

# The Meaning of Restriction of Competition Under the Monopolistic Agreements Provisions of the PRC Anti-Monopoly Law

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*International attention on the People's Republic of China PRC Anti-Monopoly Law (AML) has mostly focused on merger control and abuse of dominance. Enforcement against restrictive agreements and concerted practice seems to have been overlooked so far. This article examines how the Chinese courts and enforcement authorities have analysed restrictive agreements. Specifically, it focuses on how the courts and the authorities have applied the concept of restriction of competition in monopolistic agreement cases. With respect to horizontal cases, one largely unanswered question is whether anticompetitive effects need to be proved even in cartel cases or a proof of the mere existence of the agreement suffices. With respect to vertical cases, there remains much confusion as to the appropriate analytical framework for resale price maintenance (RPM), the per se rule or the Rule of Reason, and whether Article 14 of the AML applies to agreements beyond RPM. This article attempts to shed light on these important questions.*

## 1 INTRODUCTION

Despite its relatively short history, the Chinese Anti-Monopoly Law (AML) has achieved global prominence, especially in the arena of merger control, where it is widely viewed as the third most important jurisdiction from which to secure approval after the US and the EU. Much has been said about how the prevailing Chinese approach to merger control is not always consistent with the international mainstream and how at times non-competition concerns have driven the analysis.<sup>1</sup> Chinese enforcement of abuse of dominance has also attracted similar attention and criticisms with the recent Qualcomm decision, in which the company was fined

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<sup>1</sup> See e.g. Dan Wei, *China's Anti-Monopoly Law and Its Merger Enforcement: Convergence and Flexibility*, 14 (4) J. Int'l Econ. L. 807–844 (2011); Mark Furse, *Merger Control in China: Four and a Half Years of Practice and Enforcement – A Critical Analysis*, 36 World Competition 285–313 (2013); Fei Deng et al., *A Hard Landing in the Soft Drink Market – MOFCOM's Veto of the Coca-Cola & Huiyuan Deal*, (2) Global Competition Pol'y (Apr. 2009); Matthew T. Drenan, *Shipping Market and Why the P3 Agreement Failed*, 24 Mich. St. Int'l L. Rev. 101–108 (2015); Deborah Healey, *Anti-Monopoly Law and Mergers in China: An Early Report Card on Procedural and Substantive Issues*, 3 Tsinghua China L. Rev. 17–58 (2010); D. Danny Sokol, *Merger Control under China's Anti-Monopoly Law*, 10 NYU J.L. & Bus. 1–36 (2013).

RMB 6 billion (approximately EUR 816 million) for its licensing practices.<sup>2</sup> Meanwhile, Chinese regulation of restrictive agreements, known as monopolistic agreements under the AML, has managed to escape similar scrutiny.<sup>3</sup> It is worth examining whether the Chinese approach to monopolistic agreements, and its understanding and application of the concept of restriction of competition, which underpins analysis of restrictive agreements, shows any obvious differences from the approaches in other major jurisdictions. This article will attempt to address this question for both horizontal and vertical agreements with reference to both judicial opinions and public enforcement decisions.

## 2 RELEVANT LAWS

The relevant provisions in the AML governing the legality of agreements are Articles 13 to 15.<sup>4</sup> Article 13 is concerned with horizontal agreements, while Article 14 focuses on vertical agreements.<sup>5</sup> Meanwhile, Article 15 enumerates the admissible justifications for agreements deemed to be monopolistic under Articles 13 and 14.<sup>6</sup> One of the questions left open by the language of Articles 13 and 14 is whether an agreement that falls within the literal description of one of the enumerated categories is automatically deemed to be monopolistic and hence illegal, or whether it still needs to be shown that the agreement restricts or eliminates competition. It was understood early on that the enforcement authorities, namely the National Development and Reform Commission (NDRC) and the State Administration of Industry and Commerce (SAIC), would issue regulations and guidelines, which will hopefully shed more light on the scope of the prohibitions under Articles 13 and 14. The regulations that were eventually issued by the NDRC and the SAIC would fail to meet these expectations.<sup>7</sup>

The AML is not the only legislation applicable to potentially anticompetitive practices. There are two other statutes that also apply to such practices – the Price

<sup>2</sup> Thomas K. Cheng, *The PRC NDRC Case Against Qualcomm: A Misguided Venture or Justified Enforcement of Competition Law?*, 5(1) J. Antitrust Enforcement 76–99 (2017).

