

China Antitrust Review 2019

January 31, 2020

Last year marked the eleventh anniversary of China's Anti-Monopoly Law (the "**AML**"). In 2019, China announced the first-ever set of proposed amendments to the AML as well as the introduction of several new regulations aimed at more transparency and efficiency in antitrust enforcement and codifying noteworthy deviations between Chinese and United States and European Union antitrust laws.

In the past year, the State Administration for Market Regulation ("**SAMR**") approved five transactions with conditions (i.e., remedies), a slight uptick from four in 2018. The average review time for these five transactions was approximately one year. SAMR did not block any transactions in 2019. While SAMR reviews of significant transactions continue to be lengthy, reviews for more straightforward transactions—which comprise the vast majority of transactions reviewed by SAMR—have become quicker and more streamlined, particularly for U.S. companies.

SAMR and its local branches also continued enforcement against various anticompetitive conduct in the raw materials and automotive industries, including market allocation agreements and conditional pricing. Significantly, resale price maintenance ("**RPM**") was an area of continued enforcement focus, as well.

I. Updates to the AML and SAMR Regulations

On January 2, 2020, SAMR released for public comment the first set of official amendments to the AML since it took effect 11 years ago. The proposed amendments implement several revisions to streamline enforcement and bring certain Chinese antitrust laws closer to those in the U.S. and the EU. However, they also highlight key points of differentiation between Chinese and U.S./EU enforcers.

With respect to merger enforcement, the SAMR review clock can be suspended under certain circumstances. The AML amendments, as currently drafted, would suspend the review clock: (i) when agreed upon by the filing parties; (ii) during the period of time the filing parties are submitting supplemental documents or information requested by SAMR; and (iii) during remedy discussions. Suspending the review period can lead to short-term delays, but, overall, may make the review process more efficient by alleviating the need for the merging parties to pull and refile their merger notification if the review exceeds the statutory 180-day maximum review period.

The AML amendments also codify additional factors that can be used to determine whether Internet companies hold a dominant position. With this amendment, Chinese courts would need to consider network effects, economies of scale, lock-in effects, and the ability of these companies to understand and process relevant data. This amendment could lead to increased scrutiny of Internet companies, at the same time that many antitrust authorities across the globe are increasing their scrutiny of tech companies.

There are also several amendments that increase penalties for AML violations, both in the types of remedies and the scope of those remedies. One proposal would give SAMR the authority to impose a fine of up to 10% of the company's previous year's revenue for failing to comply with merger control reporting obligations, instead of the current fixed maximum fine of RMB500,000 (approximately US\$72,000). The amendments also state: "[C]ases that constitute a criminal offence will be met with criminal consequence." It is not clearly indicated what offenses will be criminalized.

The AML amendments contain some notable deviations between Chinese and Western antitrust law. For example, the proposed amendments would prohibit "excessive pricing," in marked contrast to Western jurisdictions that generally do not have an analogous antitrust concept.

In addition, on September 1, 2019, SAMR promulgated three interim AML regulations, intended to streamline and clarify rules for certain anticompetitive conduct.

- **Monopoly Agreements.** The *Interim Regulation Prohibiting Monopoly Agreements* clarifies that horizontal agreements (such as price-fixing, volume restriction, and market allocation agreements) and resale price maintenance will continue to be “per se” unlawful, while all other agreements are to be analyzed under a more flexible “rule of reason” analysis. The rule of reason factors include the facts giving rise to the agreement, the current status of market competition, the parties’ share and control of the market, and the agreement’s impact on the market and consumers.
- **Abuse of Dominance.** The *Interim Regulation Prohibiting Conduct Abusing Dominant Market Positions* clarifies how China determines market dominance. With respect to technology companies, SAMR can consider a variety of factors and models, including business models, user numbers, network effects, foreclosure effects, technological features, market innovation, and data control and processing. The regulation also details what constitutes abusive conduct and potential justifications for such conduct, such as legal requirements, economic efficiency and business development, future investment and innovation, the necessity for such firm’s normal business operations and realizing normal economic return, and benefits to trade counterparties or consumers.
- **Administrative Monopoly.** The *Interim Regulation Preventing Conduct Abusing Administrative Rights to Eliminate or Restrict Competition* defines certain competitive abuses by Chinese government agencies. SAMR can issue guidance and recommendations on how to rectify anticompetitive conduct by government agencies but cannot directly impose sanctions. In a step toward a more open-market system, the regulation targets actions that (i) grant exclusivity for certain producers/service providers or (ii) restrict the free movement of goods, services, and investment in China.

