAND terms could render carmakers in violation of the antitrust laws. This case also ended with settlement.

The Hankook Follow-on litigation (2018). After being sanctioned by the Shanghai Price Bureau in 2016, Hankook's RPM practices became the target once again in civil antitrust litigation before the Shanghai Intellectual Property Court in July 2018. The Plaintiff, Wuhan Hanyang Guangming Trading, one of Hankook distributors in mainland China, alleged that Hankook implemented RPM within its distribution network from 2012 to 2016, and abused its dominant market position by charging above-market prices, taking price discrimination measures, and imposing unfair dealing conditions, etc. Hankook responded that evidence submitted by the claimant was weak, since provisions to restrict minimum resale prices had been deleted in later versions of the agreement. It also denied that it had a dominant position in the relevant market. After defining the relevant market as passenger car tire replacement market in mainland China, the court held that Hankook did not have a dominant position given its low market share, and the characteristics of the relevant market for tires. As to the RPM allegation, though the plaintiff presented the Shanghai Price Bureau's decision as a piece of evidence to prove the existence of an RPM agreement and its adverse effect on competition, the court determined it was insufficient, as the plaintiff and defendant only signed an RPM agreement in 2012, yet had not performed. Given the level of competition in the relevant market, the defendant's market position, its motive to implement RPM agreement, and its effects, the court deemed that the agreement did not produce anti-competitive effects, or impede either intra-brand or inter-brand competition. In light of the above analysis, the court dismissed the case. The plaintiff has appealed the judgment to the Shanghai High People's Court.

B. Plaintiffs Face Grave Difficulty in Winning Antitrust Litigation

Despite the vigorous public enforcement, there has been no case in which a plaintiff has won in antitrust litigation against an automobile company. With an eye to the contradictory approaches adopted by courts and the administrative watchdog concerning RPM agreements, it is not surprising that in the *Hankook* case the first instance court rejected the claims, stating that no RPM agreement was implemented, and no restrictive effects were generated. It has been well-known that when tackling RPM conduct in practice, the administrative authority prefers *per se* rules, yet the courts insist on a rule of reason principle. At the end of 2018, China's Supreme Court ("SPC") closed the remarkable *Yutai* case, taking the view that the antitrust authority's approach should be respected by courts in administrative litigation, but that the judicial branch still needs to analyze the competitive effects of RPM agreements in civil antitrust litigation. Though concluded earlier than the *Yutai* case, the *Hankook* judgment is consistent with the SPC's opinion on RPM agreements.

In addition to the inconsistent approach adopted by the courts and antitrust authorities toward RPM, more potential conflicts are expected to follow. It has been reported that China's Anti-Monopoly Committee under the State Council will soon release long-awaited antitrust guidelines, including guidelines for the automobile industry. According to the draft version, certain types of territorial and customer restrictions in the automobile industry (such as restrictions on distributors' passive sales and restriction on distributors' sales of auto parts to consumers) are deemed to have strong anti-competitive effect and might thereby be reviewed under the *per se* illegal approach by the antitrust authorities. However, the courts might continue to adopt the rule of reason toward these non-RPM vertical agreements.

V. MERGER CONTROL: A "BEACH LANDING" IN THE EVE OF A RELAXED INVESTMENT POLICY

Recently, mergers in the auto sector, especially among carmakers, have become common. While China has committed to a wider "opening-up" policy aiming at attracting more foreign investment since 2018, the frequency of merger cases seems to suggest that a "beach landing" battle among car makers has started quietly.

A. China has Adopted a Wider "Opening-up Policy"

Chinese President Xi announced, in a speech at the opening ceremony of the 2018 China International Import Expo ("CIIE"), that China will continue to take measures to open its agriculture, mining, manufacturing and service industries by shortening the so-called "negative list" set out in its foreign investment regulation. The 2018 and 2019 versions of the "negative list" issued by NDRC and MOFCOM both clearly indicate that China

plans to remove its limitation on the number of shares held by foreign carmakers in Sino-foreign equity joint ventures, and the amount of joint venture companies set up by foreign carmakers, by 2022. In addition, with China's new Foreign Investment Law coming into effect on January 1, 2020, China has made moves to further open its market and level the playing field for foreign businesses competing with Chinese companies.

It used to be that foreign carmakers were not allowed to hold more than 50 percent of shares in joint ventures with Chinese automakers. This restriction will be lifted soon. In response, significant mergers emerged to embrace the new, friendly investment environment. In 2018, BMW announced that it plans to increase its shareholding in BMW Brilliance, and subsequently submitted a merger filing with the Chinese antitrust authorities. BMW will enjoy a 75 percent shareholding in the new ownership structure. The transaction is scheduled to be completed in 2022, and has been approved by the SAMR. This makes BMW the first car maker to take majority control of its Chinese JV.

B. Transactions Related to EVs are Booming in China

With China's policy to promote electric vehicles ("EVs"), more foreign automobile brands are coming to operate in China.

