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Combating Monopoly Agreements Under China's Anti-Monopoly Law: Recent Developments and Challenges

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I. INTRODUCTION

Five years after China's Anti-Monopoly Law ("AML") took effect, enforcement efforts of the antitrust agencies against restrictive agreements—called "monopoly agreements" in the AML—visibly picked up during 2013. This paper reviews recent developments, identifies a few key issues, and provides some suggestions for China to further improve its antitrust enforcement.

II. PROHIBITION OF MONOPOLY AGREEMENTS

The AML prohibits two types of monopoly agreements. Article 13 of the AML outlaws the following horizontal agreements: price-fixing, output or sales restrictions, market partitioning, agreements that restrict the purchase or development of new technology or new products, and joint boycotts. Article 14 of the AML prohibits types of vertical agreements, especially the setting resale prices or minimum resale prices to a third party. Both Article 13 and Article 14 contain a "catch-all" provision, which states that companies shall not reach other monopoly agreements as determined by the antitrust authorities.

Article 15 of the AML contains exemptions for those monopoly agreements that have the following purposes: R&D, improving product quality, standard-setting, environmental protection, enhancing competitiveness of small and medium-sized enterprises, among others. Crisis cartels and exporting cartels are also exempted. Companies wishing to benefit from the exemptions must prove that the agreement does not substantially restrict competition in the relevant market but enables consumers to share benefits deriving from the agreement.

Article 16 of the AML specifically provides that no trade association may organize conduct for the enterprises in its industry that is prohibited by monopoly agreement rules.

As a unique feature of China's antitrust enforcement structure, the monopoly agreements provisions in the AML are enforced by two separate agencies: The National Development and Reform Commission ("NDRC") is responsible for tackling price-related monopoly agreements, and the State Administration for Industry and Commerce ("SAIC") is responsible for non-price-related monopoly agreements.

Sanctions against monopoly agreements include a fine of 1 to 10 percent of the sales revenue in the previous year, plus confiscation of illegal gains. Where the concluded monopoly agreement has not been implemented, a fine of up to RMB 500,000 million (approximately U.S.$80,000) may be imposed. Violations by trade associations can be sanctioned with a fine not exceeding RMB 500,000, or lead to suspension of the association's registration.

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In line with international best practice, the AML also introduced a leniency program, albeit in very general terms: "If business operators report information concerning the conclusion of a monopoly agreement and provide important evidence to the anti-monopoly enforcement authority on their own initiative, they may be given a mitigated penalty or be granted immunity.

To provide more guidance, NDRC issued its *Anti-Price Monopoly Regulation* on December 29, 2010.[2] Consisting of 29 articles, this set of substantive rules specifies the scope of price monopoly activities, the specific forms of monopoly agreements that constitute price monopoly, the specific forms of abuse of dominance that amount to price monopoly, and what specific circumstances can be accepted as justification for engaging in these activities. NDRC also issued its *Regulation on the Administrative Enforcement Procedure for Anti-Price Monopoly* on the same day.[3] These procedural regulations contain 26 provisions and specify competence of NDRC and price authorities at the provincial level, the working relationship between NDRC and the provincial authorities, and the measures for conducting investigations. Both sets of rules took effect on February 1, 2011.

Similarly, SAIC issued its *Regulation on the Prohibition of Monopoly Agreement Conduct*, just two days later, on December 31, 2010.[4] This regulation contains 20 articles, and focuses on the definition and specific forms of monopoly agreements, and the conduct of trade associations that may facilitate monopoly agreements. It also details a leniency system that is designed to encourage active reporting of monopoly agreements by cartel participants—SAIC had already introduced its leniency program in 2009 in the *Regulation on the Procedure for the Handling of Cases Involving Monopoly Agreements and Abuses of a Dominant Market Position*.[5]

While there is still room for improvement, these NDRC and SAIC regulations to implement the AML provide further guidance on the law's relatively high-level provisions regarding monopoly agreements. This helps enhance transparency, and increases the efficiency of antitrust enforcement in China.