II. Merger Control

A. Merger Control Decisions

The most notable development in Chinese merger enforcement was increased efficiency in clearing simple cases. In 2019, SAMR appeared to issue fewer requests and undertook its reviews more quickly than it had in prior years. This was particularly true for reviews of mergers involving U.S. companies. Some speculated that SAMR acted more efficiently in part to avoid the appearance of delay during U.S.-China trade talks. In contrast, 2018 saw Qualcomm abandon its acquisition of NXP after failing to receive Chinese approval following a 20-month review, which some speculate was driven by trade tensions.¹

It is notable that SAMR did not block any transactions completely in 2019. It is also notable that SAMR continues to rely on a variety of behavioral remedies, such as hold separate agreements, non-discrimination commitments, and “fair pricing” commitments. In contrast, in the U.S., enforcement authorities have become increasingly skeptical of behavioral remedies and have emphasized an increased preference for “structural” remedies (i.e., divestitures).

Complex cases requiring remedies continue to have an extended timeline, however. The five cases requiring a remedy in 2019 took on average approximately one year for review. SAMR remedies also still deviate in meaningful ways from U.S. and EU norms.

¹ Cao Li & Raymond Zhong, *As Qualcomm Deal Is Scrapped, China Denies Trade Link*, N.Y. Times (July 26, 2018), available at <https://www.nytimes.com/2018/07/26/technology/qualcomm-china-trade-war.html>.

KLA/Orbotech

In February 2019, SAMR imposed behavioral remedies on a vertical deal in the semiconductor equipment industry: the acquisition of Orbotech Ltd. (“**Orbotech**”) (which had between 10% and 20% of a special application market and an advanced assembly deposition equipment market) by KLA-Tencor Corporation (“**KLA**”) (which had 50% to 55% of a global process control equipment market).² SAMR was concerned that this vertical merger would restrict competition in the relevant spaces due to foreclosure concerns. SAMR required the merged firm to: (1) engage with Chinese deposition and etch manufacturers on fair, reasonable, and nondiscriminatory terms; (2) refrain from proposing unfair deal terms to Chinese customers, such as tie-in sales; and (3) impose a firewall preventing Orbotech from receiving information from its competitors in the Chinese market who dealt with KLA-Tencor.

Cargotec/TTS Group

In July 2019, SAMR imposed a hold separate and behavioral remedies on the acquisition by Cargotec Corporation (“**Cargotec**”) of certain businesses of TTS Group Ltd. (“**TTS Group**”) active in the cargo handling equipment and services markets for merchant and offshore ships.³ Cargotec and TTS Group are the top two suppliers in China’s hatch cover market, with a market share of 15%-20% and 40%-45%, respectively. Cargotec and TTS Group also account for 20%-25% and 30%-35%, respectively, of the roll-on equipment for the merchant ships market and China’s cargo lifter market. SAMR concluded that the acquisition would greatly increase concentration in the product and after-sales service markets for hatch covers, roll-on equipment, cargo lifters, and anchor winches for merchant ships. As a result, SAMR imposed hold separate and firewall conditions on both companies for two years, effectively requiring the parties not to realize the benefits of integration for this period (as Chinese authorities have done repeatedly in other transactions). Cargotec is also required to compete fairly, refrain from raising prices of the relevant products in China, and refrain from restricting the relevant products from Chinese customers for five years.

II-VI/Finisar

In September 2019, SAMR imposed a hold separate and behavioral remedies on II-VI Inc.’s (“**II-VI**”) acquisition of Finisar Corp. (“**Finisar**”), both operating in the market for components used to route signals in optical communications networks.⁴ II-VI and Finisar are the top suppliers in the global wavelength selective switches market, with market shares of 10%-15% and 30%-35%, respectively. The transaction would have reduced from three to two the number of primary competitors in the Chinese and global wavelength selective switch markets, which SAMR determined was technology-intensive with high entry barriers and unlikely entry. To address its concerns, SAMR imposed hold separate and firewall conditions on the companies for at least three years. It also required the parties to supply wavelength selector switches at fair and reasonable terms and to refrain from discriminating against customers.

² Announcement of the State Administration for Market Regulation: Announcement of the Anti-Monopoly Review Decision to Approve, with Restrictive Conditions, the Concentration of Undertakings in Respect of the Acquisition of Orbotech Ltd. by KLA-Tencor Corporation (February 13, 2019), available at http://gkml.samr.gov.cn/nsjg/xwxcsl/201902/t20190220_290940.html (Chinese language).

³ Announcement of the State Administration for Market Regulation: Announcement of the Anti-Monopoly Review Decision to Approve, with Restrictive Conditions, the Concentration of Undertakings in Respect of the Acquisition of Certain Businesses of TTS Group Ltd. by Cargotec Corporation (July 5, 2019), available at http://www.samr.gov.cn/fldj/tzgg/ftjz/201907/t20190712_303428.html (Chinese language).