In 2018, BMW and Great Wall Motor received clearance from the Chinese antitrust authority to set up a local JV producing EVs. This is the first Sino-foreign joint venture transaction concerning EVs since the Chinese investment reform. In 2019, we have seen a boom in concentrations related to EVs. Of nearly 30 car-related transactions, approximately 11 transactions concern EVs, i.e. batteries or power systems, navigation systems, etc. For example, Daimler and Geely recently announced a new joint venture to build electric Smart cars in China. The transaction received clearance from the SAMR in March 2019.

C. BAIC and Hyundai Fined for Gun-jumping

Although China's auto industry and market may become more open under the new policy, this does not mean that the antitrust authority will loosen its enforcement policies. In 2019, BAIC and two Hyundai companies were fined CNY 300,000 respectively for gun-jumping. The decision relates to a JV transaction between these companies in 2018. The parties signed the JV contract on December 29, 2018, and the new company obtained a business permit on January 29, 2019. According to the decision, the parties' 2018 turnover met the notification threshold yet was not reported to SAMR. Therefore, the parties failed to fulfill the notification obligation.

Though China plans to remove the cap on foreign investment in the motor industry, regulation of mergers and acquisitions will not be loosened. For foreign carmakers preparing to adjust their ownership in their Chinese companies, the merger control notification obligation should be considered as early as possible in the process. It should be particularly noted that the maximum fine for gun jumping will be significantly increased from the current CNY 500,000 to 10 percent of the violators' turnover according to the draft amendment to the AML.

VI. ADMINISTRATIVE MONOPOLY: EMPHASIZING NEUTRALITY IN SUBSIDIES AND PUBLIC PROCUREMENT POLICY

Recent developments concerning administrative monopolies in the auto industry are also worth analyzing and discussing. Two policies relating to new energy cars ("NEVs") merit highlighting. One development is that, in 2019, China adopted new financial subsidy strategies to promote NEVs, namely vehicles powered by fuels other than petrol (gasoline) or diesel, mostly EVs, which focused more on competitive neutrality. Another development is that a new policy emphasizing the establishment of a fair competition environment for foreign and home-made NEVs in public procurement markets has been implemented.

A. A "Competition-friendly" Subsidy Policy for NEVs

In 2009, the Chinese government implemented a subsidy policy to promote domestic NEVs. Under that policy, consumers could enjoy a discount ranging from CNY 3,000 to 60,000 per car when purchasing a NEV, as the government would grant NEV makers a corresponding subsidy. Such a policy had encouraged more sales of NEVs, and resulted in great development in the relevant industry. Nevertheless, the subsidies also raised serious competition concerns, as (i) only cars using batteries produced by specific undertakings could qualify for the subsidy; and (ii) the subsidies might discourage NEV makers' motivation to compete with each other, resulting in less efficiency and less incentives for R&D.

In light of the concerns noted above, the government adopted a new policy in 2019, (i) abolishing the official list of recommended automobile battery suppliers, thus boosting competition in NEV battery markets; and (ii) adopting stricter technical specifications to qualify for a subsidy. It is to be expected that the new policy will bring more opportunities for foreign carmakers, under more competitive market conditions. In the list of companies receiving subsidies published by the Chinese government in December 2019, Tesla features, alongside Chinese companies, which may signal the beginning of new era for foreign NEVs in China.

B. Improvement of the Business Environment Promotes Competition in the Public Procurement of NEVs

In November 2019, the State Council issued its “Opinions on Further Effectively Using Foreign Investment.” This government document seeks to, among other things, optimize policies on the utilization of foreign investment in the automobile sector. One of the undeniable headline-grabbers among those measures is that the central government requires all regions across the whole country to ensure that NEVs produced by either Chinese- or foreign-funded motor manufacturers enjoy the same market access. Moreover, the government will create a level playing field in government procurement, and specifically will not discriminate against foreign entities when releasing public procurement information, setting supplier conditions, and elaborating bid evaluation standards.

Back in 2014, the Chinese government enacted a policy encouraging all levels of government to give NEVs priority over other types of vehicles. However, foreign automakers complained that the 2014 policy set an overly strict threshold for them to participate in public procurement opportunities for NEVs. Under the new 2019 policy, foreign automakers are likely to enjoy a fair opportunity to compete with domestic NEV makers in future public procurement processes.

VII. CLOSING REMARKS

The prospects for the business environment, and opportunities in the Chinese automobile industry have become brighter for both domestic and foreign automobile companies. On the other hand, public antitrust enforcement and private litigation in this industry have kept up their momentum in recent years. Enforcement activities indicate the determination and efforts taken by the Chinese antitrust authority to maintain competition and protect consumer welfare in the context of a further opening-up of industrial policy. As to EVs, whether competition policy will yield to industry policy remains to be seen. One example of the conflict is that in the draft Antitrust Guidelines on the Automobile Industry, it permits RPM for NEVs during a 9-month promotional period. To better comply with the AML, stakeholders may refer to the existing case law, which has revealed some risky practices, such as RPM, cartels, refusal to provide technical information, and restrictions on sales of spare parts in the after sales market. In this regard, the upcoming antitrust guidelines on the automobile industry will provide further guidance.



CPI Subscriptions

CPI reaches more than 35,000 readers in over 150 countries every day. Our online library houses over 23,000 papers, articles and interviews.

Visit competitionpolicyinternational.com today to see our available plans and join CPI's global community of antitrust experts.