III. RECENT ENFORCEMENT EFFORTS AGAINST MONOPOLY AGREEMENTS

Prior to 2012, the number of AML cases dealt with by NDRC and SAIC was relatively small. However, the number has increased significantly in recent years. Based on publicly available information, the two enforcement agencies have completed investigations of 22 monopoly agreements since 2010.

NDRC and SAIC visibly increased their enforcement efforts in the monopoly agreement area in 2013. During that year, NDRC investigated and imposed fines in five monopoly agreement cases:

- LCD panel price-fixing,

[2] Anti-Price Monopoly Regulation, [2010] NDRC Order No. 7, December 29, 2010.

[3] Regulation on the Administrative Enforcement Procedure for Anti-Price Monopoly, [2010] NDRC Order No. 8, December 29, 2010.

[4] Regulation on the Prohibition of Monopoly Agreement Conduct, [2010] SAIC Order No. 53, December 31, 2010.

[5] Regulation on the Procedure for the Handling of Cases Involving Monopoly Agreements and Abuses of a Dominant Market Position, [2009] SAIC Order No. 42, June 5, 2009.

- Maotai and Wuliangye's resale price maintenance ("RPM") for Chinese liquor,
- Xinjiang insurance price monopoly agreement,
- infant milk formula RPM, and
- the monopoly agreement by the Shanghai Gold & Jewelry Trade Association.

The three cases investigated and closed by SAIC during 2013 are the Zhejiang Cixi construction project verification monopoly agreement, the monopoly agreement by the Sichuan Yibin Construction Brick & Tile Association, and the monopoly agreement by the Yunnan Xishaungbanna Tourism Association.

Overall, by the fifth anniversary of the AML's entry into effect—August 2013—China's enforcement efforts against monopoly agreements had become noticeably rigorous, covering such sectors as construction, energy, tourism, insurance, electronics, the used car market, and food. Among the 22 cases investigated and closed by NDRC and SAIC since 2010, 18 were horizontal agreements, and four were vertical agreements (including the Maotai and Wuliangye *White liquor* cases where the key issues were RPM and territorial restrictions, and the *Baby milk formula* RPM case).

In terms of penalties, the heaviest fine NDRC imposed on monopoly agreements under the AML occurred in 2013. In particular, on August 7, 2013, NDRC issued the record fine of RMB 670 million (approximately U.S.$110 million) on six infant milk powder companies, including Mead Johnson Nutrition, Danone, Fonterra, Abbott Laboratories, FrieslandCampina, and Biostime International, for engaging in RPM and attempted fixing of retail prices for infant milk powder.

A number of monopoly agreement violations investigated by NDRC and SAIC involved and, in fact, were facilitated by trade associations. Among the 22 cases mentioned above, 14 involved trade associations. The first antitrust fine imposed on trade associations under the AML had been issued in the *Pre-mixed concrete* case in Lianyungang in 2010, in the amount of RMB 200,000 (around U.S.$32,000). A more recent case was the Shanghai Gold & Jewelry Trade Association case. On August 13, 2013, NDRC issued a decision imposing fines of more than RMB 10 million (approximately U.S.$1.6 million) upon the Shanghai Gold & Jewelry Trade Association and five Shanghai gold retailers. The five retailers were Shanghai Laofengxiang, Laomiao Gold, Firstasia Gold, Chenghuang Jewelry, and Tianbao Longfeng. According to NDRC's investigation, the gold and jewelry prices in these gold shops remained at the same level, supervised under the auspices of the Shanghai Gold & Jewelry Trade Association.[6]

Recent AML enforcement has also underscored the effectiveness of China's leniency programs as a weapon to combat monopoly agreements. For example, the *Sea sand* case in Guangdong involved more than 20 companies that had organized a series of secret meetings to coordinate the price of sea sand starting in November 2010. According to NDRC, the companies were fully aware that they were breaking the law and took steps to conceal their actions.

[6] *See* Xinhua, *Shanghai gold retailers fined over monopoly*, August 13, 2013, *available at* http://news.xinhuanet.com/english/china/2013-08/13/c_132626003.htm (last visited on January 9, 2014).

