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Internet Players:  
*Qihoo 360 v. Tencent*

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## Analyzing Competition Among Internet Players: Qihoo 360 v. Tencent

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### I. INTRODUCTION

In one of the most significant antitrust decisions since China implemented the Anti-Monopoly Law (“AML”) in 2008, the Guangdong High People’s Court (“Guangdong High Court”) dismissed claims on anticompetitive bundling and exclusionary practice brought by Qihoo 360 against Tencent.<sup>2</sup> The Guangdong High Court issued an 80-page decision that provided a relatively sophisticated and nuanced analysis of market definition and market power that examined internet-based competition, recognized the importance of multi-sided platforms in this competition, and highlighted the critical role of dynamic competition.

Although Qihoo 360 has appealed the decision to China’s Supreme Court it now stands as both a landmark decision in China and an exemplar of serious antitrust analysis of the internet sector for courts and competition authorities around the world.

### II. THE CHINESE INTERNET INDUSTRY

China has a large and rapidly growing internet sector based primarily on domestic Chinese firms. According to China Internet Network Information Center (“CNNIC”), there were 564 million internet users in China—42.1 percent of the population—at the end of December 2012.<sup>3</sup> Table 1 below reports the major Chinese internet platforms and their major activities as of late 2010 when Tencent engaged in the actions that gave rise to Qihoo 360’s complaint. Tencent, which focuses on instant messaging, was the largest firm based on monthly users with 340 million monthly visitors to its various sites. Its market cap as of April 15, 2013 was \$3.67 billion. Qihoo 360, which focuses on antivirus software, was the fourth largest with 275 million monthly users. Its market cap as of April 15, 2013 was \$58.74 billion.<sup>4</sup>

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<sup>2</sup> See the Guangdong Province High People’s Court’s Civil Judgment No. Yuegaofaminsanchuzi 2/2011. The Chinese version is available at <http://www.gdcourts.gov.cn/gdcourt/front/front!content.action?lmdm=LM43&gjid=20130328040159946185>. An English version is attached as an appendix to this article.

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

<sup>4</sup> As of April 15, 2013, 1USD=7.7623 HKD. The market cap of Tencent was 456 billion HKD as of April 15, 2013.

Most of the major global internet players do not have significant shares of traffic in China. Instead, domestic companies offer services similar to those offered by international players. Baidu is the leading search-engine platform, Renren is the leading social network, Taobao is the leading e-commerce site, and Sina Weibo is the leading micro-blogging site similar to Twitter. Most of these firms, including Tencent and Qihoo 360, offer a diverse set of products and services to attract users. Most of these platforms earn a significant portion of their revenue by selling advertising on the web pages seen by users.

Tencent attracts users by providing a variety of free services including instant messaging (“IM”), micro-blogging, online games, online security, social networking, search, and e-commerce. QQ, Tencent’s free instant messaging service, had 399 million monthly active users as of February 2012.<sup>5</sup> Tencent makes money from selling advertising to companies that want to reach its users, selling virtual products/items for its online gaming services, charging its users for bundled SMS packages, providing mobile games, and charging for other mobile value-added services such as mobile books and mobile games.<sup>6</sup>

Qihoo 360 attracts users by providing a variety of free services including online and mobile security such as anti-virus software, a web browser, and a game platform with games developed by third-party game developers.<sup>7</sup> Qihoo 360’s Safety Guard, which is an internet security product, had 366 million monthly active users in February 2012.<sup>8</sup> Qihoo 360 makes money from selling advertising and providing web game services.

**Table 1.** Major Chinese Web Properties, November 2010

Ranking	Platform Type	Platform	Monthly Users (Millions)	Share in Major Players
1	Instant Messaging	Tencent QQ	340.13	11.16%
2	Search Engine	Baidu	335.45	11.01%
3	Integrated Portal	Sina Web Portal	275.61	9.05%
4	Antivirus	360 Security Guards	275.33	9.04%
5	Integrated Portal	Netease	233.38	7.66%
6	Online Shopping	Taobao	220.95	7.25%
7	Integrated Portal	Sohu	212.85	6.99%
8	Online Video	Youku	203.56	6.68%
9	Online Video	Tudou	175.60	5.76%
10	Search Engine	Google	175.21	5.75%
11	Community	Tianya	132.00	4.33%
12	Site Map	Home of Websites	123.09	4.04%
13	Online Video	Ku6	120.09	3.94%
14	Online Video	Thunder Video	118.81	3.90%
15	Integrated Portal	Phoenix	104.89	3.44%

Source: 2010 Internet Usage Statistics iResearchchina.com

<sup>5</sup> iResearch data on number of users per month (February 2012).

<sup>6</sup> See TENCENT HOLDINGS LIMITED, 2011 ANNUAL REPORT 107 (2011), available at <http://www.tencent.com/en-us/content/ir/rp/2011/attachments/201102.pdf>.

<sup>7</sup> See Qihoo 360 Technology Co. Ltd, Registration Statement (Form F-1) (Mar. 14, 2011), available at <http://www.sec.gov/Archives/edgar/data/1508913/000104746911002124/a2202432zf-1.htm>.

<sup>8</sup> iResearch data on number of users per month (February 2012).

### III. QIHOO 360'S CLAIMS

Qihoo 360's claims relate to a series of events that took place in late 2010 and were widely publicized in China.<sup>9</sup>

In September 2010, Tencent asked IM users that had its "Software Manager," which did not include anti-virus software, if they wanted to upgrade to "PC Manager" which did. Consumers did not have to upgrade and, if they did, they could run other anti-virus software instead of Tencent's anti-virus software.

On November 3, 2010, Tencent required users to stop using Qihoo 360's anti-virus software if they wanted to continue to use Tencent's IM software. Tencent's users could still use anti-virus software provided by providers other than Qihoo 360 as well as Tencent's own anti-virus software. The next day, Tencent rescinded that decision following complaints from the Chinese government.<sup>10</sup>

Qihoo 360 filed a private antitrust case before the Guangdong High People's Court on November 15, 2011, accusing Tencent of violating China's AML. China's AML provides for parties to file private antitrust lawsuits and to seek remedies and damages in addition. The Tencent decision is one of the first court decisions, and arguably the most comprehensive, under the new law.

Qihoo 360 asserted that the relevant antitrust product market was integrated IM. Integrated IM includes text, audio, and video communication capabilities. Few companies provided integrated IM. Tencent is the leader with 76.2 percent of users. However, a number of companies provide one or two of the three components. Qihoo 360 argued that consumers would not substitute an integrated IM solution for one of these. It also claimed that consumers would not substitute other communication methods. To support its case, Qihoo 360 submitted a report by an economic expert. According to the Court's decision:<sup>11</sup>

The "Economic Analysis Report on the Anti-monopoly Disputes between Qihoo 360 and Tencent" by the RBB company suggests that the only difference among the three types of services is the medium of communication, but the common features are online status notice, communication among small groups of users, and real-time and cross-platform interaction. All three services are often available through a single, integrated front-end device. Therefore, it is difficult for products lacking of any of the aforementioned three functions to be considered by most consumers as a good substitute.

Qihoo 360's economic expert also argued that microblogging and social networking products were not substitutes for integrated IM services. It based that conclusion on the simple

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<sup>9</sup> Chen Zhi, *Qihoo 360 Loses Suit Against Tencent*, XINHUA NEWS (March 29, 2013), [http://news.xinhuanet.com/english/china/2013-03/29/c\\_124517084.htm](http://news.xinhuanet.com/english/china/2013-03/29/c_124517084.htm); See also Wang Guanqun, *China to Investigate Law Violation in Tencent - Qihoo 360 Spat*, XINHUA NEWS (November 21, 2010), [http://news.xinhuanet.com/english2010/sci/2010-11/21/c\\_13616063.htm](http://news.xinhuanet.com/english2010/sci/2010-11/21/c_13616063.htm).

