CLEARY GOTTLIEB Alert Memo

BRUSSELS AND HONG KONG, SEPTEMBER 16, 2009

www.clearygottlieb.com

China's Anti-Monopoly Law: One Year On

China's Anti-Monopoly Law ("AML") entered into force in August 2008. Since then, the Chinese Anti-Monopoly Commission ("AMC") and Anti-Monopoly Enforcement Authorities ("AMEAs") have made considerable progress in fleshing out China's antitrust regime, including by issuing a number of regulations, rules and guidelines.[1]

This memorandum reviews the progress made by the AMC and AMEAs, comments on continuing concerns with the Chinese antitrust regime, and discusses the work that remains to be done. Four general observations merit specific mention.

- Although a large number of regulations, rules and guidelines have been published in draft or final form, there are still significant ambiguities and a number of important holes in China's regulatory framework. Notably, although SAIC has proposed the outlines of a leniency program for non-price related antitrust violations, NDRC has so far not proposed a leniency program for price fixing and other price-related antitrust violations.

- The AMEAs have so far provided little guidance on the substantive application of the AML. MOFCOM has handled a large number of merger cases, but it has published decisions in only three, and all three decisions have attracted criticism from a Western competition law standpoint. The Anti-Monopoly and Anti-Unfair Competition Enforcement Bureau of the State Administration for Industry and Commerce ("SAIC") and the Price Supervision Department of the National Development and Reform Commission ("NDRC") have not published any decisions regarding restrictive agreements or abuses of dominant positions.

- The unusual division of authority between SAIC and NDRC creates the potential for overlapping jurisdiction in many cases. Clear rules as to which agency will handle which cases will be needed, and care will be required to ensure that the two agencies' rules and regulations are consistent.

[1] A table summarizing these measures, whether in final or draft form, can be found at the end of this alert memo.

- A number of cases alleging abuses of dominant positions have been filed before the Chinese courts, suggesting that private litigation may play a larger role in the early development of Chinese antitrust law than many expected when the AML was adopted.

I. BACKGROUND

The AML entered into force on August 1, 2008, establishing the first comprehensive competition law regime in China.

Responsibility for enforcing the AML is allocated to the AMEAs as follows:

- MOFCOM: Merger control review, as well as investigating anti-competitive conduct in international trade.

- SAIC: Non-price related violations, primarily abuses of dominant positions and administrative power,[2] but also non-price aspects of anti-competitive agreements.

- NDRC: Price-related anti-competitive agreements and abuses of dominant positions or administrative power.

The AMC, which was created by the AML, is in charge of coordinating the AMEAs' enforcement of the AML. The AMC's responsibilities also include: (i) developing competition policy; (ii) organizing surveys, assessing the general competitive situation, and issuing reports; (iii) formulating and promulgating guidelines; and (iv) performing other functions as specified by the State Council, which is the highest administrative authority in China.

II. MERGER CONTROL

Under the AML, MOFCOM must review notifiable transactions meeting the relevant thresholds, and can review transactions falling below the thresholds, to determine whether these transactions have or may have the effect of eliminating or restricting competition. The factors taken into account in such a review include not only competition-related considerations (such as market shares, degree of market concentration, and barriers to entry and expansion), but also factors such as a transaction's effect on "the development of the national economy" and "other relevant undertakings," not only consumers. MOFCOM officials have attended many antitrust seminars and workshops, held meetings with their counterparties around the globe, and consulted academics and private practitioners. MOFCOM has published rules and guidelines that clarify its merger review procedures. Finally, MOFCOM has published

[2] This alert memo does not discuss abuses of administrative powers under the AML.

its decisions in three high-profile cases. There are, however, still important uncertainties about MOFCOM's procedures and substantive analysis.

A. REGULATORY FRAMEWORK

MOFCOM has adopted several rules and guidelines in final form, while others have been published in draft form. These rules and guidelines are helpful in clarifying MOFCOM's approach to merger control, but they leave many questions unanswered. Moreover, MOFCOM has not yet tackled the difficult task of developing guidelines discussing its substantive treatment of proposed transactions.

1. Rules and Guidelines

a. Final rules and guidelines

On August 3, 2008, China's State Council published its Regulation on Notification Thresholds for Concentrations of Undertakings. Pursuant to this Regulation, a merger must be notified when either the worldwide turnover of all the undertakings concerned in the preceding year was more than RMB 10 billion or the turnover in China of all the undertakings concerned in the preceding year was more than RMB 2 billion, and, in either case, the turnover in China of at least two of the undertakings concerned was at least RMB 400 million. Special rules for applying these thresholds in transactions involving financial institutions were adopted jointly by MOFCOM and other regulatory bodies on July 15, 2009.[3]

In January 2009, MOFCOM adopted guidelines on Notification of Concentrations between Undertakings, Notification Documents and Materials for Concentrations between Undertakings, and Merger Control Review of Concentrations between Undertakings, which represented a first step in fleshing out the operation of the AML's merger control regime.

Guidelines on the Definition of Relevant Markets (the "Market Definition Guidelines") were published on July 8, 2009.[4] They detail the steps to be taken when defining relevant product and geographic markets. These guidelines also detail factors to

---

[3] These rules mainly deal with the calculation of turnover of financial institutions. Sums of money received and managed by financial institutions other than revenues, fees and interest are not taken into account. In addition, the turnover of financial institutions is automatically multiplied by 10% in order to effectively increase the threshold for financial institutions.