⁴ Announcement of the State Administration for Market Regulation: Announcement of the Anti-Monopoly Review Decision to Approve, with Restrictive Conditions, the Concentration of Undertakings in Respect of the Acquisition of Finisar Corporation by II-VI Incorporated (September 18, 2019), available at http://www.samr.gov.cn/fldj/tzgg/ftjz/201909/t20190920_306948.html (Chinese language).

ZGBH/Royal DSM

In October 2019, SAMR imposed a hold separate and behavioral remedies on the proposed joint venture (“JV”) between Zhejiang Garden Bio-Chemical High-Tech (“ZGBH”) and Royal DSM N.V. (“Royal DSM”).⁵ The JV was created to produce a key intermediate compound used in vitamin D3, 7-Dehydrocholesterol (“DHC”). ZGBH and Royal DSM, combined, would have controlled over 50% of the DHC supply to several Chinese and global vitamin markets, which would have allowed the firms to raise prices. As a remedy, SAMR required that the JV operate independently from ZGBH and Royal DSM for a period of five years—effectively echoing the dynamic of the hold separate orders imposed in the Cargotec and Finisar transactions. It also restricted ZGBH, Royal DSM, and the JV from disclosing cholesterol and vitamin D3 price information to third parties except in certain situations.

Novelis/Aleris

In December 2019, SAMR imposed both structural and behavioral remedies on the acquisition by Novelis Inc. (“Novelis”) of Aleris Corporation (“Aleris”), both active in the market for rolled aluminum sheet for automotive applications (“ABS”).⁶ Novelis and Aleris are the top two suppliers in the Chinese aluminum ABS inner plates market, with shares of 65%-70% and 5%-10%, respectively. They have the same shares in the Chinese market for aluminum ABS outer plates. The acquisition would reduce the main players in the Chinese aluminum ABS inner plates market from five to four, and in the Chinese aluminum ABS outer plates market from three to two. Among the remedies imposed, SAMR required Novelis and Aleris to divest all of Aleris’s aluminum ABS plates business in the European Economic Area—a remedy that is somewhat remarkable given its extraterritorial application to Europe rather than China.

B. Penalties for Reporting Violations

SAMR has authority to penalize parties that fail to comply with the reporting obligations stipulated in the AML by fining them up to RMB500,000 (approximately US\$72,000) and/or unwinding an unreported transaction (though it has never exercised this latter authority). All else being equal, SAMR issues larger fines for intentional disregard of reporting obligations and smaller fines if the relevant parties take remedial actions and cooperate in SAMR’s investigation.

In 2019, SAMR increased enforcement for gun-jumping and imposed penalties on 17 transactions, up from 12 in 2018. The fines ranged from RMB200,000 (approximately US\$29,000) to RMB400,000 (approximately US\$57,000). Among the 17 transactions during the past year, seven involved non-PRC parties.

III. SAMR Enforcement Actions

Continuing a 2018 trend, SAMR and its local branches brought enforcement actions in various industries, particularly in the automotive and raw materials industries, primarily targeting RPM activity and other vertical conduct.

⁵ Announcement of the State Administration for Market Regulation: Announcement of the Anti-Monopoly Review Decision to Approve, with Restrictive Conditions, the Concentration of Undertakings in Respect of the Establishment of Joint Venture by Zhejiang Garden Bio-chemical High-Tech Co. Ltd. and Royal DSM N.V. (October 16, 2019), available at http://www.samr.gov.cn/fldj/tzgg/ftjgz/201910/t20191018_307455.html (Chinese language).

⁶ Announcement of the State Administration for Market Regulation: Announcement of the Anti-Monopoly Review Decision to Approve, with Restrictive Conditions, the Concentration of Undertakings in Respect of the Acquisition of Aleris Corporation by Novelis Inc. (December 20, 2019), available at http://www.samr.gov.cn/fldj/tzgg/ftjgz/201912/t20191220_309365.html (Chinese language).

A. Monopoly Agreement Enforcement

SAMR's notable monopoly agreement enforcement targeted automakers for RPM conduct and concrete companies for unlawful market allocation agreements. For example, the largest fine in 2019 was RMB162.8 million (approximately US\$23 million), imposed on automaker Changan Ford Automobile Co., Ltd. ("**Changan Ford**") for fixing resale prices in Chongqing City. Changan Ford allegedly made "price lists," signed "price discipline agreements," and set minimum prices on certain vehicles. The fine amounted to 4% of Changan Ford's 2018 sales revenue in Chongqing City.⁷ Similarly, in December 2019, the Jiangsu Administration for Market Regulation ("**AMR**") fined Toyota Motor (China) Investment Co., Ltd. ("**Toyota**") for entering into monopoly agreements to (1) have dealers adopt uniform resale prices on online platforms, and (2) "restrict the minimum resale price" for several car models. Toyota was fined RMB87.6 million (approximately US\$12.56 million), amounting to 2% of its 2016 sales revenue.⁸