<sup>10</sup> Li Bin, *Multisectoral Come Forward to "Call a Timeout" Intermission "3Q War,"* BEIJING TIMES REPORTER, (Nov. 5, 2010), [http://epaper.jinghua.cn/html/2010-11/05/content\\_600180.htm](http://epaper.jinghua.cn/html/2010-11/05/content_600180.htm).

<sup>11</sup> See the Appendix for an English-language translation of a portion of the decision. See also the original Chinese version of the Court decision, *supra* note 2.

correlation between the weekly use of integrated IM and social networking sites. Qihoo 360 also asserted that the relevant geographic market was China.

Qihoo 360 claimed that Tencent had a dominant position in the integrated IM product market in China. Under Article 17 of the AML, a firm has a dominant market position if it has the ability to control price, quantity, or other trading conditions of products in the relevant market, or to hinder or affect other operators entering the relevant market. In other words China's definition of dominant position is similar to the notion of having significant market power. Qihoo 360 argued that Tencent was dominant because it had a 76.2 percent share of the overall integrated IM market in China.

Finally, Qihoo 360 asserted that Tencent had violated Article 17 of the AML. The AML prohibits firms from abusing a dominant position to exclude or restrict competition. Qihoo 360 argued that Tencent's September 2010 decision to include its security software with its integrated IM software was unlawful tying. It also claimed that Tencent's November 2010 decision to forbid its IM users from having Qihoo 360's anti-virus software was an exclusionary practice.

#### IV. MARKET DEFINITION

The Guangdong High Court used the evidence before it to conduct a hypothetical monopolist test to evaluate Qihoo 360's proposed relevant product market definition. It considered both demand and supply-side substitutability in doing so.

Integrated IM services are provided for free. Qihoo 360's economic expert argued that it was possible to conduct a qualitative SSNIP test by focusing on the possibility that the hypothetical monopolist could reduce quality or increase the "hidden" price to the user of having to look at advertisements. The Court rejected this reasoning and focused on evidence related to price:

The Court believes that this case reflects one of the main characteristics of the products and services provided by Internet service providers, i.e., almost all of the suppliers set the price of their basic services at zero. It is true that "free" has become a common, fundamental and viable mode of service for instant messaging services and antivirus security software provided by the defendant and the plaintiff, respectively, as well as for other services such as search engines, microblogging, e-mail, social networking services, news, video and music, etc.

The Court then went on to cite empirical evidence based on consumer surveys that users would switch away if the provider charged for the service.<sup>12</sup> It concluded that, while quality and advertising were relevant, "a more important factor to consider is whether a lot of demand

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<sup>12</sup> According to the Court, "[t]he evidence in this case shows that users of instant messaging products and services are highly sensitive to prices. According to the survey of CNNIC, up to 60.6% of users do not want to pay for instant messaging services and 32.7% of users who are willing to pay would only pay for the value-added services on the instant messaging platform, rather than paying for the basic service of instant messaging. A survey of the website eNet shows that if the defendant charges all QQ users it will lead to a loss of 81.71% of its users who will switch to other free instant messaging products and services. In the Microsoft/Skype merger case, evidence shows that if Skype starts to charge users for its service more than 75% of the individual consumers will no longer use the product." *Id.*

substitution will be generated if a hypothetical monopolist charges the service on a small scale continuously.”<sup>13</sup>

The Court then concluded, based on the evidence on price sensitivity, that consumers of integrated IM would likely switch to free component services if the hypothetical monopolist raised its price modestly from zero. Importantly, from the standpoint of sound antitrust economic analysis, the Court rejected the plea from Qihoo 360’s economic expert to focus on functional differences between products in favor of quantitative evidence, limited though it was, on the elasticity of demand.<sup>14</sup>

The next market definition issue was whether micro-blogging and social networking belonged in the relevant product market. Qihoo 360 said no. To support this conclusion its economic expert calculated the correlation coefficient between the use of social networking and IM software on a weekly and monthly basis over a short period of time. It reported that these correlation coefficients were close to zero and claimed this showed lack of substitutability.

The Court rejected this conclusion for a number of reasons including: (a) lack of micro-blogging in the analysis during a period in which there was a rapid increase in the use of micro-blogging; (b) the ability of micro-blogging, social networking, and IM to provide similar functions to the consumer which was supported by a variety of anecdotal evidence; (c) the Court’s view that an increase in price of integrated IM would lead consumers to switch to free micro-blogging and social networking products; and (d) the fact that the economic expert focused on the very short term and did not consider dynamic competition.

The last point warrants further mention since the Guangdong High Court provided a nuanced discussion of the importance of dynamic competition and its role in antitrust analysis:<sup>15</sup>

The Court finds that competition is a dynamic process, and when defining a relevant market in an antitrust lawsuit regarding the abuse of a dominant market position, we must consider the status quo and future trends and development of relevant industries. Generally speaking, those acts of abuse of market dominance which are likely to continue for some time should be stopped in order to effectively maintain the market competition mechanism. Strong network technology innovation capabilities and rapid changes of business models are significant features of the Internet industry. Since 2010, microblogs and social networking sites have demonstrated a high degree of integration with instant messaging in a relatively short period. Therefore, when identifying the relevant market it will not lead to a scientific, rational and effective suppression of abuse of

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<sup>13</sup> See the Appendix for an English-language transition of a portion of the decision. See also the original Chinese version of the Court decision, *supra* note 2. The correct SSNIP test should consider the impact of price changes on both sides of the platform—users and advertisers—but the Court focused on the single-sided SSNIP analysis presented by Qihoo 360.

<sup>14</sup> According to the Court, “[t]he Plaintiff’s expert proposes that consumers will only replace single-function instant messaging software with integrated-function instant messaging software, rather than the opposite. Such a proposition only considers the factors of functional differences, but does not fully consider the status quo that most Internet services are free of charge. So the Court does not adopt this proposition.” See the Appendix for an English-language transition of a portion of the decision. See also the original Chinese version of the Court decision, *supra* note 2.

<sup>15</sup> See the Appendix for an English-language transition of a portion of the decision. See also the original Chinese version of the Court decision, *supra* note 2.

dominance if one only considers a relatively short period of disputes between the two parties that occurred in 2010.

Qihoo 360's expert, in particular, had ignored the fact that the use of micro-blogging and social network was rapidly increasing. The Court concluded that micro-blogging and social networking services belonged in the relevant market.

The Court then examined an argument presented by Tencent that the relevant product market for evaluating Qihoo 360's claims consisted of "Internet application platforms." The Court concluded that the dominant form of competition in the Chinese internet industry involved platforms competing for the attention of users and then selling that attention to advertisers:<sup>16</sup>

The Court finds that, firstly, the Internet application platform as a business model is becoming more and more common. Consequently, users, traffic, and usage time become the main focus of competition on the Internet.... Obviously, [a number of Chinese Internet companies] provide free services to attract a large number of users and then take advantage of the huge user resources in the operation of value-added services and advertising to make profit. In turn, they use the profit generated from value-added services and advertising to support the survival and development of their free services. This has become the typical business model in the Internet industry. In this business model, the real competition among service providers is about the number of users, page views and effective usage time. The reason is that more users generate greater traffic and more effective usage time, which lead to higher profits from advertising and value-added services. Vice-versa, those companies can survive and grow their business only by providing an integrated platform to attract more users and increase their effective usage time. Secondly, there is evidence in this case showing that the competition among platforms is not the future development trend, but the current status of competition among Internet companies.... Therefore, the Internet industry is currently at the stage that different varieties of free products or services offered by platforms are merely different approaches to attract users and build up the platform.

The Court also found that this "attention rivalry" was helpful for understanding the nature of competition between Qihoo 360 and Tencent:

The competition among Internet companies is essentially the competition of valued-added services and advertising businesses offered on their platforms. This is also the reason why the "3Q war" happened between the plaintiff and the defendant, although they provide different products, i.e. security and anti-virus products and instant messaging, respectively.