[4] For a detailed review of these guidelines, please refer to our alert memo of July 24, 2009, which may be found at: http://www.cgsh.com/chinas_anti-monopoly_commission_of_the_state_council_issues_final_guidelines_for_the_definition_of_relevant_market/.

be taken into consideration when defining relevant markets, including evidence of customer switching, customer preferences and, if relevant, supply-side substitutability. While initially drafted by MOFCOM, the final guidelines were issued by the AMC and deal with market definition not only for merger control purposes, but also for the purpose of analyzing restrictive agreements and abuses of dominant positions. The Market Definition Guidelines are largely consistent with EU and U.S. practice, although they do depart from international norms in certain respects. For example, Article 7 of the Market Definition Guidelines restricts the use of the so-called "hypothetical monopolist test" to situations where the market definition is "less clear." This is inconsistent with standard practice in the U.S. and EU, which use the test as the conceptual basis and starting point for the definition of relevant markets.

b. Draft Rules and Guidelines

In January and February 2009, MOFCOM published for comment the following draft rules,[5] revised drafts of which were released by Legislative Affairs Office under the State Council in March 2009:

- Draft Provisional Rules on Investigation and Handling of Concentrations of Undertakings that are not Legally Notified ("Draft Investigation Rules");
- Draft Provisional Rules on the Collection of Evidence regarding Concentrations of Undertakings Below Thresholds but Suspected of Being Anti-Competitive ("Draft Small Concentration Rules");
- Draft Provisional Rules on Investigation and Handling of Concentrations between Undertakings Below Thresholds but Suspected of Being Anti-Competitive ("Draft Small Concentration Investigation Rules");
- Draft Provisional Rules on the Notification of Concentrations of Undertakings ("Draft Notification Rules"); and
- Draft Provisional Rules on the Examination of Concentrations of Undertakings ("Draft Examination Rules").

These rules have not yet been finalized, and we understand that the published drafts may undergo fairly significant changes before they are released in final form.

---

[5] For a detailed review of some of these rules, please refer to our alert memo of January 30, 2009, which may be found at: http://www.cgsh.com/proposed_merger_control_rules_under_the_chinese_anti_monopoly_law/.

The Draft Investigation Rules cover the investigation of transactions that were not notified but should have been. After its investigation, if MOFCOM determines that a transaction should have been notified, it may impose sanctions, including a forced unwinding of the transaction and monetary penalties. To date, no such sanctions have been imposed.

Like the U.S. agencies, MOFCOM has the power to investigate transactions that fall below the notification thresholds. The Draft Small Concentration Rules and Draft Small Concentration Investigation Rules cover the collection of evidence and investigation regarding transactions below the notification thresholds but suspected of having, or being likely to have, anti-competitive effects. Parties may voluntarily notify such transactions.

The Draft Notification Rules attempt to more precisely define the circumstances under which a transaction is notifiable and cover the procedures required for the filing of a transaction notification form. Importantly, the rules define key terms and concepts like "control" and "turnover." The rules also define materials required to be submitted with the notification.

The Draft Examination Rules summarize the tools available for MOFCOM's investigations, such as contacting competitors, customers and industry associations and holding hearings, and the parties' rights of defense. MOFCOM will conduct a preliminary review of a transaction. If it determines that it will not undertake a further review or takes no decision within the time limit (30 days from the initiation of the investigation), the parties may close the transaction. If it decides to initiate a more detailed review, it will notify the parties in writing. The more detailed review may last up to 90 days, which can be extended by up to an additional 60 days. MOFCOM may decide to clear a transaction, approve it subject to conditions, or prohibit it. The parties may offer remedies to eliminate any possible anti-competitive effects.

B. IMPLEMENTATION

Through the end of June 2009, MOFCOM had received 58 merger notifications and completed its review of 46 transactions, of which 43 were unconditionally approved, two were approved with conditions (InBev/Anheuser-Busch and Mitsubishi Rayon/Lucite), and one was blocked (Coca-Cola/Huiyuan). MOFCOM published its decisions regarding the two transactions approved with conditions and the prohibited transaction. While these decisions provide some insight into MOFCOM's application of its merger review powers under the AML, they also give cause for concern. None of these decisions articulates a clear theory of harm with supporting evidence that would clearly justify the conclusions reached, and the remedies imposed in the InBev and Mitsubishi cases were unusual from a U.S. or EU antitrust perspective.

- On November 18, 2008, MOFCOM approved InBev's acquisition of Anheuser-Busch ("AB"), subject to conditions. Particularly, MOFCOM imposed limitations on InBev/AB acquiring additional shares in certain named Chinese competitors. This was highly unusual from a U.S. or EU antitrust perspective, particularly given MOFCOM's failure to identify any competitive harm caused by the transaction.

- On March 18, 2009, MOFCOM blocked Coca-Cola's planned acquisition of Huiyuan, in the first prohibition decision adopted under the AML.[6] The prohibition was based on concerns that Coca-Cola would be able to leverage its dominant position in the carbonated soft-drink market to the fruit-juice drink market, eliminating and restricting competition from current juice manufacturers and in turn harming juice consumers. The decision's reference to leveraging suggests that MOFCOM applied a conglomerate effects theory of the kind abandoned many years ago in the United States and applied in the EU only rarely, cautiously, and in situations where the evidence has been compelling.

