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Trade Associations and Private Antitrust Litigation in China

Hao Qian

China University of Political Science and Law

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I. INTRODUCTION

Trade associations present a peculiar issue in China's competition law, due to their unusual origin and development. No voluntarily established business associations were possible or necessary in the era of central planning, when the Chinese economy was based on state-ownership and bureaucratically managed by the government. Only when China embarked on a new course to embrace a market economy in the early 1980s did trade associations begin to emerge, but they were far from representing the small and gradually expanding private sector. To facilitate the still on-going government restructuring during the past three decades, most of China's trade associations were created primarily to take over redundant/retired officials and take on the regulatory functions that reorganized administrative agencies had to divest. As of today, even though they are in theory "social organizations," trade associations still must obtain the endorsement and supervision of certain government authorities in order to register and operate legally.² The government explicitly acknowledges that trade associations have yet to unhook their connections with administrative agencies.

The inherent semi-government role of trade associations in China often enables them to exert a greater influence on the market competition than their counterparts in mature market economies. Except in a few state monopolized industries, Chinese enterprises are generally of small size and with low competitive capacity. However, trade associations are capable of initiating and orchestrating concerted action among their members. In many cases, they do so to implement government policies that are not necessarily consistent with fair competition. But even when they pursue their own self-interest, for example through various measures motivated by local protectionism, trade associations possess enhanced abilities to detect and punish any deviation by members; abilities which are essentially buttressed by their government affiliations. Additionally, the fragmented structure of the Chinese market often makes it easy for even small trade associations to organize anticompetitive activities among members, thus effectively monopolizing relatively closed and isolated local markets.

For the above reasons, trade associations have figured largely in China's competitive landscape. In the drafting process of the *Anti-Monopoly Law* ("AML"), cartels orchestrated by trade associations already posed a major concern regarding private monopolies.³ Open price-

¹ Associate Professor, China University of Political Science and Law. Research related to this article is funded by a grant from the Scientific Research Foundation for the Returned Overseas Chinese Scholars, Ministry of Education of China.

²Regulation on Registration and Administration of Social Organizations, [1998] State Council Order No. 250. Articles 3, 9, 27, 28.

³ Youngjin Jung & Qian Hao, *The New Economic Constitution in China: A Third Way for Competition Regime?*, 24 NW. J. INT'L L. & BUS. 107, 119 (2003).

fixing maneuvers in 2007 by the China branch of the “International Ramen Manufacturers Association” not only rallied additional support for the AML draft during the last stage of the bill, but also in great part enabled the insertion of three provisions specifically on trade associations⁴ into the final legislation.

Since the AML entered into force in August 2008, trade associations have remained in the spotlight in enforcement activities. Of the seventeen investigations that the State Administration for Industry and Commerce (“SAIC”) had initiated by November 2012, sixteen cases involved activities organized by trade associations.⁵ Similarly, most of the major price monopolies handled by both the National Development and Reform Commission (“NDRC”) and its local counterparts have been those arranged by trade associations.

However, at the same time, not many private antitrust suits have been brought against trade associations. In fact, Article 50 of the AML generally states that a business operator “shall bear civil liabilities” if its monopolistic conduct causes losses to aggrieved parties. In the *Provisions on Several Issues concerning the Application of Law in the Trial of Civil Dispute Cases Arising from Monopolistic Conduct*⁶ (“Judicial Interpretation”) published in May 2012, the Supreme People’s Court further lists “articles of association in violation of the AML” as a cause of civil action against trade associations.

These provisions would seem to have paved the way for private parties to bring a civil lawsuit against trade associations violating the AML. Yet they also leave much room for interpretation and point to general issues in civil law and procedure, the application of which in relation to the AML remains largely unexplored. In contrast to administrative sanctions on trade associations pursuant to Article 46(3) of the AML (the legal basis for NDRC and SAIC enforcement activities) it is unclear in the law whether, or to what extent, in a civil lawsuit a trade association should be held liable for losses caused by monopolistic conduct of its members but organized by the association.