The Court noted the importance of dynamic competition and the ease of entry and concluded that supply substitution therefore needed to be considered:

[T]he Internet industry is a dynamic market and it is very easy for other companies to imitate those products, services and business models which have been successful in this industry. The market entry barriers are very low. Thus, in addition to using demand substitution in the definition of the relevant market, the factor of supply substitution should also be considered and we should include the potential capacity of other companies in the relevant market.

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<sup>16</sup> See Evans, *op. cit.* for a detailed discussion of attention rivalry among platforms.

While the Guangdong High Court did not conclude that application platforms was the relevant product market it relied on the competitive constraints coming from attention rivalry, among the other factors discussed above, to reject the integrated IM product market put forward by Qihoo 360 and its economic expert.<sup>17</sup>

## V. MARKET POWER

Having rejected Qihoo 360's claim that the relevant product market consisted of integrated IM in China, the Guangdong High Court also found that the fact that Tencent had a 76.2 percent share of the overall instant messaging segment could not prove it had monopoly power. The Court went on, however, to consider whether Tencent could have significant market power even under the assumption that the relevant product market consisted of integrated IM services in China. Importantly, it rejected the notion that market share data was sufficient to establish market power in this instance.

The Court articulated four reasons:

1. Tencent does not have the ability to control prices in that narrow market and consumers can easily switch among integrated instant messaging products.
2. The barriers to entry and expansion in the integrated IM segment are low and there was no persuasive evidence of "customer stickiness" from network effects.
3. The instant messaging segment is highly dynamic: "Instant messaging market is in a highly competitive and highly unstable state, with new technologies, new business models emerging continuously."<sup>18</sup>
4. There are a number of potential competitors with very strong financial and technical capabilities.

The Court concluded, "due to the special market conditions of the Internet industry, market share in particular cannot be deemed as a decisive factor in the determination of a dominant market position."<sup>19</sup>

## VI. FINAL DECISION

The Guangdong Court dismissed Qihoo 360's bundling and exclusionary abuse claims since Qihoo 360 had not succeeded in identifying a relevant antitrust market in which Tencent was in a dominant position. However, the Court's analysis of the tying claim is worth noting.<sup>20</sup> It found that combining the installation of IM and security software helped users by increasing the performance of their computers and therefore was an economically rational decision for Tencent

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<sup>17</sup>The Court also rejected Qihoo 360's claim that the relevant geographic market was China.

<sup>18</sup>See the Appendix for an English-language translation of a portion of the decision. See also the original Chinese version of the Court decision, *supra* note 2.

<sup>19</sup>See the Appendix for an English-language translation of a portion of the decision. See also the original Chinese version of the Court decision, *supra* note 2.

<sup>20</sup>The Court's analysis of the exclusionary practice claim mainly focused on a counterclaim by Tencent that the Court rejected. See the Appendix for an English-language translation of a portion of the decision. See also the original Chinese version of the Court decision, *supra* note 2.



to make. It also found that Qihoo 360 had not shown any evidence that Tencent's alleged tying has excluded competition from the market.

## VII. CONCLUSION

The Guangdong High Court's decision in *Qihoo 360 v. Tencent* is a landmark in several respects.

First, it provides the most detailed antitrust analysis thus far concerning the proper approach to market definition generally and in abuse of dominance cases in particular in Chinese courts. The only other major decision that comes close is Beijing First Intermediate Court's decision in *Tangshan Renren v. Baidu*.<sup>21</sup>

Second, it demonstrates that the Chinese courts, barely five years after the AML went into effect, are already adept at rendering relatively sophisticated antitrust opinions, applying modern economic concepts. Of course, it is just one case and just one court, but it bodes well for the ability of Chinese courts to engage in rigorous antitrust analysis.

Third, it suggests that economic analysis, and economists, will play a significant role in private antitrust litigation in China as they have in U.S. private antitrust litigation and in cases brought by the European Commission. Qihoo 360 and Tencent both retained economists and introduced economic evidence before the Court.

Fourth, it is one of the world's leading and most sophisticated antitrust decisions concerning competition in internet-based industries. Although some commentators will certainly disagree with specifics of the analysis, and there are certainly areas in which more sophisticated antitrust analysis could be done, the Court provided a relatively nuanced analysis of multi-sided platform competition, rivalry in attention markets, the application of the SSNIP test to products that are offered free of charge, and the role of dynamic competition.

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<sup>21</sup> Beijing No. 1 Intermediate People's Court, *Tangshan Renren Information Service Co. Ltd. v Baidu Network Information Science and Technology Co. Ltd*, Civil Case No. Yizhongminchuzi 845/2009. The transcript of the case (in Chinese) is available at [http://www.chinacourt.org/zhibo/zhibo.php?zhibo\\_id=1865](http://www.chinacourt.org/zhibo/zhibo.php?zhibo_id=1865). See also press release <http://www.chinacourt.org/html/article/200912/18/386685.shtml>.

## Appendix: Translation of the Court Decision<sup>22</sup>

*Unofficial Translation for Discussion Purpose Only © 2013 by Global Economics Group, LLC*

The Court finds that, based on the pleadings of the plaintiff and the defendant, the focuses of the dispute in this case are: how to define the relevant market; whether the defendant has a dominant position in the relevant market; whether the defendant has abused a dominant position in order to exclude and restrict competition; and to what degree the defendant should be held responsible for civil liability.

### I. REGARDING THE ISSUE OF HOW TO DEFINE THE RELEVANT MARKET

Article 2 of the "Guidelines of the Anti-Monopoly Commission of the State Council on the Definition of Relevant Market" (hereinafter referred to as the "Guidelines") provides that any competitive behavior (including any behavior that has resulted or may result in eliminating or restricting competition) occurs within a particular market scope. The relevant market defines the market scope within which business operators compete against one another. Defining the relevant market in a scientific and reasonable manner plays an important role in key issues such as recognizing competitors and potential competitors, determining the market share of business operators and the degree of market concentration, deciding the market position of business operators, analyzing the impact of business operators' behavior on market competition, judging whether business operators' behavior is illegal, and determining business operators' legal liabilities should they be responsible for any illegal behavior. In the present case, the plaintiff accused the defendant of taking advantage of QQ software and services to restrict competition and promote the bundling of sales, which constitutes an abuse of a dominant position. To determine whether the defendant has a dominant market position, the premise is established from a precise definition of the relevant market of QQ software and services. Article 12 of the PRC Anti-monopoly Law provides that "relevant market" refers to the product scope or territorial scope within which the business operators compete against one another during a certain period of time for specific products or services (hereinafter collectively referred to as "products"). Article 3 of the Guidelines provides that in the practice of anti-monopoly law enforcement, it is usually required to define relevant product market and relevant geographic market. A relevant product market is a market composed of a group or a category of products which are substitutes based on factors such as characteristics, uses and prices of the products, and which mainly refer to products treated by consumers as close substitutes. These products are in comparatively tight competition, and may be treated as a product market where business operators are competing with one another. The relevant geographic market is a geographic area within which consumers can acquire products that have relatively strong substitution relationships. Such geographic areas illustrate a relatively intense competition relationship; therefore it may be treated as the geographic scope within which business operators' products compete with one another.

#### A. The Relevant Product Market

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<sup>22</sup> An unofficial translation of the analytical portion of the Court decision, the Guangdong Province High People's Court's Civil Judgment No. Yuegaofaminsanchuzi 2/2011. The Chinese version is *available at* <http://www.gdcourts.gov.cn/gdcourt/front/front!content.action?lmdm=LM43&gjid=20130328040159946185>.