- While MOFCOM's spokesperson stressed that the decision was based solely on competition law, the decision's references to effects on domestic small and medium-sized manufacturers and the sustainable and healthy development of the Chinese fruit-juice drink industry suggest that industrial policy considerations played a significant role. If so, MOFCOM's approach seems consistent with the AML requirement that it take account of the "development of the national economy" and "other considerations that may affect market competition as identified by the AML enforcement authority."

- On April 24, 2009, MOFCOM approved, with conditions, Mitsubishi Rayon's ("Mitsubishi's") acquisition of Lucite. The conditions imposed included restrictions against Mitsubishi adding Chinese methyl methacrylate capacity. This condition is inconsistent with generally accepted antitrust principles, since increasing output is usually considered positive from an antitrust perspective.

C. ISSUES

Although MOFCOM has been the most active of the AMEAs in applying the AML, publishing decisions and developing the regulatory framework for merger review in China, MOFCOM's published decisions have raised concerns among multinational

[6] For a more detailed analysis of the Coca-Cola/Huiyuan decision, please refer to our alert memo of March 23, 2009, which may be found at http://www.cgsh.com/coca-cola_huiyuan_first_chinese_prohibition_decision_under_new_merger_control_rules/.

companies, and there are still a number of significant ambiguities and issues in MOFCOM's regulatory framework.

With regard to MOFCOM's substantive application of its merger review powers, as discussed above, from a Western antitrust law perspective none of the three published decisions appear to justify the conclusions reached, and MOFCOM's approach to remedies appears inconsistent with U.S. and EU practice. MOFCOM was criticized especially for its prohibition of Coca-Cola/Huiyuan. In all three cases, the decisions reached suggest that MOFCOM is ready to use the merger control process to address the possibility of future, non-merger-specific harm. Future decisions will indicate whether MOFCOM's approach to merger control will converge with international standards in this area.

With regard to MOFCOM's regulatory framework, the final and draft rules, regulations, and guidelines leave a number of important issues open to interpretation. Some have argued that the ambiguity in these measures is intentional, as it gives MOFCOM more discretion. The outstanding issues can be grouped broadly into three categories.

1. Jurisdiction

A transaction triggers a notification requirement only if it qualifies as a "concentration." A concentration arises under the AML when an undertaking obtains "control" or "decisive influence" over another undertaking. The second Draft Notification Rules clarified that the acquisition of "protective" minority rights will not result in the acquisition of "control," and the draft gives examples of "protective" minority rights, such as the right to veto modifications of articles of association, increases and decreases of capital, and liquidation. In spite of these helpful clarifications, however, the definition of "control" that will give rise to a notifiable transaction, in particular the distinction between "control", "joint control", and "decisive influence", remain unclear.

Another area of ambiguity is the treatment of joint ventures. The draft rules indicate that "specific function" joint ventures (joint ventures that only carry out specific functions for their parent companies, such as research and development, sales, and production of certain products) may not be notifiable, and that a joint venture will be notifiable only if it is established on a lasting basis and is independently operated. The treatment of joint ventures under the AML has been receiving attention lately in connection with the proposed BHP Billiton/Rio Tinto transaction, which would establish a joint venture for the production of iron ore in Australia. MOFCOM personnel have argued that the transaction is reportable, while the parties argue that it is a production joint venture only and is not "full function."

2. Review Procedure

Similarly, there are significant issues related to MOFCOM's review of notified transactions.

An important practical consideration for notifying parties is the excessive information required to complete a merger notification form. Merger notifications under the AML require a significant amount of information, but MOFCOM's rules do not provide for simplified notifications in cases that raise no substantive issues. Moreover, notifications must be accompanied by vaguely but broadly defined categories of documents, many of which may not be relevant to the antitrust analysis of concentrations.

Another issue relates to the timing of MOFCOM's review. MOFCOM's review period does not begin until MOFCOM accepts a filing as complete. The breadth and vagueness of the required supporting documents give MOFCOM the ability to extend a merger review by continuously requesting supplemental materials. For example, MOFCOM asked Coca-Cola to supplement its filing regarding the proposed acquisition of Huiyuan four times. Two months elapsed before MOFCOM accepted the filing. A related issue is the effect of questions posed by MOFCOM after a filing is accepted; in some cases, notifying parties have been told that MOFCOM's review period would be suspended until they replied. Whether MOFCOM's review can be extended with the notifying parties' agreement is similarly unclear.

3. National Security Review and National Economic Security Review

While not directly related to MOFCOM's antitrust work, there are also significant ambiguities concerning the "national security review" of proposed transactions. Under Article 31 of the AML, a "national security review" is required when a transaction involving a foreign acquirer and a domestic target may impact national security. Importantly, it is unclear exactly what target activities trigger such a review, which authorities will conduct a national security review and how they will do so.

The relationship between "national security review" and "national economic security review" also needs further clarification. On July 23, 2009, MOFCOM released a revised version of its Rules on Acquisition of Domestic Enterprises by Foreign Investors (the "M&A Rules"). The revised rules replace the rules adopted in 2006, which, among other things, regulated merger control filings in China before the AML entered into force. The main substantive change introduced by the revised M&A Rules is to replace the chapter dealing with merger control with a reference to merger control rules under the AML and Regulation on Notification Thresholds for Concentrations of Undertakings. However, the M&A Rules continue to require foreign investors to determine whether a proposed transaction involves "key industries and contains factors

that would have an impact or potentially impact on national economic security or leads to the transfer of actual control of a well-known trademark or a time-honored Chinese brand from a domestic enterprise." If so, the parties must make an additional filing to MOFCOM. Additional guidance regarding the factors that might trigger a "national economic security review," the substantive standards of the review, and the relation between the "national security review" under the AML and the "national economic security review" under the M&A Rules would be helpful.

