

The New PRC Antitrust Law

by Dr. Christian Gloyer

On August 30, 2007, the new PRC, Antitrust Law was promulgated by the permanent committee of China's National People's Congress; the law will come into force on August 1, 2008. The Chinese press celebrates the new law as a 'milestone of reform legislation'. It remains to be seen, however, whether the new antitrust rules can fulfil the expectations of the public opinion.

Status Quo

First of all, it has to be noted that the Chinese economy as a 'playing field' does not offer the same set of competitive rules in all of its sectors. There are areas of the economy – such as consumer goods – where competition with regard to quality and price exists, whereas in other sectors – such as banking and financial services, but also energy and transportation, in which the state remains the dominating force as a strategic stakeholder – competition is almost non-existent. In consequence, competition rules have been scattered and often contradictory: Worth mentioning are the Law Against Unfair Competition (1993), the Consumer Protection Law (1994), the Price Law of 1998 and the Tender and Bidding Law of 2000.

This uneven legal environment, together with the well-known phenomenon of 'legal protectionism' and the tendency of national policy leaders to favour the creation of national champions in certain vital industrial areas, has led to considerable competitive restrictions for foreigners e.g. in the energy and telecommunication sectors. On the other hand, however, unfair trade practices of large foreign software companies in China have not been curbed by any legal sanctions so far.

A further deficiency of China's antitrust policies so far has been the lack of an independent administrative body solely competent in antitrust and unfair competition matters – such as the EU antitrust authority.

Another reason for concern for the Chinese public has been the growing amount of foreign funded M & A activities in China – some domestic actors, such as the Shanghai stock exchange, even went so far as to voice their fear of a 'sell out' of Chinese domestic industry, if such developments continue without any legal restraint.

The new rules roughly cover four issues: Measures against competitive restrictions, a legal prohibition of abuse of market power, merger control and, lastly, the prohibition of competitive restraints via the abuse of administrative power.

Restrictions for Foreign Investors?

Business activities of foreign investors in China may in particular be affected by the following: Firstly, the antitrust law shall apply not only to M & A activities in China as such, but also to offshore transactions with effects in the PRC. This concerns, e.g., the transfer of shares of an offshore holding company owning an investment vehicle in the PRC, if the purchaser also holds shares in a domestic PRC company which competes with the holding company's investment vehicle in the Chinese market.

Secondly, the new law introduces an additional control of merger activities with the participation of foreign capital, if such merger or acquisition is likely to threaten 'state security'. The law does not specify this vague term. One may assume that Chinese lawmakers desire to keep open a possibility of control with regard to certain industry sectors considered as vital either for the national security (such as energy supply) or the further transformation of China into a technology-oriented economy.

Prohibition of competitive restraints

The new law forbids trusts in any form, such as formal agreements, resolutions, and all informal arrangements effective as competitive restraints. Included are horizontal arrangements between competitors on the same market level, such as pricing agreements or boycotts, as well as vertical restraints, such as the prescription of resale or minimum prices. Exempted from the prohibition of trusts are agreements aiming at the promotion of technology, the improvement of production, or which help to achieve certain public goals, such as energy efficiency or environmental protection. A further exception are agreements which support the competitiveness of small-and-medium-sized companies.

It is noteworthy that companies who apply to be exempt from the antitrust rules have to prove that they do not significantly restrain competition and that the respective arrangement has a tangible positive effect for the consumer. Any illegal trust activity may lead to a confiscation of the profits thus earned and to administrative fines in the amount of up to 10 % of the company's annual turnover.

Abuse of Market Power

The antitrust law defines abuse of market power as the ability of a company to control prices, product or distribution quantities and other conditions of trade on a given market, furthermore the power to exclude others from participation. Offensive actions are e.g. the unjustified fixation of prices, the undue favouring of certain market players and forced conclusion of contracts. The new law provides a bundle of criteria to assess the extent of market power of a company, market domination will be assumed in any case if the market share of a company reaches the 50 % threshold.

Abuse of Administrative Power

A particularly delicate subject in China is the abuse of administrative power in market transactions, often with the objective to secure a competitive advantage for a company which boasts the 'right' kind of relationship to the administrative authority involved. The Chinese economy, referring to itself as a 'market economy with socialist characteristics', still has a number of sectors which are dominated by state-owned companies or administrative

monopolies, such as utility or transport. The new law at least verbally takes up the struggle against competitive restraints imposed on companies by the abuse of administrative power. The rules particularly emphasize the prohibition of administrative barriers against the inter-regional freedom of trade; once more, the so-called 'local protectionism' is in the focus of the lawmakers' efforts. The new law, however, does not abolish the still widespread sectoral monopolies in the Chinese economy.

Merger Control

Mergers and Acquisitions reaching a certain threshold size have to be registered in advance with the administrative body competent for the implementation of antitrust rules. The merger may not be executed within a period of 30 days, time within which the government officials shall verify the intended deal; if they come to the conclusion that the merger may restrain competition, it shall be prohibited, unless the companies concerned can prove that the merger has on the whole a positive effect on competition or is in the interest of the general public. The antitrust law does not specify as from which size or market share of a company involved in a M & A transaction the merger control regime becomes applicable. The highly controversial proposals of the law's first draft (world-wide annual turnover of companies involved in the amount of 12 billion RMB and domestic turnover of 800 million RMB) have not been incorporated in the final draft.

Antitrust authorities

The antitrust rules stipulate the establishment of a central antitrust authority directly under the state council. However, the state council shall leave the implementation of the new rules to other administrative bodies which in their turn may delegate certain duties to their administrative counterparts on the provincial level. It remains to be seen whether such division of labour can secure a strict implementation of the law.

Conclusion

With the promulgation of the PRC, Antitrust Law, the Chinese government has added a further element to the legislative corpus which shall secure the transformation of the Chinese society from state to market economy. The new law roughly covers all the issues which are, from a European point of view, considered vital for an effective antitrust legislation, in particular the prohibition of trusts, prohibition of market power abuse, and merger control. A Chinese speciality contained in the new rules is the prohibition of abuses of administrative power. The many legal monopolies in China still existing today are however not abolished. Foreign investors have to pay even more attention to possible side-effects in China of their offshore transactions, if their Chinese subsidiaries are possibly affected by such dealings.

Remarks:

Opinions expressed in this contribution are those of the author.

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