As a result, to date, private antitrust suits against trade associations have not appeared to be a desirable option. On the other hand, the limited number of antitrust cases in which a trade association was sued for civil damages sheds important lights on how the courts have tackled ambiguities in the law. This paper examines some of the major issues that the courts have addressed in several reported court judgments of such cases, in the context of both the AML and relevant laws, in order to analyze the emerging legal rules applicable in civil suits against trade associations for AML violations.

II. TRADE ASSOCIATIONS AS BUSINESS OPERATORS?

According to Article 50 of the AML, a trade association must be a “business operator” in order to be subject to civil liabilities under this provision. For the purpose of the AML, Article 12 defines a “business operator” as a natural person, legal person, or any other organization that

⁴ Anti-Monopoly Law of the People’s Republic of China, [2007] Presidential Order No. 68. Articles 11, 16, 46(3).

⁵ See SAIC announcement, *available at* <http://news.hexun.com/2012-12-04/148689653.html>.

⁶ Provisions by the Supreme People’s Court on Several Issues concerning the Application of the Law in the Trial of Civil Dispute Cases Arising from Monopolistic Conduct, [2012] Judicial Interpretation No. 5.

engages in the production of or operation of business relating to commercial goods, or the provision of services.

As the language of both the term itself and the definition seem to suggest that business activities are essential for the concept of the business operator, given the established semi-public role of trade associations in China, a threshold question arises as to whether the definition of “business operators” is broad enough to include trade associations. To be more specific, it is debatable whether the work of the trade association can be reasonably construed to be the kind of “services” covered by Article 12.

“Business operator” is a generic term used in various Chinese laws, most of which were promulgated before the AML. The interpretation of the term under other statutes provides useful references to answer how “business operator” should be defined under the AML.

The argument against labeling trade associations as business operators is probably best supported by the fact that the two groups are organized pursuant to different laws. By registering with the Ministry of Civil Affairs and its local entities, trade associations are established as “social organizations,” which are explicitly prohibited from engaging in for-profit business activities.⁷ In contrast, business organizations are registered with SAIC and its local counterparts in accordance with company law, partnership law, proprietorship law, or individual business regulations. The different treatment makes it more sensible to distinguish trade associations from business operators, a term which has been created by the law with the purpose of covering only those independent profit-making market competitors.

Indeed, “business operators,” as defined under the *Anti-Unfair Competition Law* (“AUCL”),⁸ clearly acknowledges such a distinction. Article 2(3) of the law provides that a business operator refers to a legal person, other economic organization, or a natural person that engages in operation of business relating to commercial goods, or profit-making services.

This definition of business operators has been used in other laws or accepted by authorities in the enforcement of other laws. For example, according to Article 55 of the *Food Safety Law*,⁹ if a social organization (often a trade association) recommends certain food products to the consumers in false advertisements, it should be held jointly liable for damages together with the manufacturer/business operator. In an official reply¹⁰ issued in 2003 to clarify the definition of “business operators” under the *Price Law*, NDRC stressed that a business operator must have obtained legal qualifications to engage in business activities. One could reasonably view this requirement as to exclude trade associations.

However, the courts have not always strictly applied the AUCL definition of business operators. In *Zhonghui v. The China Electrical Equipment Industry Association* (“CEEIA”),¹¹ the CEEIA contacted manufacturers of electric cables and wires to assert its exclusive control over

⁷ Regulation on Registration and Administration of Social Organizations, [1998] State Council Order No. 250. Article 4.

⁸ Anti-Unfair Competition Law of the People’s Republic of China, [1993] Presidential Order No. 10.

⁹ Food Safety Law [2009] Presidential Order No. 9. Article 55.

¹⁰ A Reply on How to Define “Business Operators” under the Price Law, [2003] NDRC General Office, No. 884.

¹¹ Beijing [2006] First Intermediate Civil Final 2494.

the publication of the *Catalog of Price Quotations of Electric cable and Wire Products*, prohibiting any cooperation with *Zhonghui*, a company that was working to produce a similar catalog. This particular catalog, as found by the Beijing First Intermediate People's Court, was used to provide price change information and regulate pricing activities within the industry. Highly authoritative, and with force similar to that of government guidelines, the document could only be issued by an entity approved by the government. Each party argued that it had the authorization from the appropriate authorities, thus vying for certain regulatory functions rather than the right to provide commercial products. The court decided that AUCL did not apply to the CEEIA, because as a social organization with regulatory responsibilities the association was not a business operator.