## 1. The method adopted for defining the relevant product market in this case

Article 4 of the Guidelines provides that the scope of the relevant market is mainly determined according to the substitution degree of the products (or geographic areas). Those products that have a relatively strong substitution relationship, or those geographic areas in which such products can be provided in the market from the perspective of consumers, constitute the most direct and effective competition constraint on the business operators' behaviors in market competition. Therefore, demand substitution analysis from the consumers' perspective shall be conducted in the relevant market definition. Where supply substitution has similar competition constraint on business operators' behaviors as demand substitution, supply substitution shall be considered in the relevant market definition. Article 5 provides that demand substitution is to determine the degree of substitution among different products from the perspective of consumers according to the products' functions and uses, quality, price acceptance and their availability to the consumer. In principle, from the perspective of consumers, the greater the degree of substitution among products, the fiercer is the competition, and the more likely that the products fall into the same relevant market. Article 10 provides that the hypothetical monopolist test may help resolve the uncertainty that may arise from the relevant market definition. It supposes a profit maximizing business operator (hypothetical monopolist) and the issue to be analyzed is whether the hypothetical monopolist is able bring about a non-transitory (normally one year) increase in the price of the target product on a small scale (normally 5 to 10 per cent) provided that the sales conditions of other products remain the same. If the price increase provokes consumers to switch to close substitute products, rendering the price increase unprofitable, then the substitute products shall be added to the relevant product market and form together with the target product a product group. Then analysis shall be conducted on whether the price increase of the product group would be profitable for the hypothetical monopolist. If the result is affirmative, the new product group constitutes the relevant product market, otherwise the aforesaid analysis process shall continue. The expansion of the product group causes the products inside and outside the group to become increasingly less substitutable. Eventually, a particular product group is formed, in which the hypothetical monopolist can make profit through a price increase. Hence, a relevant product market is defined.

In accordance with the above provisions, the Court determines that the process of defining of a relevant product market in this case may adopt the following methods: to determine the degree of substitutability among different products from the perspective of consumers based on factors such as the functions and uses of the QQ software and its services that consumers require, as well as quality, price acceptance and availability; meanwhile, the impact of supply substitution should also be taken into consideration.

Regarding whether the analytical method of the hypothetical monopolist test may be adopted, the plaintiffs' expert RBB issued an "Economic Analysis Report on the Anti-monopoly Disputes between Qihoo 360 and Tencent". The report states that all instant messaging product suppliers have decided to set the prices of basic services at zero while also trying to monetize the relationship between the users and the product suppliers; the "hidden" price that users pay may take the form of advertising which pays for the "free" instant messaging products. Whether free instant messaging products can constitute a relevant market depends on whether a hypothetical

monopolist which holds all instant messaging products may make profit by lowering product quality or by non-temporarily increasing the "hidden" price of the product on a small scale. The focus of competition among instant messaging products is not price. Thus, the quantitative hypothetical monopolist test is not an effective method to define the relevant product market in this case. Due to the fact that there is a lack of perfect data, it is recommended that a qualitative analysis of the demand substitution between instant messaging products and other communication products should be conducted to assess whether such substitution is sufficient to prevent a hypothetical monopolist from unilaterally reducing the quality of instant messaging products. The Court believes that this case reflects one of the main characteristics of the products and services provided by Internet service providers, i.e., almost all of the suppliers set the price of their basic services at zero. It is true that "free" has become a common, fundamental and viable mode of service for instant messaging services and antivirus security software provided by the defendant and the plaintiff, respectively, as well as for other services such as search engines, microblogging, e-mail, social networking services, news, video and music, etc. The evidence in this case shows that users of instant messaging products and services are highly sensitive to prices. According to the survey of CNNIC, up to 60.6% of users do not want to pay for instant messaging services and 32.7% of users who are willing to pay would only pay for the value-added services on the instant messaging platform, rather than paying for the basic service of instant messaging. A survey of the website eNet shows that if the defendant charges all QQ users it will lead to a loss of 81.71% of its users who will switch to other free instant messaging products and services. In the Microsoft/Skype merger case, evidence shows that if Skype starts to charge users for its service more than 75% of the individual consumers will no longer use the product. Based on this, the European Commission deems that the success of service providers depends to a large extent on the free provision of services. The European Commission believes that if a service provider starts to charge a fee for a service that has been free for a long time and if there are alternative free services on the market then consumers will immediately start using those free alternative services. When consumers determine the quantity of certain types of instant messaging products, they will take into account the opportunity costs of acquiring such services. However, once suppliers start to charge for such services, consumers' first choice will be to use other free products, even if the opportunity cost of using those free products is higher than that of using the paid products. In other words, compared with the opportunity cost of spending time viewing advertisements, "free of charge" plays a more important role in defining the relevant market. Therefore, when assessing whether the instant messaging products can constitute a relevant market, one should take into account whether a hypothetical monopolist controlling all instant messaging products may make profit by lowering product quality or non-temporarily increasing the "hidden" price of the product on a small scale. However, a more important factor to consider is whether a lot of demand substitution will be generated if a hypothetical monopolist charges the service on a small scale continuously. Accordingly, despite the fact that there is an absence of perfect data, it is still appropriate to consider if the defendant continuously (assuming one year) raises the price from zero to a modest charge and whether there is evidence to support that consumers will switch to other close substitutes in order to determine whether those products should be included in the same relevant product market.

## **2. Regarding the three types of instant messaging software belonging to the same relevant product market agreed upon by both parties**

QQ software is an integrated instant-messaging software, with key features such as text transmission, voice chat, video chat, SMS to mobile phones and offline transfer of files, and asynchronous and offline (non-real-time) communication features, which means that users can receive messages and files of the logged-on users without logging on QQ. Besides the communications services mentioned above, the QQ software also integrates other Internet service functions. The plaintiff's complaint identifies that according to the 2009 "Research Report on Instant Messaging Users in China" by CNNIC, instant messaging software and services can be subdivided into three categories: integrated instant messaging services such as Tencent QQ and Microsoft's MSN; (2) cross-platform instant messaging services, such as Fetion of China Mobile; and cross-network instant messaging services, such as the Skype software services of Tom Group Limited. These three types of products are closely related with each other and can substitute each other in terms of technology and service. The defendant does not object that claim of the plaintiff and the Court confirms that those three types of instant messaging products and services are part of the product group in the same relevant product market.

### **3. Regarding the substitutability between integrated instant messaging and text, audio and video instant messaging**

In this case, text instant messaging refers to a type of real-time SMS service, usually with the function of detecting the status of other users. Audio instant messaging refers to network voice services transmitted in whole or in part over Internet Protocol networks. Video instant messaging refers to the communication services that allow users to interact with two-way synchronous video and voice transmission from at least two or more places. The "Economic Analysis Report on the Anti-monopoly Disputes between Qihoo 360 and Tencent" by the RBB company suggests that the only difference among the three types of services is the medium of communication, but the common features are online status notice, communication among small groups of users, and real-time and cross-platform interaction. All three services are often available through a single, integrated front-end device. Therefore, it is difficult for products lacking of any of the aforementioned three functions to be considered by most consumers as a good substitute. The three types of products may constitute a separate, overlapping relevant market, and such a market might be a market outside the integrated instant messaging products market because consumers will only replace single-function instant messaging software with integrated-function instant messaging software, rather than the other way around.

The Court finds that, when taking demand substitution into account, consumers can easily and immediately switch among the three services of text, audio and video instant messaging at no cost; from the perspective of supply substitution, most of the service providers are able to provide services of the three functions simultaneously. Therefore, text instant messaging, audio and video messaging should not be distinguished based on the functions, nor be considered as separate communication services. However, they should be considered as part of a broader market; any type of these services does not constitute a separate market, and it is very difficult to divide the instant messaging market into smaller and functionally non-overlapping markets. At the same time, there is evidence in this case showing that consumers are highly sensitive to the price of instant messaging products and services and that they are unwilling to pay any fee for the use of basic services of instant messaging products. If the defendant continuously (assuming one year) raises the price from zero to a modest charge, the

Court has reason to believe that consumers may choose instead any kind of service among free text instant messaging, audio or video messaging, so that the defendant makes no profit by doing so. The Plaintiff's expert proposes that consumers will only replace single-function instant messaging software with integrated-function instant messaging software, rather than the opposite. Such a proposition only considers the factors of functional differences, but does not fully consider the status quo that most Internet services are free of charge. So the Court does not adopt this proposition. There is close substitutability between integrated instant messaging and single medium instant messaging as text, audio and video instant messaging. Thus, they belong to product groups of the same relevant product market.

