

China Antitrust Review 2018

January 31, 2019

2018 marked the tenth anniversary of China's Anti-Monopoly Law ("**AML**"). Over the course of the past decade, Chinese antitrust has diverged at times from antitrust enforcement in the U.S. and Europe, with a more bureaucratic framework, more uncertain timelines, a legal standard that involves both competition policy and trade policy, and remedies that U.S. and European authorities have generally not accepted.

The past year saw little change in the substance of Chinese enforcement, but potentially significant changes in the enforcement process. For companies with potential antitrust exposure in China, there are three key takeaways from 2018:

- First, as a matter of process, China has created a more streamlined bureaucratic structure, replacing a complex tripartite structure with a single antitrust authority. The restructuring does not assure parties of quicker investigations, however. Despite a more efficient structure, China has signaled that it will still undertake detailed reviews of large transactions, particularly those involving key industrial policy areas.
- Second, U.S. and European authorities disfavor the use of conduct commitments (behavioral remedies) in horizontal cases, and recently the U.S. has rejected the use of behavioral remedies even in vertical cases. (Indeed, the U.S. rejected such remedies in deciding to challenge the AT&T/Time Warner transaction.) In contrast, China has made no such shift away from behavioral remedies.
- Third, most antitrust laws around the globe are founded on principles of protecting competition. China's AML, however, explicitly directs antitrust authorities also to consider Chinese national economic development alongside competition principles. Enforcement in 2018 shows no evidence of moving away from trade policy concerns in antitrust decisions.

Below, we survey the key developments in China's agency reorganization and its enforcement decisions.

I. Establishment of a Single Antitrust Agency

Early in 2018, China replaced its decade-long tripartite antitrust enforcement system (consisting of the Ministry of Commerce ("**MOFCOM**"), the National Development and Reform Commission ("**NDRC**"), and the State Administration for Industry and Commerce ("**SAIC**") with a unified antitrust enforcement agency: the State Administration for Market Regulation ("**SAMR**"). (Previously, MOFCOM had been responsible for merger review, NDRC investigated price-related conduct, and SAIC investigated non-price-related conduct.) While SAMR's institutional framework is still under development, the Anti-Monopoly Bureau ("**AMB**") within SAMR has taken on the responsibilities previously divided among MOFCOM, NDRC, and SAIC.

We expect SAMR to continue the recent trend toward faster and more efficient merger review. Since May 2018, it has accepted formal merger notifications and unconditionally cleared the majority of transactions, including those it inherited from MOFCOM. It has generally taken SAMR one to two months to clear simple cases, and in its first quarter, SAMR took an average of 17 days to clear a transaction submitted under the fast-track process. These averages represent a substantial improvement over the timelines of its predecessor agency.

Despite this trend of quicker review, SAMR has still closely scrutinized sectors that appear to be of strategic trade interest to China as well as deals posing potential competition concerns.

Beyond substantive review of mergers, SAMR has also continued the efforts of its predecessor agency to sanction parties for breaching their notification obligations under the AML. To date, SAMR has only issued financial penalties and has yet to unwind any unreported transactions.

Finally, another notable development is that SAMR has divided its jurisdiction between itself and its provincial units. While SAMR handles trans-regional cases, including cases that are complex or likely to have a major national impact, it authorizes its provincial units to carry out antitrust law enforcement activities within their administrative regions, focusing on cases involving monopoly agreements, abuse of market dominance, and abuse of administrative power. The provincial units of SAMR handle most local cases in their own name but report controversial cases to SAMR for consultation.¹

II. Merger Control

A. Merger Control Decisions

During the past year, SAMR imposed remedies in four transactions and failed to issue a ruling in another transaction, leading to the deal's demise.

Qualcomm/NXP

On October 27, 2016, Qualcomm Inc. ("**Qualcomm**") announced an agreement to acquire Netherlands-based NXP Semiconductors N.V. ("**NXP**") in a \$44 billion deal that would join the companies' largely complementary product portfolios. In July 2018, Qualcomm called off the deal, paying NXP a \$2 billion termination fee after Chinese regulators did not issue a ruling on the transaction following over 20 months of review. At the time, eight other jurisdictions, including the United States, had approved the proposed deal.² In coverage of the deal, analysts speculated that MOFCOM/SAMR's lengthy review was the result of a trade war between Washington, D.C. and Beijing over issues such as tariffs on Chinese goods and the U.S. ban on ZTE buying components from American companies.³

