A BRIEF ANALYSIS OF STANDARDS FOR RESALE PRICE MAINTENANCE REGULATIONS UNDER THE PRC ANTI-MONOPOLY LAW

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I. DIFFERENT STANDARDS ARE ADOPTED IN ADMINISTRATIVE ENFORCEMENT AND JUDICIAL PRACTICE ON RESALE PRICE MAINTENANCE ("RPM")

Article 14 of the PRC Anti-Monopoly Law (the "AML"), which came into effect on August 1, 2008, prohibits RPM.[2] Nevertheless, the National Development and Reform Commission (the "NDRC")[3] did not issue its first RPM penalty decision, namely the *Liquor* case against Moutai and Wuliangye, until February 2013. In that case, the NDRC adopted the principle of "prohibition plus exemption," which is similar to the "*per se illega*l" standard. In particular, once a given agreement is deemed constitute RPM, the NDRC presumes it to be illegal without conducting any detailed analysis of its effects on competition, and is illegal unless it qualifies for an exemption under Article 15.[4] After the *Liquor* case, the NDRC continuously paid close attention to RPM agreements and imposed administrative penalties on RPM behavior in various industries such as milk powder, contact lenses, automobiles, household electric appliances and medical equipment. As recently as December 2019, the State Administration for Market Regulation (the "SAMR") imposed an administrative penalty of RMB 87.613 million yuan on Toyota. Based on the penalty decisions issued and published by the enforcement agencies, i.e. the NDRC and the SAMR, RPM agreements are presumed to have the effects of eliminating and restricting competition, and no detailed analysis was carried out.[5]

In contrast to the "*per se illegal*" principle adopted by the enforcement agencies, the "*rule of reason*" approach is adopted by the courts in civil lawsuits involving RPM. The application of the "*rule of reason*" was first established in the final judgment of the Shanghai High People's Court in the case of *Rainbow v. Johnson & Johnson* dated August 1, 2013.[6] In that case, the Shanghai High People's Court ruled that RPM agreements should not be subject to the "*per se illegal*" principle. For the purpose of determining whether the vertical agreement between Johnson & Johnson and Rainbow had the effects of eliminating and restricting competition, the following factors were analyzed in detail by the court: (1) whether the competition in the relevant market is sufficient; (2) whether the defendant has a strong market position; (3) the defendant's motivation to impose RPM; and (4) the anti-competitive effect and pro-competitive effect of RPM agreement.

By referring to the definition of "monopoly agreement" under Article 13 of the AML, the Shanghai High People's Court considered that the effects of "eliminating and restricting competition" are a necessary requirement for a finding of a "monopoly agreement." The court further determined that an RPM agreement would only constitute a monopoly agreement if the effects of eliminating or restricting competition are material and also cannot be offset by its pro-competitive effects. Hence, during the trial, the court made a substantive measurement and comprehensive analysis of the pro and anti-competitive effects of the agreement. In several subsequent civil lawsuits involving RPM agreements, other courts followed the approach established in the *Johnson & Johnson* case.

The discrepancy in the standards for analyzing RPM agreements adopted by law enforcement agencies and courts has aroused heated discussions among scholars and practitioners. Many scholars have called for a unified standard, but so far, administrative enforcement agencies and courts are still following two independent tracks on this issue.

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2 The "Anti-Monopoly Law of the People's Republic of China" was promulgated on August 30, 2007, and came into effect on August 1, 2008. Article 14 of the current AML stipulates that operators are prohibited from entering into monopoly agreements with counterparties, including fixing the price of commodities for resale to a third party and restricting the minimum price of commodities for resale to a third party.

3 NDRC is one of the three predecessors of the current antitrust enforcement agency, the State Administration for Market Regulation. It was in charge of regulating price-related monopoly behavior before April 2018.

4 Article 15 of the AML stipulates that, a monopoly agreement will be exempted from Articles 13 and 14 if the business operators can prove that the monopoly agreement reached falls into the following circumstances: (1) (the monopoly agreement is reached) for the purpose of technologies improvement, and research & development of new products; (2) for the purpose of product quality improvement, costs reduction, efficiency improvement, unifying product specifications or standards, carrying out professional labor division; (3) for the purpose of enhancing operational efficiency and reinforcing the competitiveness of small and medium-sized business operators; (4) for the purpose of realizing public interests such as conserving energy, protecting the environment and providing disaster relief, etc.; (5) for the purpose of mitigating the severe decrease of sales volume or obviously excessive production caused by economic recessions; (6) for the purpose of protecting the justifiable interests of the foreign trade or foreign economic cooperation; and (7) other circumstances prescribed by the law or the State Council.
Where a monopoly agreement falls under any of the circumstances prescribed in items (1)-(5) and is exempted from Articles 13 and 14 of this Law, business operators must also prove that the reached agreement shall not substantially restrict competition in the relevant market and can enable the consumers to share the benefits generated from the agreement.