But, less than two months later, the same court gave a different opinion in *Aizhi v. the China Friction & Sealing Material Association*¹² ("CFSMA"). CFSMA had the responsibilities to "guide, supervise and coordinate" activities within the friction and sealing material industry. In order to dispel improper publicity about a member company, the association sent written statements to consumers about the company and its products. According to the court, due to CFSMA's special status its statements were especially authoritative and influential, with a direct impact on the competition between its members and non-members such as *Aizhi*. Although it was recognized that the CFSMA was a nonprofit organization according to its articles of association, in the view of the court, by issuing a statement about one particular member company that had the effect of an advertisement, the CFSMA had participated in market competition and therefore should be subject to AUCL.

The Shanghai High People's Court took a step further in *Bohua & CMP v. China Food Additive Production & Application Industry Association* ("CFAA")¹³ and held that the CFAA qualified as a business operator due to its profit-making services of hosting professional exhibitions of food ingredients. The court reasoned that the key element of the AUCL "business operator" definition was profit-making activities. According to this judgment, any person or organization, even one entrusted with authority to regulate a certain industry such as the CFAA, to the extent it engages in for-profit business should be considered as a business operator under the AUCL.

These three cases reveal practical difficulties in applying pre-AML competition provisions, due to the conflicting roles of trade associations. Working closely with the government authorities, trade associations are designed to be *de facto* regulators, as demonstrated in the *Zhonghui* case. However, in reality, trade associations often engage in activities inconsistent with their quasi-regulatory responsibilities, either interfering with competition as in *Aizhi*, or competing directly in the market as in the *Bohua* case. Clearly, in both cases, the courts saw it necessary to rein in the trade associations. But due to the lack of laws/regulations specifically on trade associations, the courts sought to subject them to the rules on business operators.

¹² Beijing [2006] First Intermediate Civil Final 5251.

¹³ Shanghai [2006] High Civil III (IP) Final 102.

Compared with the AUCL, a notable change in the definition of business operator under the AML is that the “for-profit” element has been dropped. In effect this allows the AML to move along the lines of *Aizhi* and *Bohua* to make the definition more inclusive to cover trade associations. The court’s reasoning in *Aizhi* has an obvious caveat. Just because CFSMA’s statement would have an impact on competition among its members and other companies does not make the CFSMA itself a competitor or subject it to the legal treatment of a competitor. In the *Bohua* case, the court plainly erred in abdicating the explicit legal requirement that forbids trade associations from for-profit activities. CFAA’s profit-making service to organize professional exhibitions should have been held illegal, but instead the court viewed it to be the basis to make the CFAA a business operator.

Under the AML, the problems presented in *Aizhi* and *Bohua* no longer exist. The courts do not have to stretch the definition of business operator or identify the for-profit services provided by a trade association in order to invoke Article 50. For example, in *Hui Erxun v. Shenzhen Pest Control Association* (“SZPCA”),¹⁴ one of the latest antitrust private cases against a trade association, the issue of the SZPCA as a business operator was never disputed. In fact, the association implicitly admitted being a business operator under Article 50. Given the evolution of the definition of business operator, it is likely that the courts will continue to follow the permissive approach in order to allow the initiation of civil litigation against trade associations under Article 50.

III. HOLDING TRADE ASSOCIATIONS LIABLE IN CIVIL CASES UNDER THE AML

Although the Judicial Interpretation has specified an additional cause of action against trade associations—articles of association in violation of the AML—its value is doubtful. It is quite rare for a trade association to include illegal terms in its articles of association, which are generally worded and must be approved by various government authorities in the process of its establishment. As shown by the enforcement activities of SAIC and NDRC, most of the AML violations by trade associations that have taken place involve monopolistic agreements. This section briefly looks into the main issues for suing trade associations under Article 50 for organizing monopolistic agreements.