Bayer/Monsanto

In March 2018 (prior to the SAMR reorganization), MOFCOM imposed structural and behavioral conditions on the acquisition of Monsanto Co. ("**Monsanto**") by Bayer Ag ("**Bayer**").⁴

China raised concerns of anticompetitive harms in four areas, which are similar to areas of concern found by authorities in Europe and the U.S.: (1) the Chinese market for non-selective herbicide; (2) the Chinese market for various vegetable seeds; (3) the global markets for corn, soybean, cotton and rapeseed traits; and (4) the global market for digital agriculture. Authorities' concerns arose primarily from the parties having combined shares well above other competitors and from the low likelihood of entry by others in these areas, resulting in a risk of market power and the ability to tie products. Of particular note, the Chinese authorities raised concerns about preserving innovation competition in the digital agriculture

¹ Announcement of the State Administration for Market Regulation [2018] No. 265: Announcement of the State Administration for Market Regulation to Authorize its Provincial Units to Carry Out Antitrust Law Enforcement Activities (January 3, 2019), available at http://samr.saic.gov.cn/xw/yw/wjfb/201901/t20190103_279720.html (Chinese language).

² Don Clark, Qualcomm Scraps \$44 Billion NXP Deal After China Inaction, NY Times, July 25, 2018, <https://www.nytimes.com/2018/07/25/technology/qualcomm-nxp-china-deadline.html>.

³ Qualcomm/NXP: As Deal End Date Approaches, SAMR Decision Poised for Key Impact on U.S.-China Trade, Telecom Tensions, The Capitol Forum, July 20, 2018, <https://library.thecapitolforum.com/docs/2ayx0p20xn9e>.

⁴ Announcement of the Ministry of Commerce [2018] No. 31: Announcement of the Anti-Monopoly Review Decision to Approve, with Restrictive Conditions, the Concentration of Undertakings in Respect of the Acquisition of Monsanto Company by Bayer Aktiengesellschaft (March 13, 2018), available at <http://fdj.mofcom.gov.cn/article/ztxx/201803/20180302719123.shtml> (Chinese language).

space, where Bayer and Monsanto are both particularly strong. Global authorities have become increasingly concerned about preserving R&D/innovation competition, and China's concerns about innovation reflect similar concerns in Europe and the U.S. While China imposed various divestitures to address these concerns, however (as other global authorities did), it also took a more unusual step of requiring the merged firm to give Chinese agricultural application developers access to Bayer's digital agriculture platform—a remedy that appears particularly designed not just to preserve competition but to benefit local Chinese competitors.

Essilor/Luxottica

In July 2018, SAMR imposed a number of behavioral remedies on the merger of Essilor International (“**Essilor**”) and Luxottica Group S.p.A. (“**Luxottica**”), two of the largest companies in the optical industry.⁵

SAMR raised concerns that the combined market shares of Essilor and Luxottica were high enough to result in the elimination and/or restriction of competition post-transaction in the Chinese wholesale and local retail markets for optical lenses, optical frames, and sunglasses. While U.S. and European regulators approved the transaction after finding that the companies sold mainly complementary products and would not have enough market power to engage in vertical foreclosure, SAMR required behavioral remedies that would address the potential vertical effects of the transaction—and do so in a way to benefit Chinese retail firms. For example, SAMR required the combined company to refrain from tie-in sales of glasses products absent justifiable reasons; to avoid exclusivity conditions on Chinese glasses retailers; and to supply all frame and sunglasses products and offer necessary trademark licensing to Chinese glasses retailers on fair, reasonable, and nondiscriminatory (“**FRAND**”) terms.

Linde/Praxair

In September 2018, SAMR imposed structural and behavioral conditions on the merger of Linde AG (“**Linde**”) and Praxair, Inc. (“**Praxair**”).⁶

Similar to other antitrust authorities, China raised concerns that the merger between Linde and Praxair would eliminate and/or restrict competition in a number of industrial gas product markets, such as the global markets for helium and the local markets for liquid oxygen and nitrogen. According to SAMR, these markets offer few alternative suppliers and pose high barriers to entry and, as a result, the proposed merger would likely reduce consumers' bargaining power and strengthen the combined companies' control of the markets.