III. ANTI-COMPETITIVE AGREEMENTS AND ABUSES OF DOMINANT POSITIONS

Responsibility for the enforcement of the AML with regards to anti-competitive agreements and abuses of dominant positions is divided between SAIC (if the abuse is non-price related) and NDRC (if the abuse is price-related).

While SAIC and NDRC have seemingly not been as active as MOFCOM, SAIC has issued a number of draft and final rules, and NDRC issued important draft rules in August 2009. Due to the unusual division of authority between SAIC and NDRC, there is a considerable potential for overlap, and multinational companies could benefit from additional clarification regarding the boundaries of each AMEA's jurisdiction. In this regard, we understand that SAIC and NDRC have been collaborating to ensure that their draft rules and guidelines do not conflict. In addition, like MOFCOM, both NDRC and SAIC have attended and hosted antitrust seminars and taken other action to prepare for AML enforcement. Neither SAIC nor NDRC has to date published any decisions under the AML.

A. ANTI-COMPETITIVE AGREEMENTS

1. Non-Price Related Agreements

On June 5, 2009, SAIC adopted procedural rules that apply to anti-competitive agreements and abuses of dominant market positions agreements: Procedural Rules on Investigating and Handling of Cases of Restrictive Agreements and Abuse of Market Dominance by the Administrative Authority of Industry and Commerce ("Investigation and Handling Rules").

These rules detail SAIC's procedure when enforcing the non-price-related antitrust provisions of the AML, including the jurisdiction of provincial authorities, launching investigations of allegedly anti-competitive conduct and the tools available to SAIC for conducting its investigations.

On April 27, 2009, SAIC published draft Rules on Prohibition of Restrictive Agreements (the "Draft Restrictive Agreement Rules"). The Draft Restrictive Agreement Rules provide guidance with respect to (i) the definition of "restrictive

agreements"; (ii) types of restrictive agreements that are prohibited under the AML; (iii) the role of industry associations; and (iv) SAIC's proposed leniency program.

The Draft Restrictive Agreement Rules prohibit horizontal agreements that: (i) restrict the volume or production of sales; (ii) divide sales or procurement markets among competitors; (iii) restrict the purchase or development of new technology or equipment; (iv) jointly boycott a buyer or seller; and (v) result in collusion in bidding. The rules also prohibit the following vertical agreements: (i) between a tenderer and bidder during a bid; (ii) agreements that, without justifiable reasons, restrict the territory in which a transaction counterparty may operate; and (iii) exclusive dealing arrangements that, without justifiable reasons, limit a purchaser's options.

Under the Draft Restrictive Agreement Rules, restrictive agreements include written agreements, oral agreements and concerted practices (with explicit or tacit collusion). To determine whether practices are in fact "concerted," SAIC will consider the degree of consistency in the relevant companies' behavior, the existence (or not) of legitimate reasons for identical or similar acts, the structure of the relevant market, and changes in market conditions.

The factors set out in the Draft Restrictive Agreement Rules to determine what practices will be considered "concerted" are quite vague. By contrast, there is well-developed precedent in the United States and Europe regarding the analysis of available evidence (known in the United States as "plus factors") to determine whether concerted action rises to the level of an illegal agreement, and the government carries a fairly high burden of proof.

The Draft Restrictive Agreement Rules also outline the first leniency program to be proposed by an AMEA. However, the rules do not make clear whether they apply only to hard-core agreements such as cartels, the specifics of the requirements for obtaining leniency and whether the agencies have discretion to deny leniency to applicants that meet the requirements.

In addition, the Draft Restrictive Agreement Rules do not adequately distinguish between agreements that could be prohibited *per se* (like an output restriction or an agreement to allocate territories) and those that should be analyzed under a rule-of-reason approach that considers the effects and justifications for the alleged conduct.

2. Price-Related Agreements

On August 12, 2009, NDRC published draft Rules on Anti-Pricing Monopoly (the "Draft Anti-Pricing Monopoly Rules"), which apply to price-related anti-competitive agreements and provide detail as to the types of behavior that will constitute such an anti-competitive agreement. Price-related anti-competitive agreements are defined as "any agreements, decisions, in writing or verbally, or other concerted actions

between two or more undertakings that eliminate or restrict competition in price." The draft rules prohibit competitors from fixing prices or discounts, using a standard formula to calculate prices, agreeing not to modify prices, restricting output, dividing up markets and similar conduct.

Surprisingly, the Draft Anti-Pricing Monopoly Rules suggest that NDRC has jurisdiction over agreements between competitors that restrict output or sales volume or divide markets if such agreements affect prices. This may suggest that NDRC has responsibility for any agreements that affect price, even indirectly. If so, substantial overlaps between NDRC's and SAIC's areas of responsibility are likely.

As with MOFCOM's and SAIC's draft rules, the Draft Anti-Pricing Monopoly Rules raise a number of concerns. For example, Article 5 indicates that "concerted action" can be evidenced by "consistent" pricing conduct and communications between businesses. It is unclear if both elements must be satisfied to find concerted action. It is also unclear what exactly constitutes "consistent" behavior. In addition, the draft states that NDRC will consider whether the alleged consistent behavior has a legitimate justification. As written, however, it appears that consistent behavior may raise a presumption of illegality that must be rebutted by the parties. Inferring coordination based on consistent pricing may chill a company's ability to respond rationally and unilaterally to pricing competition from its rivals. Moreover, it is unclear whether all of the price-related agreements referenced above are prohibited regardless of their impact on consumers.