#### **4. Regarding substitutability between QQ and social networking sites, microblogging service**

(1) Regarding functions and purposes, products such as microblog and social networking web sites all provide web-based instant messaging services and separate instant messaging software services. The plaintiff's expert thinks that there is strong competition and demand substitution between web-based instant messaging services and separate instant messaging products provided by microblog and SNS social networking web sites and QQ. Thus, they belong to the same relevant product market to which the defendant has no objection, and the Court adopts this proposition.

(2) When microblog and SNS social networking web sites provide web-based instant messaging products and services, i.e., taking IM products as part of its core products, the issue of whether there is substitutability between QQ and microblog, SNS services is controversial in this case. The plaintiff's expert thinks that the key difference between instant messaging products and social networking websites is that the latter focuses on communication between groups comprised of a large number of users, with fewer requirements for real-time functions, and that the former focuses on real-time communication among a relatively small group of users. Based on the data of weekly effective usage time during the entire period from the first week of 2009 to the last week of 2011, the correlation coefficient of the weekly effective usage time of the two products was 0.098, close to zero. The correlation coefficient of monthly effective usage time is even lower, -0.0248. So the way that social networking software is used in China is different from that of instant messaging software and social networking software may not be an effective substitute. Firstly, the Court finds that there is a lack of data on microblogs in the data used by RBB in making the above conclusions and there is evidence showing that this period of time saw the rise and rapid development of microblogs provided by Sina, Tencent and Sohu. There are reasonable grounds to believe that the rapidly expanding market share of microblogs would exert a great impact on the weekly or monthly effective usage time of social networking web sites, which would ultimately affect the correlation analysis of the social networking web sites and instant messaging products. Secondly, regarding functions and purposes, when one considers instant messaging products as part of microblogs' core products, both microblogs and QQ instant messaging products have the function of instant transmission of information and the diversity of information carrier. Both can offer the function of point-to-point private instant messaging among a small number of groups. Both the micro-groups of microblogs and QQ groups can conduct real-time interaction between two or more people. Instant messaging tool services of social networking websites are used to support its social functions, and both SNS and

QQ have social networking attributes. The network of relationships of both SNS and QQ are important means with which to retain users and there is also close substitutability between the two services. In its analysis of the "substitute threats" to instant messaging software, CNNIC points out that after social networking websites, such as renren.com and kaixin001.com, have integrated instant messaging services and similar video sites, and financial websites have integrated instant messaging services, these products all constitute substitute threats to instant messaging software. Analysys International believes that the microblog of some users has replaced QQ. Zhou Hongyi, CEO of the Plaintiff, thinks that Sina microblog will undermine Tencent. In the case of Microsoft/Skype, the filing party thinks that text, audio and video usually cannot be divided into separate services, but are increasingly viewed as appendages of other activities such as social networking behaviors. The European Commission believes that there is growing consumer demand for a user experience of integrating a range of communication functions. Social networking websites and similar social ecosystems such as Facebook and Google+ explain this trend of providing a broader range of communication services to consumers. Thirdly, taking the price factor into account, there is reason to believe that if the defendant continuously (assuming one year) raises the price from free of charge to a modest charge, it is very likely that consumers will instead choose microblog and SNS social networking services, making the defendant's action of charging fees unprofitable. Fourthly, the plaintiff's expert finds that it is sufficient to define the appropriate relevant market including instant messaging products at the time of the occurrence of "3Q war", which took place in late 2010. However, at that time, there were major distinctions between instant messaging and social networking and microblogs and they did not belong to the same relevant antitrust market. The Court finds that competition is a dynamic process, and when defining a relevant market in an antitrust lawsuit regarding the abuse of a dominant market position, we must consider the status quo and future trends and development of relevant industries. Generally speaking, those acts of abuse of market dominance which are likely to continue for some time should be stopped in order to effectively maintain the market competition mechanism. Strong network technology innovation capabilities and rapid changes of business models are significant features of the Internet industry. Since 2010, microblogs and social networking sites have demonstrated a high degree of integration with instant messaging in a relatively short period. Therefore, when identifying the relevant market it will not lead to a scientific, rational and effective suppression of abuse of dominance if one only considers a relatively short period of disputes between the two parties that occurred in 2010. The Court does not accept testimony of the plaintiff's expert. In summary, QQ, social networking websites and microblogging services belong to product groups of the same relevant market.

## **5. Regarding the substitutability between traditional telephone, fax and instant messaging products and services**

The defendant suggests that there is a relatively high degree of substitutability between instant messaging services and traditional means of communication, such as telephone and fax. Thus they should be included in product groups of the same relevant market. The plaintiff believes that instant messaging is a completely Internet-based service and is significantly different from traditional non-network services, and thus they do not belong to the same relevant product market. The Court finds that QQ products and services is essentially still a communication service and there is some competition between QQ and traditional

communications services such as telephone, cell phone, and text messages. However, compared with traditional communications services such as telephone, cell phone, and text messages, QQ is technically quite different. What's more, landline, mobile phone and SMS are all fee-based services, while instant messaging is a free service. So there is no close substitutability between QQ and such traditional means of communication as SMS, mobile communication and landline, and there is no substitution relationship between them.

#### **6. Regarding whether QQ software and e-mail belong to product groups of the same relevant product market**

The defendant believes that there are strong competitive and substitution relationships between e-mail products and instant messaging services. The Court finds that although the core function of e-mail products is network communication, they also have text, images, audio, and video file transfer capabilities, which are not instant communication products. Although most of the E-mail service providers have developed instant messaging functions, such as chat with friends and embedded such functions in the e-mail interface, there is still a huge difference between such functions and instant messaging software in terms of voice communications, video communications, plug-in games, screenshots and the convenience of operation of the tools. A friends-chat feature is only a supplement to the communication function of e-mail, and its actual usage is not frequent. It is generally difficult for users to switch directly between those two services and there is only a weak relationship of substitution between e-mail and such instant messaging products as QQ. Because of the sharp differences in functions and purposes, even if QQ started to charge small fees for a long period, it would be difficult for consumers to choose to use e-mail. Therefore, e-mail and QQ do not belong to the same relevant product market.

#### **7. Regarding whether to define the relevant market as Internet application platforms**

The defendant's experts propose that QQ software is an integrated platform product, which provides value-added services and advertising services in addition to instant messaging services. Operators of Internet application platforms include the plaintiff (Internet safety platform), the defendant (instant messaging platform), and other Internet companies in the industry, such as Baidu (search platform), Sina (news portal platform and microblogging platform). So the relevant market in this case is much larger than the market for instant messaging software and services. The Court finds that, firstly, the Internet application platform as a business model is becoming more and more common. Consequently, users, traffic, and usage time become the main focus of competition on the Internet. QQ has the functions of an integrated services platform, providing services such as advertising, information, dating, and microblogging in addition to the instant messaging service. All those services can be integrated and cross-used. MSN is a platform that integrates a series of Internet application services, such as instant messaging features, Bing search, translation, E-mail, online shopping, and games. Aliwangwang and Fetion also integrate various Internet applications, including instant messaging. The survey of CNNIC shows that more than 50.2% of users will log on to use other services through the instant messaging service software. Similarly, after having a large number of users through the core product, microblog, Sina Microblog starts to provide various applications such as instant messaging, advertising, games, micro-music, and microdata on the platform of microblogs. 360 Browser also provides translation, games, e-mail, and many other services to its