The increase in the price of sea sand affected the price of concrete and, subsequently, the cost of several ongoing construction projects, including the Hong Kong-Zhuhai-Macau Bridge. This attracted the attention of, first, the government of Guangdong province, and then NDRC. As the authorities initially encountered difficulties in investigating the cartel, they targeted six core members and used the leniency program to obtain essential evidence, including the names of the participants and the text messages exchanged between them. Fines were imposed on three of the cartel participants, two of whom were identified as organizers of the cartel and the third being the primary beneficiary of the cartel. One of the two "ringleaders" saw its fine reduced by 50 percent for voluntarily providing important evidence to the authorities under the leniency program. The other two companies each received the maximum fine permitted under the AML—10 percent of the preceding year's sales revenue. Other participants received a warning but were not subject to a monetary penalty.[7]

In the *Baby milk formula* case, NDRC also applied the leniency program. Three companies involved in the same case—Nestlé, Meiji, and Zhejiang Beingmate Scientific Technology Industry &Trade—were not punished because they cooperated with the investigators, provided important evidence, and carried out active "self-rectification." The other six companies were fined, heavily, as mentioned above.

IV. INTERESTING ISSUES REFLECTED IN KEY CASES

A. More Guidance Is Needed on Standards of Legality

Chapter 2 of the AML covers both horizontal and vertical monopoly agreements. The language of the AML does not specify explicitly whether the *per se* rule or the rule of reason applies to either horizontal or vertical agreements (or both). On the one hand, Article 13—governing horizontal agreements—prohibits "hard-core cartels" such as price-fixing, setting output/sales quota, and market partitioning, which are mostly treated under the *per se* rule by international standards. On the other hand, Article 15 provides that even hard-core cartels can be exempted for a number of reasons; for example, to cope with recessions or to promote exports.

Of NDRC's and SAIC's 18 closed horizontal cases, all were hard-core cartel agreements and none seemed to fall into the exemption category of recession or export cartels. In addition, all cases seem to be dealt with by the *per se* rule. Further, with one exception, there has not been any information made public that indicates the cartel members engaged in an affirmative defense of their conduct. The exception is NDRC's investigation of the Liaoning cement association price-fixing case in 2012.[8] With these cases being examined under a *per se* rule approach, this is a good sign that China's antitrust enforcement against cartels is consistent with international best practice.

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[7] Information about NDRC's investigation can be found at NDRC website at http://www.sdpc.gov.cn/zjgx/t20121026_510843.htm (last visited on January 9, 2014). *Also see China's NDRC Uses Leniency Program to Uncover and Punish Members of Cartel*, *available at* http://www.mondaq.com/unitedstates/x/210306/Antitrust+Competition/UK+Supreme+Court+Issues+First+Antitrust+Ruling (last visited on January 9, 2014).

[8] In this case, NDRC considered such factors as the presence of excessive capacity in the sector and ruled that the agreement was not illegal. *See*, e.g., http://info.ccement.com/news/content/4182375948569.html, last visited on February 6, 2014.

On vertical agreements, the AML specifically singles out just two types of illegal agreements: setting the resale prices, or minimum resale prices, to a third party—in other words, resale price maintenance ("RPM"). Three of the four vertical agreements investigated and closed by NDRC (the *Maotai*, *Wuliangye,* and the *Baby milk formula* cases) were violations of the RPM prohibition.

Although these three cases created nation-wide attention in China, it is still not clear whether a *per se* rule or the rule of reason applies to vertical agreements such as RPM—even after five years of enforcement since the AML went into effect. In fact, in the *Maotai* and *Wuliangye* cases, the final AML violation decisions issued by the local NDRC offices seem to have adopted different rules toward RPM.