Moreover, similar concepts receive differing treatment in the draft NDRC and SAIC rules. For example, the Draft Anti-Pricing Monopoly Rules define "anti-competitive agreement" and "coordinated practice" differently from the definition of "anti-competitive agreement" and "acts of collaboration" in the Draft Restrictive Agreement Rules. These differences could result in confusion and complicate companies' compliance efforts.

In spite of the publication of the Draft Anti-Pricing Monopoly Rules, one of the main disappointments of the first year of the AML is the lack of guidance from NDRC regarding price-related anti-competitive agreements, in particular cartels. Cartels are generally viewed as the most serious violations that antitrust laws are intended to prevent. Similarly, it is striking that NDRC has not proposed the adoption of a leniency regime comparable to that established by SAIC.

B. ABUSES OF DOMINANT POSITIONS

1. Non-Price Related Conduct

a. Regulatory Framework

As mentioned above, on June 5, 2009, SAIC adopted the Investigation and Handling Rules and the Prohibition Rules.[7] In addition, on April 27, 2009, SAIC published the draft Rules on Prohibition of Abuse of Dominant Market Positions (the "Draft Dominance Rules"), which define a dominant market position and provide further detail regarding the acts that might be considered an abuse of a dominant position.

The AML defines a "dominant market position" as a "market position in which an undertaking has the ability in the relevant market to control the price or quantity of products, or other transactional terms regarding products, or to impede or affect other undertakings' ability to enter the relevant market." The Draft Dominance Rules clarify the phrases "other transactional terms" and "ability to impede or affect other undertakings' ability to enter the relevant market":

- "Other transactional terms" include "factors other than price and quantity of products that may materially affect market transactions, such as product quality, payment conditions, delivery methods, and after-sale services, *etc*."

- "The ability to impede or affect other undertakings' ability to enter the relevant market" refers to "the ability to exclude from or delay entry into the relevant market by other undertakings in reasonable time or increase considerably the costs of entry into the relevant market by other undertakings such that they cannot effectively compete with the incumbent undertakings."

The Draft Dominance Rules provide further guidance with regard to the AML's non-exhaustive list of factors used to determine whether a company holds a dominant market position:

- Market share and the "competitive situation":

    - With respect to market shares, the Draft Dominance Rules restate the AML's rebuttable presumptions of market dominance.[8]

---

[7] For a detailed review of the relevant rules, please refer to our alert memo of June 18, 2009, which may be found at: http://www.cgsh.com/saic_issues_rules_under_the_chinese_anti-monopoly_law/.

[8] A dominant market position is presumed when the market share of one company reaches one-half of the relevant market, the aggregate market share of two companies reaches two-thirds of the relevant market (except for companies having a market share of less

- The "competitive situation" includes such factors as the level of development of the relevant market, the number of existing competitors, the existence of potential competitors and barriers to entry, market shares of other companies, the degree of product differentiation, and market transparency. Factors relevant to barriers to entry include rules affecting market access, the role of networks and other necessary facilities, sales channels, capital requirements, technological requirements, economies of scale, and cost advantages.

- Upstream and downstream markets: The degree to which the company in question controls sales channels or raw material supplies, including its ability to affect or determine price, quantity, contract terms or other transactional terms, or to acquire raw materials on a preferential basis.

- Financial and technological strength: The company's assets, financial condition, profitability, access to financing, research and development capabilities, technical equipment, and intellectual property rights.

- Dependency of other companies: Relevant factors include the volume of other companies' transactions with the allegedly dominant company, the duration of the relationship, and the difficulty with which counterparties can switch to an alternative counterparty.

The prohibited practices include: (i) refusals to deal (reducing, restricting or terminating current transactions with counterparties or refusing to engage in new transactions with counterparties without justifiable reason); (ii) exclusive dealing (a dominant company is prohibited from restricting its counterparty to trade only with it or with a company designated by it without justifiable reasons); (iii) violations of the essential facilities doctrine (a dominant company may not deny other companies the use of necessary networks or other facilities under reasonable terms, if the other company cannot otherwise commence operations); (iv) tying and bundling (dominant companies, without justifiable reason, may not impose "bundled sales" or other unreasonable trade terms, such as conditioning a sale upon the counterparty's purchase of other products or promise not to purchase from other companies); and (v) the imposition of discriminatory sales terms in equivalent transactions.

Although welcome, the Draft Dominance Rules leave many questions unanswered. In particular, the Draft Dominance Rules do not sufficiently stress the need to show actual or likely anti-competitive effects of abusive practices – harm to

---

than one-tenth of the relevant market), or the aggregate market share of three companies reaches three-quarters of the relevant market (except for companies having a market share of less than one-tenth of the relevant market).

consumers by way of a reduction in the number of competitors, amount of innovation, foreclosure of reasonably efficient competitors, *etc.*

In addition, SAIC's form-based approach may raise particular issues in an area that has been controversial in the U.S. and the EU in recent years; the interface between the abuse of dominance rules and intellectual property rights. It would be useful, for example, if the Draft Dominance Rules had addressed the circumstances in which dominant companies may be required to grant patent licenses or provide interoperability information to competitors. We understand that SAIC are developing guidelines on enforcement of the AML in the field of intellectual property rights.