Article 16 of the AML prohibits any trade association from organizing business operators in its industry to engage in monopolistic conduct forbidden by Chapter II of the law, i.e. to reach or implement monopolistic agreements. From the language of this provision, it is not clear whether such “organizing” would also constitute a kind of “monopolistic conduct,” as required in Article 50 in order to incur civil liabilities. In contrast, enforcement agencies only need to prove that a trade association indeed organized any monopolistic agreement to impose administrative sanctions pursuant to Article 46(3). Although as a matter of law the issue needs to be clarified, so far the ambiguity has not presented a problem. In both *Liu Fangrong v. Insurance Association of Chongqing* (“IACQ”)¹⁵ and *Hui Erxun v. Shenzhen Pest Control Association* (“SZPCA”), the courts focused on whether there existed any price-fixing agreement among members, suggesting that once such an agreement was established, the trade association organizing it should bear civil liabilities as well.

¹⁴Guangdong [2012] High Civil III Final 155.

¹⁵Zhan Hao, *The Hot Issues of China Anti-Trust Private Litigation*, Law Press (2012), 247-248.

The general rule of burden of proof in civil litigation, which requires each party to provide evidence to support its own claim,¹⁶ makes it extremely difficult for a private party to establish that first a monopolistic agreement exists among members of a trade association, and second that the trade association organized this agreement. Compared with administrative enforcement activities, civil antitrust litigation against trade associations is almost only possible when key evidence is made public or easily available. One typical example relates to monopolistic agreements that take the form of a self-disciplinary code imposed by a trade association.

In the *Liu Fangrong* case, local insurance companies all signed an industry self-disciplinary code that required them to comply with “advisory insurance rates” set by the IACQ. Non-compliance with the price provision would result in severe sanctions, also laid out in the code. The plaintiff sued the IACQ for violation of Article 13 of the AML on horizontal monopolistic agreements.¹⁷

In the *Hui Erxun* case, an almost identical issue was raised. The SZPCA signed a Shenzhen Pest Control Service Self-Disciplinary Code with all its members. The code sets the minimum prices as 80 percent of those stipulated by the Shenzhen Price Bureau in a 1997 circular. Any price below the price floor would constitute “unfair competition” subject to sanctions by the SZPCA, including the revocation of the qualification certificate to provide service. The plaintiff was a company that paid for pest control services from a member of the SZPCA. Not only was the price floor contained in the code and implementing rules, the contract between the plaintiff and the pest control company also included a reference to the code as the basis for price calculation.

In both cases, essentially the core issues narrowed to become similar to those in a civil suit challenging a monopolistic agreement without the involvement of a trade association. Although the court in *Liu Fangrong* did not rule because the suit ended in settlement, in the part of the proceeding that did take place, both sides set out to argue the legality of the price clauses of the self-disciplinary code. In the *Hui Erxun* case, the court identified and focused on only two issues: (1) whether the conclusion of the Shenzhen Pest Control Service Self-Disciplinary Code amounted to price-fixing; and (2) whether SZPCA’s activities in relation to the code could be justified or, in other words, whether there were grounds to exempt the code according to Article 15.

Another issue concerns the civil remedies that the plaintiffs can seek in such cases. Although the courts have provided virtually no guidance in AML cases, it seems well accepted in other areas that the purpose of suing trade associations is more about correction of wrongdoings than to obtain monetary damages. For example, the court in *Aizhi* stated that in bringing the lawsuit the plaintiff primarily aimed to put an end to CFSMA’s inappropriate advertisement and to restore normal business order within the industry. In the judgment, the court ruled in favor of the plaintiff but only ordered the CFSMA to stop circulating the disputed statement and publish a revised announcement on its website for 24 hours. The plaintiffs in the *Bohua* case likewise

¹⁶Civil Procedure Law (amended), Presidential Order [2012] No. 59. Article 64.

¹⁷The plaintiff soon withdrew the suit when the IACQ proved that the disputed code was revised in accordance with the AML.

won without being awarded any damages. The court saw it sufficient to order the CFAA to lift the ban on attending other exhibitions and run an online statement to eliminate adverse effects.