browser users. In addition to providing social networking services, Renren.com also provides instant messaging, advertising and other services. Obviously, all those companies provide free services to attract a large number of users and then take advantage of the huge user resources in the operation of value-added services and advertising to make profit. In turn, they use the profit generated from value-added services and advertising to support the survival and development of their free services. This has become the typical business model in the Internet industry. In this business model, the real competition among service providers is about the number of users, page views and effective usage time. The reason is that more users generate greater traffic and more effective usage time, which lead to higher profits from advertising and value-added services. Vice-versa, those companies can survive and grow their business only by providing an integrated platform to attract more users and increase their effective usage time. Secondly, there is evidence in this case showing that the competition among platforms is not the future development trend, but the current status of competition among Internet companies. For instance, the competition between global search engine service provider Google and global social networking site Facebook in the online advertising market in the United States proves that different service platforms compete directly with one another. The plaintiff also claims in its Prospectus that its biggest competitor is Tencent and that these two companies take advantage of their respective platforms to compete in value-added services and online advertising. Zhou Hongyi, the CEO of the Plaintiff thinks that an "Internet platform can take the form of instant messaging, search engine, or security (software)." Therefore, the Internet industry is currently at the stage that different varieties of free products or services offered by platforms are merely different approaches to attract users and build up the platform. The competition among Internet companies is essentially the competition of valued-added services and advertising businesses offered on their platforms. This is also the reason why the "3Q war" happened between the plaintiff and the defendant, although they provide different products, i.e. security and anti-virus products and instant messaging, respectively. In this case, although we still cannot determine whether there is close substitution between the security-software platform and the instant-messaging platform, status of products competition and market structure of the Internet industry should be taken into account in defining the relevant product market. Thirdly, the Internet industry is a dynamic market and it is very easy for other companies to imitate those products, services and business models which have been successful in this industry. The market entry barriers are very low. Thus, in addition to using demand substitution in the definition of the relevant market, the factor of supply substitution should also be considered and we should include the potential capacity of other companies in the relevant market.

Based on the analysis of the claims both parties have made, the Court finds that the plaintiff's claim that integrated instant messaging products and services constitute a separate relevant product market is unfounded and the Court does not support it.

### ***B. The Definition of the Relevant Geographic Market***

The plaintiff claims that the relevant geographic market in this case is the instant messaging software and services market in mainland China. The defendant claims that the relevant geographic market in this case should be the global market. The Court finds that, firstly, the operators and users of instant messaging services are not limited to those based in mainland China. Due to the openness and interoperability of the Internet, operators and users are not

confined by national borders. There is evidence in this case showing that operators overseas can provide instant messaging services to users in mainland China. The defendant also provides services to users around the world. There are a certain amount of Chinese-language users in Hong Kong, Macao, Taiwan, and other regions of the world that make use of the instant messaging products provided by the defendant; there are also foreign-language users around the world making use of the foreign-language version instant messaging services provided by the defendant. Secondly, the user's language preferences and product usage habits cannot be used as the sole basis in the definition of geographic market. As mentioned earlier, operators usually provide multiple language versions of instant messaging software to meet the needs of users who speak different languages. Users in mainland China often choose instant messaging services provided by operators overseas (such as MSN, ICQ, Yahoo Messenger, Skype, etc.), illustrating that the user's language preference does not lead to the situation that instant messaging services operators abroad cannot compete with operators in mainland China. As for product usage habits, an iResearch report mentions that TOM-Skype offers a global search directory through which users can search for known or unknown friends with different search options and they can immediately engage in unimpeded voice chat. In the Microsoft/Skype case, the European Commission believes that due to the fact that worldwide users share the same habit in their acceptance of instant messaging services, there is no geographical limitations of the products and services of the operators resulting from differences in the usage habits. Thirdly, in terms of providing and accessing instant messaging services on a global scale, there are no additional transportation costs, price costs, or other costs for market participants of instant messaging products and services. At present, there are no legal or technical standards that limit the provision and use of these services worldwide. In summary, the Court finds that the relevant geographic market in this case is the global market.

## **II. ON THE ISSUE OF WHETHER THE DEFENDANT HAS A DOMINANT POSITION IN THE RELEVANT MARKET**

The second paragraph of Article 17 of the Anti-monopoly Law states that a dominant market position refers to the business operator(s)'s ability to control a product's price, quantity or other trading conditions in the relevant market, or to hinder or affect other business operators' entry into the relevant market. Article 18 provides that the following factors should be taken into consideration when determining whether a business operator has a dominant market position: the business operator's market share in the relevant market and the competition situation of the relevant market; the business operator's ability to control the sales markets or the raw material procurement markets; the financial and technical conditions of the business operator; the degree to which other business operators rely on the business operator in their transaction; the degree of difficulty for other business operators to enter the relevant market; and other factors relevant to the determination of the dominant market position of the said business operator. That's to say, in the determination of the business operator's dominant position, various factors, including market share, the competition situation of the market, and the degree of difficulty of market entry. Article 19 makes the rules of presumption of a dominant market position, i.e. if the market share of one operator in the relevant market accounts for 50 percent or more, such an operator can be presumed to have a dominant market position, but the rules allow operators to provide evidence to overturn the presumption.

As mentioned earlier, the plaintiff's definition of the relevant product market and the relevant geographic market in this case is too narrow. Thus, the market share of the defendant calculated by the plaintiff based on the plaintiff's definition of the relevant product market and geographic market is not objective, and cannot truly reflect the defendant's market share and position in the relevant markets. In particular, the product scope defined by the iResearch report, the most important evidence submitted by the plaintiff, is different from that defined by the Court in the following aspects: (1) iResearch's monitoring of instant messaging software only targets the PC end products and does not include instant messaging software on mobile phones and tablet PCs; (2) microblogging and SNS social networking sites with instant messaging products as part of their core products are not included in the product group of the relevant market; web-based instant messaging products provided by microblogging and SNS social networking sites, which the plaintiff itself claims belong to the instant messaging relevant market scope, are not included either; (3) the scope of the iResearch and CNNIC studies is limited to mainland China and does not include Hong Kong, Macao and Taiwan regions and other parts of the world that use QQ products, and so on. Therefore, the iResearch's finding that Tencent's market share of the overall instant messaging market in China in 2010 accounted for 76.2% is not a true reflection of Tencent QQ's market share in the relevant market in this case. In summary, the Court does not recognize the claim by the plaintiff that the defendant has a monopoly position in the relevant market, which is presumed upon market share calculated on an untrue basis.

To say the least, even in the narrowest relevant market proposed by the plaintiff, i.e., integrated instant messaging products and services in mainland China, it is not sufficient to presume that the defendant has a dominant market position just on the basis that the defendant's market share is more than 50% of the relevant market. The reasons are as follows:

#### ***A. The Defendant Does Not Have the Ability to Control the Price, Quantity of Goods or Other Trading Conditions***

Firstly, the defendant does not have the ability to control the prices of goods. As mentioned earlier, almost all instant messaging software and services are offered to users for free and users are not willing to pay any fees for the basic services of instant messaging software. So the defendant cannot take advantage of its leading market position and get pricing rights over other competitors. As for the plaintiffs' expert's claim that the hypothetical monopolist of free instant messaging products might generate profits by lowering the quality of products or non-temporarily raising the hidden price of the products on a small scale, the Court will address the issue in the part below about the state of market competition. Secondly, the defendant does not have the ability to control the quantity of goods or other trading conditions. There are various types of instant messaging software on the Internet and users have many choices. According to a CNNIC survey, the ratio of users who use more than two kinds of instant messaging software within six months is as high as 63.4%; another 8.7% of users of instant messaging services have changed their tools for chat within six months and many users who have changed their tools turn to emerging instant messaging software. There is a high degree of substitutability among instant messaging products. Once one instant messaging software malfunctions, users can immediately replace it with another instant messaging software. There is no evidence showing that the defendant dares to easily refuse to provide products and services to users or to change the terms

of trade. Thirdly, regarding the degree to which other business operators rely on the defendant, the counterparty can easily choose to deal with other corporations and is thus less dependent on the defendant. The plaintiff's proof concerning commercial disputes between the defendant and LineKong and UCWeb Inc. is the unilateral declaration of LineKong and UCWeb Inc. The available evidence is insufficient to prove that the defendant has strong control over the counterparty in the transactions.