In the first instance, the Price Bureau in Guizhou Province in the Maotai case stated in its decision that "Maotai had imposed minimum retail prices in its contracts with its distributors, and imposed penalty on those distributors not obeying the minimum retail price, thus violating Article 14 of the AML, and eliminating and restricting competition, and harming consumer welfare." There was no further elaboration on how the Bureau reached its decision.[9] The Baby milk formula RPM case also seemed to be dealt with in a similar way by NDRC.[10]

However, in the *Wuliangye* case, the official statement published by NDRC office in Sichuan Province pointed out that Wuliangye used its "market strength" to fix the minimum resale price. It found that such behavior violated Article 14 of the AML, as it restricted competition and damaged the interests of consumers. To support this finding, NDRC's Sichuan office further analyzed various anticompetitive effects arising from Wuliangye's conduct, referring to restrictions to both intra-brand and inter-brand competition. Also, the NDRC office held that Wuliangye's conduct damaged consumer welfare as it impaired the consumer's right to buy products at a lower price. The regulator also found that the degree of substitutability of Wuliangye's liquors was low.

The decision of the Sichuan NDRC office is consistent with the rule of reason approach established in the United States where the U.S. Supreme Court established the rule of reason approach for RPM in its *Leegin* decision, after decades of academic and legal debates. The Sichuan decision is also consistent with the decision in the *Rainbow v. Johnson & Johnson* case by a Shanghai court in 2013.[11]

Based on their cases to date, it would be sensible for NDRC and SAIC to explicitly establish a rule of reason approach toward vertical agreements such as RPM, especially in light of the decisions regarding *Maotai* and *Wuliangye* cases.

Similarly, the 18 horizontal agreements fined by NDRC and SAIC so far seem to have been adjudicated under the *per se* rule approach. Based on these decisions, and consistent with

[9] The official decision (in Chinese) can be found at http://finance.21cn.com/news/macro/a/2013/0222/16/20446945.shtml, last visited on January 9, 2014.

[10] *See* http://news.xinhuanet.com/fortune/2013-08/07/c_116846276.htm, last visited on February 6, 2014.

[11] Shanghai High People's Court, *Bangrui Yonghe Technology Trading Co., Ltd. v. Johnson & Johnson (Shanghai) Medical Equipment Co., Ltd. and Johnson & Johnson Medical (China) Ltd.*, August 1, 2013, [2012] Hu Gao Min San (Zhi) Zhong Zi No. 6.

international standards, it would be appropriate for NDRC and SAIC to explicitly announce that the *per se* rule applies to those hard-core cartels that are neither recession nor export cartels (so as to be consistent with Article 15 of the AML).

B. High Level of Trade Associations Involvement

An important feature of the monopoly agreements that have been uncovered and fined by NDRC and SAIC is the high level of involvement of trade associations. In particular, in 14 of the 18 horizontal monopoly cases closed by the two agencies as of 2013, trade associations acted as organizers of the illegal agreements. These cases include the pre-mixed concrete cartel case in Lianyungang, price-fixing by the Fuyang Paper Association, the monopoly agreement by the Xishuangbanna Tourism Association in Yunnan, and the Shanghai Gold & Jewelry Trade Association case.

Frequent involvement of trade associations in monopoly agreement cases in China may be caused by several reasons. The first reason—which may be relatively easy to overcome—is that many trade associations in China were, and still are, unaware of the existence of the AML. Influenced by the traditional central-planning way of reasoning, some trade associations still consider coordinating activity by, and helping organize monopoly agreements among, firms in their respective sectors as their "duty." Some trade associations publically promote coordination among firms, and even push the firms to follow their "self-regulations." In some cases, trade associations have even pushed members to sign written agreements or meeting minutes.[12] The Pre-mixed concrete and Shanghai Gold & Jewelry Trade Association cases belong to this category. In the Shanghai case, the trade association was even blaming the NDRC staff for interfering with their normal duties.[13]

The second possible reason for Chinese trade associations to engage in anticompetitive practices is the insufficient deterrence effect of the AML towards conduct by trade associations. While Article 16 of the AML specifically provides that trade associations shall not engage in anticompetitive conduct, the maximum penalty applicable for violations by trade associations is only RMB 500,000.