SAMR, like the Federal Trade Commission (“**FTC**”) in the U.S. and the European Commission (“**EC**”), approved the merger of Linde and Praxair subject to the divestiture of numerous assets. Unlike the FTC and EC, however, SAMR also imposed a number of behavioral remedies, including the requirements that the combined company assist buyers of divested helium assets in transporting the gas to China for processing and sale, and supply certain rare gas mixtures to China at a reasonable price and in a timely and stable manner.

⁵ Announcement of the State Administration for Market Regulation [2018]: Announcement of the Anti-Monopoly Review Decision to Approve, with Restrictive Conditions, the Concentration of Undertakings in Respect of the merger of Essilor International Compagnie Generale D Optique SA and Luxottica Group S.p.A. (July 25, 2018), available at http://samr.saic.gov.cn/gg/201807/t20180726_275250.html (Chinese language).

⁶ Announcement of the State Administration for Market Regulation [2018]: Announcement of the Anti-Monopoly Review Decision to Approve, with Restrictive Conditions, the Concentration of Undertakings in Respect of the merger of the merger of Linde AG and Praxair, Inc. (September 30, 2018), available at http://samr.saic.gov.cn/gg/201809/t20180930_276188.html (Chinese language).

Rockwell Collins/UTC

In November 2018, SAMR imposed both structural and behavioral conditions on the acquisition of Rockwell Collins Inc. (“**Rockwell Collins**”) by United Technologies Corporation (“**UTC**”).⁷ SAMR raised concerns that the acquisition would eliminate and/or restrict competition in the global markets for trimmable horizontal stabilizer actuators (“**THSAs**”), throttle quadrant assemblies, rudder brake pedal systems, and pneumatic wing ice protection systems among other products. SAMR, like the U.S. Department of Justice, required the combined entity to divest businesses related to THSAs and SMR technology, among others. SAMR, however, uniquely imposed a conduct commitment requiring the combined entity to refrain from tie-in sales or bundling absent justifiable reasons.

B. Penalties for Reporting Violations

Like MOFCOM before it, SAMR has authority to penalize parties who fail to comply with the reporting obligations stipulated in the AML, either by imposing a fine up to RMB500,000 (approximately US\$73,000) and/or by unwinding an unreported transaction. While SAMR has not exercised the latter authority, it has proposed to increase the penalty for merger notification violations, potentially up to 1%-10% of a violating company’s revenue in the previous year.⁸

In the past year, SAMR strengthened its enforcement efforts on gun-jumping and imposed penalties on 12 transactions, compared to nine in 2017. The fines ranged from RMB150,000 (approximately US\$22,000) to RMB300,000 (approximately US\$44,000). All else being equal, SAMR typically issues a larger fine for what it deems to be intentional disregard of reporting obligations and a smaller fine if the relevant parties take remedial actions and cooperate in SAMR’s investigation. Of the 12 transactions during this past year, over half of them involved foreign parties, and the businesses of these fined parties involved multiple industries, including papermaking, real estate, engineering, and chemical and raw materials.

III. NDRC/SAMR Enforcement Actions

The NDRC, China’s antitrust agency for price-related conduct prior to the consolidation of SAMR, continued its enforcement efforts in the medical and shipping industries, with numerous fines—including against Chinese companies. Fines vary, but have often been in the range of 4% of the prior year’s sales.

As in 2017, the NDRC/SAMR pursued enforcement actions in the Chinese medical industry. In December 2018, SAMR fined Chengdu Huayi Pharmaceutical Excipients Manufacturing (“**Chengdu Huayi**”), Sichuan Jinshan Pharmaceutical (“**Sichuan Jinshan**”), and Taishan Xinning Pharmaceutical (“**Taishan Xinning**”) for price-fixing in the acetic acid active pharmaceutical ingredients (“**APIs**”) market. In addition to confiscation of illegal gains, SAMR imposed a fine of RMB1,427,700 (approximately US\$208,000), RMB2,060,500 (approximately US\$300,000) and RMB2,763,400 (approximately US\$403,000) of Chengdu Huayi, Sichuan Jinshan, and Taishan Xinning, each amounting to 4% of the companies’ sales in the acetic acid APIs market in 2017, respectively.⁹ Similarly, at the end of December 2018, SAMR

⁷ Announcement of the State Administration for Market Regulation [2018]: Announcement of the Anti-Monopoly Review Decision to Approve, with Restrictive Conditions, the Concentration of Undertakings in Respect of the acquisition of Rockwell Collins Inc. by United Technologies Corporation (November 23, 2018), available at http://samr.saic.gov.cn/gg/201811/t20181123_277177.html (Chinese language).