5 In the *Medtronic* case and a few other cases, the enforcement agencies have conducted a relatively brief analysis of the anti-competitive effects and the effects of harm to consumers caused by the monopoly agreements reached by the parties.

6 Appeal case of vertical monopoly agreement dispute between Beijing Rainbow Science and Trade Co., Ltd. and Johnson & Johnson (Shanghai) Medical Equipment Co., Ltd, by Shanghai High People's Court, (2012) Hu Gao Min San (Zhi) Zhong Zi No. 63. The case was listed by the Supreme Court as one of the top ten antitrust judicial cases announced on the tenth anniversary of the implementation of the AML in 2018.

II. REASONS FOR DIFFERENT STANDARDS FOR ADMINISTRATIVE ENFORCEMENT AND JUDICIAL PRACTICE

A. Differences in Interpreting the Provisions of the AML

The differences between administrative enforcement and judicial practice can be traced back to the AML itself, particularly its provisions on the regulation of vertical "monopoly agreements." This ambiguity at the legislative level allows enforcement agencies and judicial authorities to interpret and apply laws from different perspectives and positions.

In the process of interpreting the law, enforcement officials focused their attention on the word "prohibit" in Article 14 of the AML, and believed that the principle of "prohibition plus exemption" was grounded in the wording of the AML. For example, Xu Kunlin, the former Director General of the NDRC's Price and Antitrust Bureau, stated in an article that "the provisions of China's Anti-Monopoly Law on vertical monopoly agreements are clear and definite. The Article 14 prohibits…vertical monopoly agreements and…Article 15 stipulates the conditions for exemption. There is no other legal interpretation from the legislative intent and textual understanding."[7] Other law enforcement officials such as Xu Xinyu,8 Wu Dongmei,[9] and Wan Jiang[10] also expressed similar views in their respective writings.

Judicial officials, on the other hand, are of the view that a determination of the existence of an actual effect of eliminating or restricting competition is a necessary requirement for finding the existence of a "monopoly agreement," considering that it is stated in Section 2 of Article 13 of the AML that "monopoly agreements as mentioned in this Law refer to… agreements, decisions or other concerted behaviors that may eliminate or restrict competition." Pursuant to Article 7 of "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," for the alleged monopolistic conduct that constitutes horizontal monopoly agreement as described in Article 13 of the AML, the burden shall be borne by the defendant to prove that the agreement does not have the effect of excluding or restricting competition.

Based on the above, a finding of the effect of excluding or restricting competition is obviously a necessary element for a horizontal monopoly agreement. Through this provision only directly applies to horizontal agreements, it serves as guidance for vertical agreements. In particular, considering that in contrast to horizontal agreements, vertical agreements are usually less likely to cause anti-competitive effects, it is reasonable to consider the effect of excluding or restricting competition to be a necessary element for prohibiting a vertical agreement. Hence, in several civil lawsuits including the *Johnson & Johnson* case, the courts ruled that the plaintiff not only needs to prove the existence of the agreement, but also needs to prove that the agreement has the effect of eliminating or restricting competition.

B. Considerations Behind the Standard Adopted by Enforcement Agencies

By analyzing articles and discussions published by officials from enforcement agencies, it is not difficult to see that enforcement agencies deliberately chose to adopt more stringent "prohibition plus exemption" standards for enforcement activities, in order to provide for greater deterrence of illegal conduct by enterprises and incentivize operators into strengthening antitrust compliance in future. This is not only a choice based on their understanding of the legislation, but also a choice made on the basis of comprehensive consideration of the current domestic situation in China. Specifically, enforcement agencies take the following elements into consideration when carrying out enforcement activities:

First, the general population's awareness and recognition of the AML is insufficient. Compared with Europe and America where the antitrust regime has been established for a relatively long time, and antitrust compliance awareness is deeply rooted in most enterprises, China's antitrust enforcement system is still in its infancy, and ordinary citizens know very little about the contents of antitrust laws and what they prohibit. In many industries and regions, companies and consumers do not realize that they have suffered losses, even if they are harmed by monopolistic behavior. This also explains why there is limited civil antitrust litigation in China. In the meantime, the implementation of the AML in China mainly depends on administrative enforcement agencies with professional capabilities.