Consistent with international standards, the AML prohibits anticompetitive conduct by trade associations as well as by business operators. Monopoly agreements organized or facilitated by trade associations have the same competitive effects as agreements reached by companies directly. One could even go further and argue that monopoly agreements, especially cartels, reached by trade associations are more detrimental to competition—trade associations may be able to provide more effective channels for businesses to communicate, achieve, and enforce cartel agreements. In addition, cartels facilitated by trade associations cause more damage to "competition culture" compared to cartels organized (secretly) by some, but not all, firms in the relevant sector.

[12] *See* Clare Gaofen Ye, *The Anti-monopoly Regulation of the Monopoly Agreements in China*, REPORT ON COMPETITION LAW AND POLICY OF CHINA 2011, Ch. 2 (2011) and http://news.xinhuanet.com/fortune/2008-07/31/content_8883762.htm, last visited on February 6, 2014.

[13] *See* NDRC website at http://jjs.ndrc.gov.cn/gzdt/t20130813_553441.htm (last visited on January 9, 2014).

Based on the above considerations—including the observed high frequency of AML violations by trade associations—I am of the view that the legal consequences for AML violations by trade associations are not severe enough and should be strengthened.

It is striking to see that many trade associations in China are still unaware of the AML and instead regard their cartel-facilitating services as contributing to the healthy development of their sectors—even five years after the AML took effect. Judging from the cases, such ignorance even exists among trade associations in China's economic and financial center, Shanghai. It is thus imperative for China's enforcement agencies, including the Anti-Monopoly Commission, to increase their efforts in competition advocacy and promote a culture of fair competition and educate the business community.

Furthermore, the antitrust authorities should be more transparent about closed cases. This would increase competition awareness within the business community, particularly by trade associations, and would thus enhance the deterrence effect of the AML. The business community would understand better the legal and economic reasoning of the agencies in their decisions,[14]helping reduce legal uncertainty. Such awareness, in turn, would help reduce the number of cartels organized by trade associations, and thus lead to great benefits for consumers in China.

C. Effectiveness of and Consistency Between Leniency Programs

In China, leniency programs have played an important role in NDRC's detecting antimonopoly violations; for example, for the cartel activities in the *Sea sand* and *LCD panel* cases and RPM conduct in the *Baby milk formula* case. SAIC, by contrast, has not yet applied the leniency program as stipulated in the *Regulation on the Procedure for the Handling of Cases Involving Monopoly Agreements and Abuses of a Dominant Market Position.*

It is interesting to note that there are several important differences between the two leniency programs of NDRC and SAIC as applied to their respective responsibilities, namely price-monopoly agreements for NDRC and non-price monopoly agreements for SAIC:

- First, "organizers of monopoly agreements" do not qualify for exemption or fine reduction under SAIC's leniency program.[15] By contrast, there is no such restriction in NDRC's leniency program. In fact, in the *Sea sand* case in Guangdong, NDRC showed that even organizers/leaders of cartel agreements can enjoy partial immunity—one of the three organizers was given a 50 percent reduction in the fine. (The other two organizers were imposed the maximum fine level under the AML, namely 10 percent of the sales revenues in the preceding year.)
- Second, the NDRC leniency program stipulates that the first firm that comes forward with important evidence "may" enjoy full immunity and the fine for the second whistle-

[14] In this regard, SAIC has done a better job in that its official announcements of the 12 monopoly agreements cases were much more comprehensive and detailed.

[15] Regulation on the Procedure for the Handling of Cases Involving Monopoly Agreements and Abuses of a Dominant Market Position, [2009] SAIC Order No. 42, June 5, 2009, Art. 10.

blower "may be" reduced by up to 50 percent.[16] By contrast, SAIC's leniency program provides more certainty by stipulating that "full immunity will be granted" to the first whistle-blower to provide the authority with relevant information and important evidence.[17]

It may be argued that granting (even partial) immunity to organizers of a cartel may be "injustice" and, hence, SAIC's leniency program is fairer. However, NDRC's leniency program may be more effective in detecting a monopoly agreement by inducing the "ring leader" to come forward. If SAIC's leniency program had been applied in the *Sea sand* case, the organizer might not have come forward to provide important evidence to NDRC and the cartel might not have been detected as easily.