<sup>3</sup> But see Yichen Yang, *Price Related Cartels Under the Chinese Antimonopoly Law Regime: The Need to Clarify Four Substantive and Procedural Issues*, 39(3) World Competition 479–512 (2016).

<sup>4</sup> Fan longduan fa [Anti-Monopoly Law] (promulgated by the Standing Comm. Nat'l People's Cong., 30 Aug. 2007, effective 1 Aug. 2008) 2007 Standing Comm. Nat'l People's Cong. Gaz.517(P.R.C.).

<sup>5</sup> *Ibid.*, at Arts 13–14.

<sup>6</sup> *Ibid.*, at Art. 15.

<sup>7</sup> 反價格壟斷規定 [Regulations on the Prohibition of Price Monopoly] (promulgated by NDRC Price Supervision and Anti-Monopoly Bureau, 29 Dec. 2010, effective 1 Feb. 2011) (P.R.C.), [http://jjs.ndrc.gov.cn/zcfg/201101/t20110104\\_389399.html](http://jjs.ndrc.gov.cn/zcfg/201101/t20110104_389399.html) (accessed 31 Jan. 2017); 工商行政管理机关禁止垄断协议行为的规定 [Regulations on the Prohibition of Monopolistic Agreements by the Administration of Industry and Commerce] (promulgated by SAIC Anti-Monopoly and Anti-Unfair Competition Enforcement Bureau, 31 Dec. 2010, effective 1 Feb. 2011) (P.R.C.), [http://www.saic.gov.cn/zcfg/xzgzjgfwj/fgs/201101/t20110107\\_103375.html](http://www.saic.gov.cn/zcfg/xzgzjgfwj/fgs/201101/t20110107_103375.html).

Law of 1997 and the Law Against Unfair Competition (LAUC) of 1993 (often known as the Anti-Unfair Competition Law).<sup>8</sup> During the drafting and the deliberation of the AML, there were suggestions that provisions in the Price Law and the LAUC that may overlap with the functions of the AML be repealed.<sup>9</sup> The idea was that it could help avoid duplication and unnecessary confusion, lest different standards for the same conduct are developed under different laws. In the end, a decision was made against repeal. Fortunately, the fear of confusion and inconsistent legal standards did not come to pass. The LAUC is largely no longer invoked by the enforcement authorities and civil litigants against potentially anti-competitive conduct. While the Price Law has been used by the NDRC and its local Price Bureaus, it was usually used in cases in which the conduct began before the AML was adopted.<sup>10</sup> Thus the enforcement authorities had no choice but to invoke the Price Law. In any case, the AML and the Price Law were invoked concurrently to the extent possible, and were applied to price fixing in most instances, which is clearly prohibited by both laws. Therefore, the issue of inconsistent standards has not arisen.

### 3 THE MEANING OF RESTRICTION OF COMPETITION IN HORIZONTAL AGREEMENT CASES

Given the bareness of the statutory language, a fuller understanding of the meaning of restriction of competition must be gleaned from the decisional practices of the enforcement authorities and from the case law.

The distribution of cases handled between the courts and the enforcement authorities has shifted over the years. In the initial two to three years of enforcement of the AML, agency enforcement was relatively subdued. For example, the NDRC did not issue its first enforcement decision until 2010.<sup>11</sup> Meanwhile, civil

<sup>8</sup> Jiage Fa [Price Law] (promulgated by Standing Comm. Nat'l People's Cong., 29 Dec. 1997, effective 1 May 1998) 1997 Standing Comm. Nat'l People's Cong. Gaz. (P.R.C.), [http://www.npc.gov.cn/wxzl/gongbao/1997-12/29/content\\_1480187.htm](http://www.npc.gov.cn/wxzl/gongbao/1997-12/29/content_1480187.htm); Fan buzhengdang jingzheng fa [Law Against Unfair Competition] (promulgated by the Standing Comm. Nat'l People's Cong., 2 Sept. 1993, effective 1 Dec. 1993) 1993 Standing Comm. Nat'l People's Cong. Gaz. (P.R.C.), [http://www.npc.gov.cn/wxzl/gongbao/2000-12/05/content\\_5004600.htm](http://www.npc.gov.cn/wxzl/gongbao/2000-12/05/content_5004600.htm).