This pattern will likely continue in AML civil lawsuits. In both the *Liu Fangrong* case and the *Hui Erxun* case, the plaintiffs only requested that the respective self-disciplinary codes be invalidated and that a nominal damage of one yuan be paid by the defendant association.

IV. DEFINING THE ROLE OF TRADE ASSOCIATIONS

According to Article 11 of the AML, trade associations should endeavor to improve industry self-discipline, guide business operators to engage in lawful competition, and preserve the competition order in the market. Yet, as discussed above, the often-conflicting roles of a trade association make it difficult to draw the line between quasi-regulation and anticompetitive activities.

All of the reported decisions made by the enforcement agencies are based on findings of AML violations. So these decisions have significantly contributed to an improved understanding of how trade associations might abuse their positions and distort market competition. But, on the other hand, these decisions provide little assistance in determining the trade associations' appropriate role in the market. In this regard, the courts are in the unique position to develop such rules, and the *Hui Erxun* case presents a particularly useful example.

In this case both the court of the first instance (the Shenzhen Intermediate People's Court) and the appellate court (the Guangdong High People's Court) seem to have deliberately chosen to discuss the propriety and reasonableness of the behavior of SZPCA, after having concluded that the self-disciplinary code did not constitute price-fixing.

The lower court declared that the rule of reason should be applied to determine whether monopolistic agreements existed. According to the court, even where a certain agreement had restrictive effects, it could be exempted due to justifiable purposes. Then the court proceeded to apply to the case Article 15(1) (4), the relatively open-ended public interest provision under the article that can exempt agreements among business operators from the application of Articles 13 and 14. The court reasoned that pest control service was a special sector that affected the public interest, due to the large amount of poisonous pesticides used and the potential dangers to public health. If service providers were allowed to engage in price wars, quality and standards of service would suffer, resulting in great harm to the environment and human health. Therefore the court found that its legitimate goal of avoiding destructive competition provided sufficient justification for the code, which lent additional support to the conclusion that the code did not amount to a monopolistic agreement.

The Guangdong High People's Court did not base its analysis on Article 15 and limited its discussion on SZPCA's defense that its behavior was justifiable. The court emphasized that the AML should protect fair competition as well as consumers' interests and public interests. The court cited several government documents in which below-cost pricing in the pest control industry was identified as a threat to market competition, consumers' interests, and the public interests. Therefore the court accepted SZPCA's defense on justification.

The two courts employed different arguments in reaching the same conclusion. The Shenzhen Intermediate People's Court conducted a more interesting antitrust analysis by

invoking the rule of reason and attempting to find a solution in Article 15. In doing so, it raised a defense for the SZPCA and explored a solution unnecessary for its ruling. However, this provided a more normative approach in addressing issues on trade associations. The Guangdong High People's Court probably provided a line of reasoning more appropriate for the case. It also focused more on the connection between government authorities and the SZPCA, a factor also important in understanding the role of trade associations. Both arguments are likely to be further developed and used in future cases.

V. CONCLUSION

Among the small number of private antitrust lawsuits in China so far, only very few have involved trade associations. But trade associations have long posed complex issues to China's competition law and practice, particularly due to their conflicting and unsettled roles which have been shaped by China's economic transition and on-going government restructuring. Although enforcement activities have focused on trade associations, it is still important to push for more progress in private litigation, especially because administrative enforcement seldom reaches beyond provincial levels while China's highly fragmented market is rampant with small cartels organized by local trade associations.

Due to the small number of antitrust private cases against trade associations, this paper examines three issues on which only broad strokes have been painted. The definition of "business operator" has gradually broadened in order to include trade associations under Article 50 of the AML. However, while civil suits can be brought against trade associations, the heavy burden of proof has made it possible to challenge only overt cartels, with hardly any monetary remedies available. In addition, due to the semi-regulatory role of the trade associations, their activities might be supported by justifications such as policy considerations and public interest for which the AML leaves much room.

In addition to the common difficulties in private antitrust litigation, civil cases against trade associations face other challenges. In the foreseeable future those cases will still be limited and continue to be contingent on the development of both civil procedural rules and the AML. At the same time, it will continue to be an interesting area where many of the pathologies of the antitrust law in China are demonstrated.