The second difference between the two authorities' leniency programs reveals that SAIC's program is "more lenient" in that it grants full immunity to the first whistle-blower and hence provides certainty (unless the first whistle-blower was the organizer of the monopoly agreement). In contrast, there is some degree of uncertainty as to whether a fine reduction can be obtained under NDRC's leniency program. This uncertainty may discourage participants in a monopoly agreement from coming forward with evidence. Considering these two differences, it is not clear which leniency program is more effective.[18]

In any event, the inconsistency between the two agencies' leniency programs creates uncertainty about the rules, and contrasts with international standards for using leniency programs to combat cartels. [19] A revision of the two agencies' leniency programs to set a uniform policy seems justified.

Finally, another interesting observation is that NDRC has applied its leniency program to vertical monopoly agreements, as seen in the *Baby milk formula* case. This extension of leniency program to vertical agreements is not common in antitrust practices outside China.

V. CONCLUDING REMARKS

Several interesting patterns have emerged from the increasing antitrust enforcement efforts by NDRC and SAIC, in particular during 2013. For example, trade associations have played an important role in facilitating horizontal monopoly agreements; this was the case in 14 out of the 18 such agreements fined by the two agencies as of the end of 2013. Also, NDRC has applied its leniency program both to horizontal agreements (for example, in the *Sea sand* case) and, interestingly, vertical agreements (in the *Baby milk formula* case).

China's antitrust enforcement can be further improved with clear(er) legal standards towards vertical agreements, heavier penalties for AML violations by trade associations, as well as

[16] Regulation on the Administrative Enforcement Procedure for Anti-Price Monopoly, [2010] NDRC Order No. 8, December 29, 2010, Art 14.

[17] Regulation on the Procedure for the Handling of Cases Involving Monopoly Agreements and Abuses of a Dominant Market Position, [2009] SAIC Order No. 42, June 5, 2009, Art. 11.

[18] It is conceivable that the self-reporting organizer of the Guangdong Sea Sand price-fixing case was assured by NDRC staff of getting a fine reduction conditional upon providing evidence during the investigation.

[19] *See*, e.g., INTERNATIONAL COMPETITION NETWORK, ANTI-CARTEL ENFORCEMENT MANUAL (2009).

better competition advocacy and increased transparency. A unified leniency program based on the existing leniency policies of NDRC and SAIC is also desirable.

Moreover, the separation of enforcement duties for price and non-price monopoly agreements between NDRC and SAIC has been criticized by many,[20] as the separation increases the risks of inconsistency in AML enforcement. Indeed, a monopoly agreement may have both pricing and non-pricing dimensions, in which case cooperation between NDRC and SAIC is necessary.[21] To avoid the dilemma of contrasting decisions, the two agencies should set up an effective cooperation mechanism that includes an information/file exchange. It may also make sense for the agencies to set up project-based task-force groups that would help identify potential complementary expertise between their officials and facilitate effective cooperation on a case-by-case basis.

[20] *See*, e.g., Wang, Xiaoye, ANTI-MONOPOLY LAW at 333-335 (2011); Allan Fels, *China's Antimonopoly Law 2008: An Overview*, 41(7) REV. INDUS. ORG., 7–30 (2012), and Angela Huyue Zhang, *The Enforcement of the Anti-Monopoly Law in China: An Institutional Design Perspective*, 56 ANTITRUST BULL. 630-663 (2011).

[21] Such a situation arose in the Liaoning Cement Trade Association 2012 case, which involved both price-fixing and output restrictions. Both NDRC and SAIC investigated the same facts but reached different decisions. SAIC found the output restriction arrangement to violate the AML, but NDRC held that the same restriction did not constitute monopoly conduct. *See* SAIC website: http://www.saic.gov.cn/zwgk/gggs/jzzf/201307/t20130726_136746.html, last visited on February 6, 2014, and http://info.ccement.com/news/content/4182375948569.html, lasted visited on February 6, 2014. Also see Clare Gaofen Ye, *The Anti-monopoly Regulation of the Monopoly Agreements in China*, REPORT ON COMPETITION LAW AND POLICY OF CHINA 2013 (2013).