### ***B. The Defendant Does Not Have the Ability to Impede or Affect Other Operators' Entry Into the Relevant Market***

#### **1. This market's entry barrier is low and the hindrance to expansion is small**

Firstly, the barrier for operators to enter the instant messaging market is low. Instant messaging services do not need heavy investment or complex technology. Internet service providers, terminal manufacturers, software companies and the three major operators are generally optimistic about the market and there are large numbers of operators entering this market every year. For instance, in mainland China in 2011, many instant messaging products, such as Shanda Youni, Apple iMessage, China Unicom "Wo You", "Kouxin" launched by the plaintiff, China Mobile "Feiliao", China Telecom, Corpease IMO, Tudu Talk2.0Beta and "NetEase Messenger" entered the market. Secondly, the means of entry into the market are diversified. For instance, NetEase and Kaixin Network entered the market through the integration of instant messaging services in mailbox services and social networking sites services; meanwhile, Renren.com and Sina microblog have quickly developed their own client software products for instant messaging. A CNNIC survey shows that with the number of users of other internet services growing, some emerging instant messaging tools relying on other Internet services have developed rapidly. Thirdly, newcomers to the market have a strong ability to expand and a lot of success stories prove that the resistance to market expansion is weak. For instance, various kinds of instant messaging software such as Fetion launched by China Mobile in 2006, Aliwangwang launched by Alibaba in 2007, Baidu Hi launched by Baidu Inc in 2008, YY Voice launched by Duowan.com in 2008, have quickly obtained a certain share of the market by segmenting their respective users not long after their respective entries into the market.

#### **2. Regarding "customer stickiness," i.e. network effect**

The plaintiff has repeatedly emphasized that there is an obvious network effect in the instant messaging industry, i.e., for one user, the value of an instant messaging product depends on the number of other users of such products. In other words, the more users who use a certain instant communication product, the more attractive it is to other users. Meanwhile, in the instant messaging industry, there is a user lock-in effect. That is, during the long-term use of QQ, users have formed a chain of friends on QQ and established their social circles on QQ. If they switch to other instant messaging products, the cost of rebuilding a social circle will be high. Meanwhile, switching to other instant messaging products also requires the user to get familiar with features and characteristics of the new product and to change usage habits. Due to the existence of network effect and user lock-in effect, it is generally difficult for other operators to enter this market, and difficult to survive after entry. The Court finds that, firstly, because most users connect with friends and family, i.e. the "core circle," through instant messaging services, the role of the network effect is greatly reduced. According to data from Facebook, users usually maintain two-way interactions only with four to six people. So these users can easily change among instant

messaging services. Secondly, in the Microsoft/Skype case, the European Commission found that a lot of users freely switch their access among a number of consumer communications service providers. The circumstances of the QQ software in this case are similar. The CNNIC report points out that "around the year of 2007, along with the development of a number of the emerging instant messaging tools, the ratio of users who use two to three different instant messaging software simultaneously increased gradually, already more than 50%"; The report also predicts that "in the future, users who use a variety of instant messaging tools simultaneously will increase further." The QQ software is not a "must have" product to users since there are a variety of alternatives to meet users' needs for instant messaging. The defendant is unable to control the user's choice of instant messaging software. Meanwhile, users can build social networks with a high degree of overlapping with several kinds of instant messaging software at the same time, so they can minimize the impact of the user lock-in effect, i.e. "customer stickiness," when switching between different instant messaging software. Thirdly, when the defendant started the development and operation of the QQ products, MSN was the leading instant messaging service provider with the largest share of the Chinese market. However, thanks to its unique products and quality service, the defendant has quickly expanded the scale of operation to attract more users and has ultimately achieved a larger market share than that of MSN in a relatively short period of time. Therefore, the network effect and the user lock-in effect are not insurmountable barriers for instant messaging products and services.

### **3. Sufficient competition in the relevant market**

Instant messaging market is in a highly competitive and highly unstable state, with new technologies, new business models emerging continuously. There is no evidence suggesting that one enterprise may control the market for a long period of time. Even in the absence of external forces, this market can also easily achieve full competition and self-renewal. Firstly, the evidence of this case shows that there is fierce competition among traditional instant messaging software products. In recent years, the number of users of such products as Fetion, Aliwangwang, and YY Voice has increased sharply, each with more than 100 million users. Secondly, with integration of instant messaging services in emerging SNS, microblogging, e-mail, and other products, competition in the relevant market is further intensified. Emerging instant messaging products have brought tremendous competition pressure and market impact on traditional instant messaging products. Survey results of iResearch show that in recent years emerging microblogging and social services have been trying to replace instant messaging. With the rapid development of microblogging and social networking sites, users' dependence on instant messaging has started to decrease. The survey results of CNNIC show that many potential alternatives pose a threat to instant messaging: with the rapid development of the e-mail market, many service providers have integrated instant messaging features into the mailbox, driving the development of market consolidation. In addition, with the development of SNS sites such as kaixin001.com and renren.com, as well as the increase of user stickiness, users make more frequent use of information transfer functions of the social networking sites, which also have a certain impact on the use of instant messaging tools. Therefore, the instant messaging services market claimed by the plaintiff is a highly innovative, competitive, and dynamic market. Operators have the ability to engage in continuous innovation in order to maintain a competitive edge in this market. At the same time, in such a state of competition, the operators do not dare to lower product quality, or make a lot of advertising which will affect the level of user experience,

regardless of the feelings of consumers. Therefore, the Court finds that there does not exist many persistent instances to make profits by lowering product quality or non-temporarily raising the hidden price of products as alleged by the plaintiff's expert.

#### **4. The financial status and technical conditions of the defendant do not enable it to substantially exclude new competitors from entering the market or expanding capacity**

Firstly, the evidence in this case suggests that China Mobile, China Unicom, China Telecom, Alibaba, Baidu and other competitors entering the field of instant messaging in the wake of Tencent all have very strong financial and technical capabilities. All these large enterprises have enough strength to exert a tremendous impact on the leading position of the defendant in this field. Secondly, in the Internet field, there are a lot of venture capital funds. As long as companies have good products and users, venture capital institutions will actively enter the market and provide strong financial support to business operators. Most Internet companies rely on venture capital funds to rapidly expand their scale of operation.

In summary, due to the special market conditions of the Internet industry, market share in particular cannot be deemed as a decisive factor in the determination of a dominant market position. Even in the narrowest relevant market claimed by the plaintiff, as is mentioned in the CNNIC report, Tencent's dominant market position does not suppress or limit the scope of market development of other instant messaging products and does not constitute obstacles to the development of the market as a whole. Tencent does not have a dominant position in this market.

### **III. REGARDING WHETHER THE DEFENDANT ENGAGES IN CONDUCT OF ABUSING A DOMINANT POSITION TO EXCLUDE OR RESTRICT COMPETITION**

A party's dominant market position is the basis upon which the conduct of restricting transactions without legitimate reasons is prohibited by Article 17 of the Anti-monopoly Law. Through the above analysis of the definition of the relevant market, standards for the calculation of market share, as well as the fact that market share is not the decisive factor of a dominant position, the Court finds that the plaintiff cannot prove that the defendant has a dominant position in the relevant market in this case. Therefore, regardless of whether the relevant conduct of the defendant is consistent with the requirements of the conduct of illegally restricting transactions, such conduct cannot be identified as conduct of restricting transactions without legitimate reasons or as a tying arrangement. However, in order to correctly define what kind of market conduct of Internet companies is indicative of abuse of dominance, to maintain market order of the Internet industry, and to fully protect the market competition mechanism, the Court will analyze the essence of "forcing users to choose one of the two" in the 2010 "3Q war", as well as whether the defendant-made tying arrangements.