Although the Draft Dominance Rules provide that a dominant company may defend conduct that would otherwise violate the AML based on "justifiable reasons" for its conduct, the rules apparently place the burden of proof on the dominant company while offering no guidance on what justifications SAIC will consider in different scenarios and the nature of the evidence that dominant companies will be required to provide.

b. Implementation

Nation-wide, administrations for industry and commerce in the first quarter of 2009 have investigated 76 cases regarding (i) limiting fair competition by public utilities undertakings and undertakings with dominant positions granted by the law, and (ii) abuses of administrative powers. However, such investigations were conducted under the Anti-Unfair Competition Law rather than the AML. SAIC also received a large number of complaints (probably including not only non-price related abuse of dominant positions but also non-price related restrictive agreements) under the AML, but so far it has apparently not adopted any decisions, or even publicly launched formal investigations, under the AML. The AML does not seem to oblige SAIC to publish its decisions (whether on abuses of dominant positions or non-price related restrictive agreements), contrary to MOFCOM's obligation to publish conditional merger control clearances and prohibitions.

On the other hand, a number of private suits alleging defendants' abuses of dominant positions have been filed in Chinese courts. Two notable cases are Tangshan Renren Information Services v. Baidu Network Technology Co. ("Baidu") and Mr. Li Fangping v. Beijing Branch of China Netcom ("Beijing Netcom").

On April 22, 2009, the Beijing No. 1 Intermediate People's Court heard one of the first cases based on a private action alleging abuse of a dominant position under the AML. Tangshan alleges that Baidu, the most frequently used search engine in China, abused its dominant position in web search by deliberately lowering Tangshan's ranking on searches to negotiate a higher payment from it. Baidu argued that it is not dominant

and that it has not engaged in any abuse. Tangshan also filed complaints against Baidu with SAIC as early as October 2008.

On June 25, 2009, the Beijing No. 2 Intermediate People's Court heard arguments in the Beijing Netcom case. Mr. Li Fangping alleges that Beijing Netcom abused its dominant position in fixed-line telephone services by offering different programs to and charging higher rates to non-Beijing residents. Beijing Netcom argued that it does not have a dominant share.

Both cases will be closely watched, not least in view of the prominence of the defendants, one a state-owned enterprise and the other a champion of China's developing technology sector. In addition, the Supreme People's Court is working on an interpretation regarding civil cases under the AML.

2. Price-Related Conduct

a. Regulatory Framework

NDRC's Draft Anti-Pricing Monopoly Rules provide further detail regarding the definition of a dominant position, the types of conduct that may constitute an abuse, and the circumstances in which a dominant firm may be able to justify its otherwise abusive behavior. Consistent with the AML, predatory pricing, refusals to deal, "unfairly high" or "unfairly low" pricing, and price discrimination are prohibited.

In Articles 12 and 13, the Draft Anti-Pricing Monopoly Rules elaborate on the AML's prohibitions against selling at unfairly high prices, purchasing at unfairly low prices, and predatory pricing. Article 12, regarding unfairly high or low prices, lists a variety of factors for NDRC to consider, including whether the price is "obviously" higher or lower than the cost of the product, whether an increase or decrease in price is beyond "normal" levels, whether a price increase or decrease is obviously inconsistent with a change in cost, and whether the price is obviously different from the price of similar products offered by other companies. While cost is a relevant benchmark in both Articles 12 and 13, neither article defines the term nor clarifies which measures of cost apply.

Notably, Article 13 lists several possible justifications for below-cost pricing, including selling perishable or seasonal products at a discount prior to expiration, bankruptcy or going-out-of-business sales, short-term promotions to attract customers, matching competitors' prices, and taking advantage of economies of scale to reduce costs resulting in benefits to consumers. The first two justifications are in line with relevant provisions of China's Anti-Unfair Competition Law regarding below-cost selling.

Articles 12 and 13 will likely be difficult to implement, as it is hard to determine whether prices are "normal" or "reasonable", or whether low prices are "predatory"

based on objective factors, and the draft rules lack a requirement that NDRC make a finding that challenged pricing by a dominant company resulted in harm to consumers.

Article 14 expands on prohibited refusals to deal and states, "Undertakings with dominant market positions are prohibited from refusing in disguise to deal with a trading counterparty by setting unfairly high or low prices without any justifiable reasons." It goes on to define "unfairly high or low prices" to mean "the trading counterparty cannot attain normal profit after normal production and sale if the commodities are sold at such prices." First, it is surprising that a refusal to deal falls within NDRC's jurisdiction, as it is typically considered a non-price restraint that would normally fall under SAIC's jurisdiction. Second, basing the definition on the subjective notion of "normal profit" will likely result in uncertainty and confusion. It will also likely prove extremely difficult for one party to be able to predict another's profit margin, much less determine whether such profit is "normal."