⁸ SAMR Policy: China’s New Antitrust Regime to be Fully Functional by Early September, Merger Enforcers Set to Lead Integrated Agency, The Capitol Forum (Aug. 7, 2018), <https://library.thecapitolforum.com/docs/2ccxe3xr0f06>.

⁹ The State Administration for Market Regulation Published Administrated Penalty Decisions on the API Manufacturing Price-Fixing Case (市监局发布冰醋酸原料药垄断按行政处罚决定书) (December 24, 2018), available at http://samr.saic.gov.cn/gg/201812/t20181224_278969.html (Chinese language).

confiscated the illegal gains and imposed fines in an aggregate amount of RMB12.43 million (approximately US\$1.81 million) against Hunan Er-Kang Medical Operation and Henan Jiushi Pharmaceutical, with such fine amounting to 8% and 4% of their respective annual sales in 2017, for abuse of dominance in the domestic market for chlorpheniramine maleate APIs.¹⁰

During 2018, NDRC/SAMR also pursued enforcement actions in the Chinese shipping industry. In June 2018, SAMR fined four Shenzhen tugboat companies for price-fixing totaling RMB12.86 million (approximately US\$1.88 million), amounting to 4% of their sales in 2017. The four companies involved were competitors near the Port of Shenzhen, operating in different port areas, and in early 2010, the companies agreed to raise their service charge.¹¹ Around the same time, SAMR also fined China United Tally Shenzhen (“**China United**”) and China Ocean Shipping Tally Shenzhen (“**China Ocean**”) a total of RMB3,163,108 (approximately US\$462,000) for entering into a monopoly agreement that divided sales and service locations among the companies.¹² In July 2018, Tianjin Municipal Development and Reform Commission (“**Tianjin DRC**”) issued a fine totaling approximately RMB50 million (approximately US\$7.30 million) on 23 local container yard operators for entering into and implementing monopoly agreements that significantly raised the container handling comprehensive charges and unloading fees. Later in November 2018, Tianjin DRC imposed another fine of RMB45.1 million (approximately US\$6.58 million) on 17 local container yard operators for forming and implementing price-fixing agreements.¹³

IV. Conclusion

2018 saw a significant change in the structure of Chinese antitrust agencies with the restructuring of the former tripartite regime into a single antitrust agency in the State Administration for Market Regulation. This development could streamline the process for obtaining antitrust approval in China. With that said, it appears that SAMR will continue to undertake detailed reviews of large transactions and transactions of strategic importance to China.

2018 also reflected China’s preference for behavioral over structural remedies when granting merger approvals—and its application of these remedies in a manner that protects Chinese firms in particular. In multiple instances, China was the only jurisdiction that required companies to implement various behavioral remedies in order to obtain merger approval. These dynamics suggest that, despite recent trends in other jurisdictions, there is no sign of a shift in approach to Chinese antitrust enforcement.

¹⁰ News Release of State Administration for Market Regulation on Penalty against Manufacturers of Chlorpheniramine Maleate APIs (January 2, 2019) *available at* http://samr.saic.gov.cn/xw/yw/xwfb/201901/t20190102_279577.html (Chinese language).

¹¹ The State Administration for Market Regulation Published Administrated Penalty Decisions on Four Shenzhen Tugboat Companies over Price-Fixing (市监总局发布对深圳4家拖轮公司的行政处罚决定书) (June 25, 2018) *available at* http://samr.saic.gov.cn/gg/201806/t20180625_274741.html (Chinese language).

¹² The State Administration for Market Regulation Published Administrated Penalty Decisions on Two Shenzhen Tally Companies over Price-Fixing (市监总局发布对深圳2家理货公司的行政处罚决定书) (July 20, 2018) *available at* http://samr.saic.gov.cn/gg/201807/t20180720_275163.html (Chinese language).

¹³ Tianjin Municipal Development and Reform Commission: Announcement of Administrative Penalty Decision [2018] (天津市发展和改革委员会价格行政处罚决定), *available at* http://fzgg.tj.gov.cn/zw/gk/wjgl/jgxzcfjd/index_1.shtml (Chinese language).

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