7 Xu Kunlin, "The leniency policy applies to vertical monopoly agreements." China Economic Herald dated October 31, 2013, Section A03.

8 Xu Xinyu, "Research on China's Regulatory Framework of Vertical Monopolistic conduct [D]," (2016) University of Science and Technology of China 51.

9 Wu Dongmei, "Analysis on the Legal Regulation of Vertical Price Monopoly Agreement," Price Supervision and Anti-Monopoly in China, No.1 2014, page 42.

10 Wan Jiang, "Antitrust Law in China: theory, practice and comparison across jurisdictions," China Legal Publishing House, 2015, page 74.

Second, market competition in China is insufficient. Enforcement by administrative agencies has long been "based on the current state of China's socio-economic development as the background, with inadequate market competition and frequent vertical price monopolies being the main colors of the background."[11] In the *Milk Powder* case, the enforcement agencies found that the companies involved, although selling milk powder in China, the United States, and Europe at the same time, only implemented an RPM agreement in China, which reflects that the companies involved have did not pay sufficient attention to China's antitrust rules. On the other hand, it also reflects the insufficient competition in the Chinese market.[12] Similar behavior still exists widely in various industries in China. Therefore, antitrust enforcement agencies believe that market conditions within China are still immature. Given this limited ability to self-correct, the restrictive effects of vertical agreements need to be taken seriously and regulated under a stricter standard.

Third, the "prohibition plus exemption" standard also ensures enforcement efficiency. As stated in the Supreme Court's decision in the *Yutai* case that antitrust enforcement in China is still at an initial stage, if law enforcement agencies are required to conduct full investigations and complex competition analysis of each RPM agreement, it would increase the cost of enforcement and reduce enforcement efficiency, which would not meet China's antitrust enforcement needs at the present stage.[13]

C. Differences in the Judicial Process

As mentioned above, administrative enforcement is pro-active, which is reflected on the legislative level. According to Article 46 of the AML, law enforcement agencies conduct enforcement not only against enterprises who have reached and implemented the RPM agreement (presumably have actually disrupted the order of market competition), but also against the enterprises who have reached but not yet implemented the monopoly agreement.

In contrast, judicial procedures in civil lawsuits follow the principle of "he who asserts must prove" and adopt an adversarial approach. On one hand, the plaintiff needs to prove the existence of a monopoly agreement and the specific damage to the competition it caused; on the other hand, the defendant is allowed to refute and disprove these claims. In many lawsuits, both sides will engage economists to conduct comprehensive analysis, and the court will make a judgment after fully hearing the opinions of both parties.

Jurisprudentially, judicial officers believe that RPM can lead to two-sided effects on competition. The adoption of a "prohibition plus exemption" rule would require empirical evidence to prove that the negative effect of a given RPM practice in fact outweighs its positive effects. However, there exists no generally applicable statistical analysis for all types of RPM. Therefore, as long as no universally applicable conclusion can be drawn with regard to RPM, the application of the AML to RPM still calls for a case by case analysis, under the "*rule of reason*."[14] In addition, judges have recalled in some cases that price competition is only one aspect of competition and although RPM may limit price competition, it may promote non-price competition. In many industries in China, price competition has led to excessive investment and excessive competition.[15]

III. POSSIBLE FUTURE LEGISLATION

At this stage, academics and the practitioners still have not reached a consensus on the question of which principle should be applied to RPM agreements. However, regardless of whether the "prohibition plus exemption" principle or the "*rule of reason*" principle is adopted, differences between the administrative agencies and the judiciary remain to be bridged.

At the end of 2018, the Supreme People's Court's decision in the *Yutai* case attracted much attention from the public. The Supreme People's Court's decision affirmed the standard adopted by the enforcement agencies as well as the agencies' discretion in enforcement. In particular, the Supreme People's Court held that enforcement agencies only need to prove the existence of an RPM agreement and do not bear

11 Xu Kunlin, "The leniency policy applies to vertical monopoly agreements," China Economic Herald dated October 31, 2013, Section A03.