As with SAIC's Draft Dominance Rules, the Draft Anti-Pricing Monopoly Rules do not clearly indicate that a finding of consumer harm is required to establish an abuse of dominance. Unlike cartel behavior, which is generally recognized to result in harm to consumers regardless of any alleged justification, an abuse of a dominant position is often accompanied by pro-competitive justifications and benefits. It is unclear if NDRC will balance pro-competitive benefits against perceived harms when investigating allegedly prohibited conduct.

b. Implementation

As is the case of anti-competitive agreements, NDRC has so far apparently not taken any formal action in regard to price-related abuse of dominant positions. Like SAIC, NDRC is not obliged to publish its decisions. Some reports indicate, however, that NDRC has begun an investigation regarding the pricing practices of the Civil Aviation Administration of China's ticketing website, TravelSky. NDRC received tips accusing TravelSky of fixing the prices of airline tickets by manipulating its discounting policies. TravelSky is a State-owned business that, among other things, issues tickets for the major airlines. Its major shareholders are State-owned airline companies.

C. ISSUES

As noted, neither SAIC nor NDRC have published decisions, or even apparently launched formal investigations, regarding violations of the AML within their areas of jurisdiction. It is thus premature to comment on SAIC's and NDRC's approach to enforcing the AML. On the other hand, several cases are pending before the Chinese courts, and the outcome of these cases will be closely watched.

With respect to the regulatory framework, SAIC and NDRC have published several draft and final rules, including SAIC's and NDRC's draft rules on assessing restrictive agreements and abuses of dominant positions and SAIC's final procedural rules. These rules provide welcome guidance, but a number of ambiguities remain.

1. Shared Jurisdiction and Consistency

Jurisdiction over cases regarding anti-competitive agreements and abuse of dominant positions is shared by SAIC and NDRC. Given the potential for overlapping jurisdiction, consistency between the agencies' rules and practice will be critical. The published draft rules are inconsistent in several respects, including the concepts of "anti-competitive agreements" and "coordinated practice."

NDRC's draft rules published in August 2009 created a further potential for confusion by asserting jurisdiction over restrictive agreements that affect pricing only indirectly. It would be better clearly to allocate to SAIC cases regarding restricting output or sales volume, dividing up markets and refusal to deal, even though prices may be affected by such violations.

Rules on how to handle cases that involve both price-related conduct and non-price related conduct would be welcome on questions such as which agency will take the lead in what types of cases, how SAIC and NDRC will cooperate with one another, and how the decision-making process will work in practice.

2. *Per Se* v. Rule-of-Reason

As mentioned above, both SAIC's and NDRC's rules fail clearly to distinguish between cases that are prohibited *per se* and those that should be assessed under a rule-of-reason. Experience in the U.S. and EU shows that p*er se* prohibitions should be limited to situations like price fixing, output restriction, and market/customer sharing. For the remaining cases, rule-of-reason is a preferable approach, in particular for cases regarding abuses of dominant positions. It would be useful for implementing measures to emphasize the need for the agencies to show likely anti-competitive effects, to apply economic analyses on a case-by-case basis, and to address the analysis of possible justifications.

In particular, it would be helpful for SAIC's and NDRC's rules to stress the need to prove consumer harm before prohibiting allegedly restrictive agreements, particularly in the case of vertical agreements, which are normally pro-competitive. Similar issues arise in SAIC's and NDRC's proposed rules on abuses of dominant positions, which arguably take an excessively formalistic approach in areas such as the "essential facilities doctrine" and the treatment of intellectual property rights.

IV. CONCLUSION

The AMEAs have made impressive progress during the AML's first year of application in developing the regulatory framework for their respective activities, publishing numerous final and draft rules, regulations and guidelines. In the coming months, we anticipate that the AMEAs will release final versions of several of these drafts and publish a number of additional drafts, including notably SAIC's substantive rules on restrictive agreements and abuse of dominant positions, and guidelines on the enforcement of the AML in the area of intellectual property rights. These rules should help clarify existing ambiguities and fill a number of holes, including a leniency regime for price-fixing.

The AMEAs' progress in developing guidance on the substantive application of the AML is so far less impressive. MOFCOM has published three merger decisions, all of which have been criticized in the United States and the EU. SAIC and NDRC have so far not published any decisions nor even (as far as they have indicated) launched any formal investigations under the AML, even though numerous complaints have reportedly been filed. In fairness, however, regulators in other jurisdictions have developed their bodies of precedents over many years. Moreover, a number of private antitrust cases are working their way through the Chinese courts. These cases will be closely watched not only for their intrinsic interest, but also as a sign of whether private litigation may play a larger role in the early development of Chinese antitrust law (outside the merger area) than enforcement activities by the AMEAs.

Many U.S. and European observers have expressed concern that the AML will be used to further industrial policy goals or nationalist sentiments unrelated to antitrust law. At this stage, it is too early to tell if such fears are justified. On the one hand, the AML and the published rules and guidelines are largely consistent with international antitrust norms. On the other hand, the AML and the draft and final rules and guidelines are, perhaps purposefully, quite vague and leave significant discretion to the AMEAs. As noted, MOFCOM's three publicly available merger review decisions do little to allay the concerns, and the co-existence of requirements for merger control filing, national security filing and national economic security filing by foreign investors that acquire certain domestic enterprises raises more ambiguity.

The AMEAs have accomplished a great deal in a year's time. The coming year should help to remove some of the existing uncertainty regarding procedural framework and provide further guidance on the AMEAs' enforcement of the AML.