#### ***A. On the Essence of the Defendant's Conduct of "Incompatible Products" (Users' Choice of One From the Two)***

Article 17 of the Anti-monopoly Law provides that a business operator with market dominant position restricting trade counterparties to dealing exclusively with itself or with its designated business entities, without legitimate reason(s), is conduct of abuse of dominant position. In this case, the defendant forced users to "choose one from the two," ostensibly giving

users the option, but if the defendant is an operator with a dominant market position, the users are very likely to give up 360 and choose QQ. The defendant's purpose of adopting the measure of "choice of one from the two" is not to refuse to deal with the users, but rather to force the users to only deal with QQ and stop dealing with 360. The act of the defendant essentially still belongs to conduct of restricting transactions.

The defendant counterclaims that making the QQ software incompatible with the 360 security guards is attributable to the tort by the plaintiff. The plaintiff took advantage of 360 Privacy Protector, Koukou bodyguards and the pop-up page function of the 360 security guards to destruct and tamper with features of the QQ software and slander QQ. At the same time, the plaintiff integrated 360 Privacy Protector and 360 Koukou bodyguards into the 360 Security Guards, making use of the large number of users of 360 Security Guards to implement further infringement. In order to ensure the proper functioning of QQ, the defendant had to take technical measures of incompatibility to prevent and exclude the destruction from the plaintiff's software to defendant's own products. Thus, it is a legitimate act of self-remedy. The Court finds that, according to Articles 128 and 129 of China's General Principles of the Civil Law and Articles 30 and 31 of "Tort Liability Act," there are two types of self-remedies in the civil law: justifiable defense and the emergency actions. Justifiable defense is an act of defense employed to stop an unlawful infringement for the purpose of avoiding the said infringement in the public interest, or for defender's own or another person's right of the person, property right, thus causing harm to the unlawful infringer. Anyone who causes harm to another for exercising justifiable defense shall not be subject to tort liability. Emergency actions refer to an act that a person is compelled to commit in an emergency to avert an immediate danger to the public interest or to his own or another person's lawful rights, and that causes harm to another smaller interest. If harm occurs through emergency actions taken to avoid danger, the person who gives rise to the danger shall be subject to the liability. Justifiable defense and emergency actions shall not exceed the limits of necessity. In view of the fact identified by Beijing No.2 Intermediate People's Court [2011] No. 12237 Final Civil Judgment, the plaintiff had engaged in unfair competition against Tencent Technology (Shenzhen) Inc. & Shenzhen Tencent Computer System Inc. through 360 Privacy Protector and remarks on the Internet. Due to the unique nature of the Internet industry, violations implemented through the Internet spread broadly and quickly, and the losses are difficult to recover. So the legitimate rights and interests of the defendant were indeed at risk at that time. But even if the legitimate rights and interests of the defendant are subject to unlawful infringement and justifiable defense was needed, the direct object of self-remedy counterattack shall be the unlawful infringer, i.e. the plaintiff in this case, but not Internet users. Meanwhile, the preliminary injunction system in the intellectual property infringement litigation conferred intellectual property rights holders the right to apply to the People's Court for interim measures to timely, efficiently, and effectively stop the occurrence or continuance of unlawful infringement when its legitimate rights and interests might suffer an emergency or irreversible infringement. Given the circumstances expressly provided for by law, the defendant did not lawfully exercise its litigation rights to seek ways to stop the unlawful infringement in favor of unilaterally taking the measure of "choice of one from the two," resulting in the expansion of the "3Q war" and affecting users. Thus their conduct is not justifiable. In addition, the defendant's act of forcing users to make the "choice of one from the two" is beyond the limits of necessity. In this case, regardless of whether the plaintiff has engaged in acts of coercing users to use Koukou Bodyguards, or

whether the plaintiff has hijacked the QQ security module which led to the malfunction of QQ, the defendant has no right to force users to take actions for the security of QQ accounts. The scope of rights of the defendant is limited to making appropriate risk warnings for this matter. It is the users' own inherent right to decide whether to remove the 360 software or not and the defendant shall not make a choice for the users. Forcing users to make the "choice of one from the two" is beyond the limits of necessity.

***(B) On the Issue of Whether the Defendant has Engaged in Conduct of Selling Goods Through a Tying Arrangement Without Legitimate Reasons as is Prohibited by Item (E) of Paragraph One of Article 17 of the Anti-Monopoly Law***

According to the provisions of the Anti-Monopoly laws, a tying arrangement is the act taken by a firm in a dominant market position to force the counterparty to buy products or services unrelated to the contract from nature or trading habits. The purpose of a tying arrangement is to extend the dominant market position to the market of the tied products or to prevent potential competitors from entering the market. A tying arrangement is identified by the following criteria: the tying product and the tied product are separate products; the company making tying arrangements has a dominant market position; the company making the tying arrangement gives consumers no choice but to purchase the tied product; tying arrangement is an unreasonable arrangement, i.e. the tying arrangement is not out of the trading habits of such goods; selling the tied goods separately will not be detrimental to the performance or the value of the goods; the tying arrangement has an anti-competitive effect. In this case, the main function of the defendant's QQ software is instant messaging, which is indeed a separate software product vis-a-vis other software products, such as the QQ Doctor, the QQ PC Manager, the Security Manager, and Safety Management; but firstly, the defendant does not have a dominant position in the instant messaging market. Secondly, the defendant does not limit users' options. The defendant provides users with the option to uninstall the QQ software management and the defendant's provision of QQ software services is not preconditioned by the user having to use the QQ software management, which is not a mandatory act; in addition, when the defendant upgraded the QQ software management and QQ Doctor to QQ PC Manager, an upgrade notice was issued to the users before the upgrade. The upgrade would proceed only after the users had made such a choice. So the defendant has fulfilled the obligation of informing users and giving users the option to make a decision. Thirdly, the defendant's acts are of economic rationality. The package installation of QQ software management and the QQ software is the functional integration of products, which is conducive to better management of the QQ software by users through the use of auxiliary tools software, protecting the security of the users' QQ accounts; to the contrary, if the defendant does not offer security products together with QQ instant messaging software, such an act may be detrimental to the performance or value of the QQ software products. Fourthly, the relevant acts of the defendant do not produce the effect of eliminating or restricting competition. The plaintiff has no evidence proving that the defendant's packaged installation behavior has led to a significant drop in market share of the plaintiff's similar products; and no evidence proving that such behavior has resulted in the elimination or restriction of competition among other competitors in the same market. Fifthly, the plaintiff does not provide evidence proving that the defendant's behavior of packaged installation of QQ software management and the upgrade of QQ software management and QQ Doctors to QQ PC



Manager has caused or will cause damage to consumers. Therefore, the plaintiff's claim that the defendant has engaged in acts of tying arrangement and abuse of dominance is unfounded.

In summary, because the plaintiff's definition of the relevant product market in this case is wrong and the evidence provided by the plaintiff is insufficient to prove that the defendant has a monopoly position in the relevant product market, the plaintiff's request that the Court order the defendant to immediately stop the monopoly tort of abuse of dominance, jointly and severally compensate for the plaintiff's economic loss as well as a reasonable cost of protecting its rights, and make an apology is lacking of factual and legal basis, and therefore cannot be established, and should be dismissed. In accordance with the provisions of the first paragraph of Article 64 of the Civil Procedure Law of the People's Republic of China, it is ruled as follows:

Dismissed all the claims of the plaintiff Beijing Qihoo Technology Co., Ltd.

In this case, the acceptance fee of the court of first instance is 796,800 yuan, which shall be borne by the plaintiff Qihoo Technology Co., Ltd.

If a party refuses to accept this judgment, it can file an appeal petition with this Court within 15 days after the date on which the written judgment is served and copies of the appeal petition shall be provided according to the number of persons in the other party and appeal at the Supreme People's Court.

The Presiding Judge: Zhang Xuejun

Judge: Deng Yanhui

Acting Judge: Yue Lihao

March 20, 2013