12 Wu Dongmei, "Analysis on the Legal Regulation of Vertical Price Monopoly Agreement," Price Supervision and Anti-Monopoly in China, No.1 2014, page 42.

13 Administrative Ruling of the Supreme People's Court of the People's Republic of China on *Hainan Yutai Science and Technology Feed Co., Ltd. v. Hainan Provincial Price Bureau* for administrative retrial ruling, the Supreme People's Court (2018), Zui Gao Xing Shen No.4675.

14 William Ding, "Judicial evaluation of restrictions on RPM behavior," (2014) Journal of Law Application, Page 59.

15 *Wuhan Hanyang Guangming Trading Co., Ltd. v. Shanghai Hantai Tyre Sales Co., Ltd.* case, Shanghai Intellectual Property Court (2016) Hu 73 Min Chu No.866.

the burden of proof as to whether a given agreement restricts competition. The court also held that the accused has the right to rebut the presumption of "restriction of competition" by submitting countervailing evidence. In addition, the judgment pointed out that for a plaintiff to prevail in antitrust civil litigation, they must prove actual losses and that those losses are in fact a direct result of the anti-competitive effects of an RPM agreement. In other words, in civil litigation, it is not inappropriate for the court to examine whether the RPM agreement has led to the effect of eliminating or restricting competition.

In the *Yutai* case, the Supreme Court hoped to establish guidance that would bridge the long-standing differences between administrative enforcement and civil litigation on the standards to be used for the analysis of RPM agreements under the AML. However, it remains to be seen whether the case can completely resolve these inconsistencies.

The newly published administrative decisions following *Yutai* case are illustrative. At the end of 2019, Toyota was subject to administrative penalties by the SAMR for implementing an RPM agreement. If an enterprise files a civil lawsuit to the court on the basis of those administrative penalties, claiming that Toyota's monopolistic behavior caused them losses, would the plaintiff need to re-prove the anti-competitive effects of the RPM agreement in the litigation process? If the plaintiff is allowed to rely on the existing administrative penalties without proving any anti-competitive effects of the RPM agreement, it would contradict the Supreme People's Court's ruling in the *Yutai* case with respect to the plaintiff's burden of proof; nevertheless, if the plaintiff is still required to prove the anti-competitive effect of the RPM agreement, the plaintiff would lose the opportunity to enjoy the benefits of follow-on litigation. In follow-on litigation, plaintiffs are supposed to be able to rely on administrative decisions to a large extent. However, in the current situation, administrative enforcement and judicial proceedings are implemented in parallel, the plaintiff still has to bear a heavier burden of proof.

It is worth noting that in the current version of the AML, the definition of "monopoly agreement" is set out in Section 2 of Article 13, while Section 1 of the same Article concerns the prohibition of horizontal monopoly agreements. However, in the proposed amendments of the AML (Public Consultation Draft) recently released, the definition of "monopoly agreement" is listed separately, before the articles concerning horizontal and vertical agreements. This draft can be interpreted to mean that both horizontal and vertical agreements caught by the AML need to be in fact anti-competitive, which reflects that legislators have paid attention to concerns arising from practices.[16] However, even with this adjustment to the AML, it would still be unclear how to resolve the differences between administrative enforcement and judicial practice. We expect legislators, enforcement agencies, and judicial authorities to further clarify the standards by modifying the law, formulating judicial interpretations, issuing guiding cases, or issuing guidelines for enforcement against vertical agreements, so as to provide business operators with clearer guidance.

16 King & Wood Mallesons antitrust team (Susan Ning, Kate Peng, Zhifeng Chai, Ruohan Zhang, Tianjie Zhang, Nan Du), "Potential Impacts of the Proposed Anti-monopoly Law Amendments" (Jan. 8, 2020), see https://www.chinalawinsight.com/2020/01/articles/antitrust/%e5%8d%81%e9%97%ae%e5%ae%9e%e7%ad%94%ef%bc%9a%e3%80%8a%e5%8f%8d%e5%9e%84%e6%96%ad%e6%b3%95%ef%bc%88%e4%bf%ae%e8%ae%a2%e8%8d%89%e6%a1%88%ef%bc%89%e3%80%8b%e5%af%b9%e4%bc%81%e4%b8%9a%e7%9a%84%e5%bd%b1/, accessed on Feb. 1, 2020.

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