* * *

For additional information, please do not hesitate to contact Stephan Barthelmess, Brian Byrne, Christopher Cook, Maurits Dolmans, Thomas Graf, Francisco Enrique González-Díaz, Nicholas Levy, James Modrall, Till Müller-Ibold, Robbert Snelders, Romano Subiotto, John Temple Lang, Dirk Vandermeersch, or Antoine Winckler of the Firm's Brussels office (+32 2 287 2000); Mario Siragusa, Marco D'Ostuni, or Giuseppe Scassellati-Sforzolini in Rome (+39 06 69 52 21); Dirk Schroeder or Romina Polley in Cologne (+49 221 800 400); François Brunet in Paris (+33 1 40 74 68 00); Shaun Goodman in London (+44 20 7614 2200); Leah Brannon, Jeremy Calsyn, George Cary, David Gelfand, Michael Lazerwitz, Mark Leddy, Mark Nelson, or Matt Slater in Washington, DC (+1 202 974 1500); Matthew Bachrack in Hong Kong (+852 2521 4122); or Filip Moerman in Beijing (+86 10 5920 1000).

CLEARY GOTTLIEB STEEN & HAMILTON LLP

AML Related Regulations, Rules and Guidelines

Fields	Rules	Issuer(s)	Date Issued
General	Guidelines on the Definition of the Relevant Market	AMC	5/2009
Merger Control	Regulation on Notification Thresholds of Concentrations between Undertakings	State Council	8/2008
	Guidelines on Notification of Concentrations between Undertakings	MOFCOM	1/2009
	Guidelines on Notification Documents and Materials for Concentrations between Undertakings	MOFCOM	1/2009
	Guidelines on Merger Control Review of Concentrations between Undertakings	MOFCOM	1/2009
	Flowchart for Merger Control Review of MOFCOM on Concentrations between Undertakings	MOFCOM	1/2009
	Rules on Acquisition of Domestic Enterprises by Foreign Investors	MOFCOM	6/2009 (effective as of 22/6/2009)

Fields	Rules	Issuer(s)	Date Issued
	Rules on the Calculation of Turnover for the Prior Notification of Concentrations of Undertakings in the Financial Industry	MOFCOM, PBC, CBRC, CSRC, and CIRC	7/2009 (effective as of 15/8/2009)
	Draft Provisional Rules on the Notification of Concentrations between Undertakings	MOFCOM	Released for comment 1/2009
	Draft Provisional Rules on the Review of Concentrations between Undertakings	MOFCOM	Released for comment 1/2009
	Draft Provisional Rules on Investigation and Handling of Concentrations between Undertakings that are not Legally Notified	MOFCOM	Released for comment 1/2009
	Draft Provisional Rules on the Collection of Evidence regarding Concentrations between Undertakings Below Thresholds, but Suspected of Being Anti-Competitive	MOFCOM	Released for comment 1/2009
	Draft Provisional Rules on Investigation and Handling of Concentrations between Undertakings Below Thresholds but Suspected of Being Anti-Competitive	MOFCOM	Released for comment 2/2009

Fields	Rules	Issuer(s)	Date Issued
Restrictive Agreements	Procedural Rules on Investigating and Handling Cases of Restrictive Agreements and Abuse of Market Dominance by the Administrative Authority of Industry and Commerce	SAIC	6/2009
	Draft Rules on Prohibition of Restrictive Agreements	SAIC	Released for comment 4/2009
	Draft Rules on Anti-Pricing Monopoly	NDRC	Released for comment 8/2009
Abuses of Dominant Market Positions	Procedural Rules on Investigating and Handling Cases of Restrictive Agreements and Abuse of Market Dominance by the Administrative Authority of Industry and Commerce	SAIC	6/2009
	Draft Rules on Prohibition of Abuse of Dominant Market Positions	SAIC	Released for comment 4/2009
	Draft Rules on Anti-Pricing Monopoly	NDRC	Released for comment 8/2009

CLEARY GOTTLIEB

Office Locations

BRUSSELS
Rue de la Loi 57
1040 Brussels, Belgium
32 2 287 2000
32 2 231 1661 Fax

NEW YORK
One Liberty Plaza
New York, NY 10006-1470
1 212 225 2000
1 212 225 3999 Fax

WASHINGTON
2000 Pennsylvania Avenue, NW
Washington, DC 20006-1801
1 202 974 1500
1 202 974 1999 Fax

PARIS
12, rue de Tilsitt
75008 Paris, France
33 1 40 74 68 00
33 1 40 74 68 88 Fax

LONDON
City Place House
55 Basinghall Street
London EC2V 5EH, England
44 20 7614 2200
44 20 7600 1698 Fax

MOSCOW
Cleary Gottlieb Steen & Hamilton LLP
CGS&H Limited Liability Undertaking
Paveletskaya Square 2/3
Moscow, Russia 115054
7 495 660 8500
7 495 660 8505 Fax

FRANKFURT
Main Tower
Neue Mainzer Strasse 52
60311 Frankfurt am Main, Germany
49 69 97103 0
49 69 97103 199 Fax

COLOGNE
Theodor-Heuss-Ring 9
50668 Cologne, Germany
49 221 80040 0
49 221 80040 199 Fax

ROME
Piazza di Spagna 15
00187 Rome, Italy
39 06 69 52 21
39 06 69 20 06 65 Fax

MILAN
Via San Paolo 7
20121 Milan, Italy
39 02 72 60 81
39 02 86 98 44 40 Fax

HONG KONG
Bank of China Tower
One Garden Road
Hong Kong
852 2521 4122
852 2845 9026 Fax

BEIJING
Twin Towers – West
12 B Jianguomen Wai Da Jie
Chaoyang District
Beijing 100022, China
86 10 5920 1000
86 10 5879 3902 Fax