In the concrete market, the Zhejiang AMR imposed a cumulative fine of RMB7.7 million (approximately US\$1.10 million) in May 2019 on eight companies for entering into an agreement to divide the premixed concrete market in Quzhou City. The fine amounted to 1% of their respective 2017 sales revenues.⁹ In October 2019, Guangdong AMR imposed RMB7.65 million (approximately US\$1.10 million) in fines against 19 concrete companies for a similar scheme in the local Maoming City market.¹⁰

B. Abuse of Dominance Enforcement

SAMR also reported two cases of abuses of market dominance. In April 2019, Shanghai AMR imposed a fine of RMB24.38 million (approximately US\$3.5 million) on Eastman (China) Investment Management Co., Ltd ("**Eastman**"), accounting for 5% of Eastman's 2016 sales. Eastman sells a coalescing aid for latex paints in mainland China. The firm was found to have entered into exclusive agreements with domestic coating companies whereby customers were required to meet minimum procurement quantity requirements, corresponding to almost 80% of annual demand for five customers and 60% for a sixth. The regulator also found Eastman to have entered into exclusive agreements giving customers most favored nation ("**MFN**") rates if the total procurement quantity was a certain proportion of a customer's total demand.¹¹ In this action, Chinese enforcement appears to echo Western concerns about ways that conditional pricing practices, such as extending discounts at certain volume thresholds, can foreclose competition.

⁷ The State Administration for Market Regulation Published Administrated Penalty Decisions on Changan Ford over Resale Price Fixing (市场监管总局对长安福特实施纵向垄断协议依法处罚) (June 5, 2019) available at http://www.samr.gov.cn/xw/zj/201906/t20190605_302109.html (Chinese language).

⁸ The State Administration for Market Regulation Published Administrated Penalty Decisions on Toyota Motor (China) Investment Co., Ltd. over Resale Price Fixing (市场监管总局发布丰田汽车(中国)投资有限公司垄断案行政处罚决定书) (December 27, 2019) available at http://www.samr.gov.cn/fldj/tzgg/xzcf/201912/t20191227_309552.html (Chinese language).

⁹ The State Administration for Market Regulation Published Administrated Penalty Decisions on Eight Concrete Firms for Entering into Market Allocation Agreement (市场监管总局发布对衢州市8家混凝土企业实施垄断协议案的行政处罚决定书) (December 27, 2019) available at http://www.samr.gov.cn/fldj/tzgg/xzcf/201912/t20191227_309552.html (Chinese language).

¹⁰ Guangdong Administration for Market Regulation Published Administrative Hearing Notice over Monopoly Agreement in Maoming City (茂名混凝土垄断案举行行政处罚听证会) (October 29, 2019) available at http://amr.gd.gov.cn/zwdt/xwfbt/content/post_2661135.html (Chinese language).

¹¹ The State Administration for Market Regulation Published Administrated Penalty Decisions on Eastman (China) Investment Management Co., Ltd for Abuse of Dominant Market Position (市场监管总局发布伊士曼公司滥用市场支配地位案行政处罚决定书) (April 16, 2019) available at http://www.samr.gov.cn/fldj/tzgg/xzcf/201904/t20190429_293241.html (Chinese language).

In May 2019, the Tianjin Market and Quality Supervision Commission (the “**Tianjin Regulator**”) found that Tianjin Water Supply Group Co., Ltd. (“**Tianjin Water Supply**”), the exclusive public water supplier in southern Tianjin, had forced real estate developers constructing secondary water supply facilities to use certain products manufactured by Tianjin Water Supply’s subsidiary. Tianjin Water Supply was fined RMB7.4 million (approximately US\$1.06 million), representing 3% of Tianjin Water Supply’s 2016 revenue. Reports indicate that SAMR imposed only a small penalty due to the company’s active cooperation and remedial actions.¹²

IV. Conclusion

This past year built on China’s earlier efforts to refine and streamline antitrust enforcement. The arrival of the first AML amendments and regulations may help clarify expectations for companies operating in China, though certain key deviations from Western antitrust enforcement remain. At its core, even as China appears to find efficiency gains in quicker merger review, certain causes of action (such as “excessive pricing”) and the remedies imposed for violations continue to differ from the types of remedies imposed by Western authorities.

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¹² The State Administration for Market Regulation Published Administrated Penalty Decisions on Tianjin Water Supply Group Co., Ltd. for Abuse of Dominant Market Position (市场监管总局发布天津市自来水集团有限公司滥用市场支配地位案行政处罚决定书) (May 23, 2019) available at http://www.samr.gov.cn/fldj/tzgg/xzcf/201907/t20190712_303427.html (Chinese language).

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