<sup>9</sup> Organization for Economic Cooperation and Development, *Governance in China* 365 (2005).

<sup>10</sup> 南宁、柳州部分米粉生产厂家串通涨价受到严厉查处 [Nanning, Liuzhou Vermicelli Producers Fined for Price Fixing] (Guangxi Province Price Bureau, 31 Mar. 2010) (P.R.C.), [http://jjs.ndrc.gov.cn/fjgld/201003/t20100331\\_338262.html](http://jjs.ndrc.gov.cn/fjgld/201003/t20100331_338262.html); 浙江省富阳市造纸行业协会组织经营者达成价格垄断协议受到严厉处罚 [Fuyang Paper Manufacturer Trade Association Punished for Price Fixing] (Zhejiang Province Price Bureau, 4 Jan. 2011) (P.R.C.), [http://jjs.ndrc.gov.cn/gzdt/201101/t20110104\\_389453.html](http://jjs.ndrc.gov.cn/gzdt/201101/t20110104_389453.html); 广东查处海砂价格垄断案件 确保国家重点工程建设顺利进行 [Guangdong Sea Sand Producers Punished for Price Monopoly] (Guangdong Province Price Bureau, 26 Oct. 2012), [http://jjs.ndrc.gov.cn/gzdt/201210/t20121026\\_510834.html](http://jjs.ndrc.gov.cn/gzdt/201210/t20121026_510834.html).

<sup>11</sup> See Nanning Vermicelli Price Fixing case, *supra* n. 10.

litigants spared no time in taking advantage of the new legislation and AML cases were filed with the Chinese courts on the day the AML came into effect.<sup>12</sup> While the number of court cases has remained relatively steady over the years, the enforcement authorities have become considerably more active in recent years. In 2014 alone, the NDRC and its subordinate Price Bureaus imposed fines totalling RMB 1.8 billion in sectors such as automobile spare parts, insurance, cement, and optical lens. The SAIC and its provincial counterparts have initiated investigation in forty-seven cases between 2008 and 2014, with fifteen initiated in 2014.<sup>13</sup> Thus the uptake is quite apparent. However, this intensified enforcement has not shed greater light on the meaning of restriction of competition. This is largely because the NDRC and SAIC and their provincial counterparts usually only issue very brief decisions in cases, if at all. Oftentimes only a press release outlining the investigation and the infringement is available. These decisions and press releases do not present detailed analysis of competitive effects. They mostly only contain a few perfunctory statements about harm to consumers and higher prices.

In contrast, the court cases are usually much more detailed and offer much more elaborate analysis. Therefore, the analysis below will begin and focus on the court cases, followed by an exposition of the decisions by the enforcement authorities. The important *Ruibang v. Johnson & Johnson* opinion by the Shanghai High People's Court runs into tens of pages and offers very meticulous analysis. The problem, however, is that many of the private AML cases tend to be abuse of dominance cases, while agency enforcement action has disproportionately focused on price fixing. There have been only a handful of court cases involving monopolistic agreements. This could be because without the evidence gathering powers of the enforcement authorities, it is very difficult for a private litigant to obtain evidence about a cartel. The one exception is cartel conduct by trade associations, which is common in China and the trade associations tend to be quite open about their behaviour. Evidence gathering is therefore usually not an issue. Additionally, in many trade association cases, it was one member suing another over enforcement of the cartel agreement. Parties to the agreement have no difficulty furnishing evidence on the existence of the cartel. Meanwhile, evidence gathering is usually less problematic in abuse of dominance and vertical agreements cases. The following analysis hence will be based on private cases involving monopolistic agreements supplemented by the decisional practices of the NDRC and the SAIC.

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<sup>12</sup> *Li Fangping v. China Netcom*, Chinalawinfo.com, (Beijing Intern. People's Ct. No. 1, 18 Dec. 2009).

<sup>13</sup> Michael Han & David Boyle, *Antitrust Developments in the PRC in 2014*, 2 Competition Pol'y Int'l (2014), <https://www.competitionpolicyinternational.com/assets/Antitrust-Developments-in-the-PRC-in-2014.pdf>.

### 3.1 RESTRICTION OF COMPETITION IN HORIZONTAL AGREEMENT CASES DECIDED BY THE COURTS

#### 3.1[a] *Prelude: A Pre-AML Case*

One of the earlier cases involving a horizontal agreement actually predates the AML. It was the *Beijing Locksmith* case, which was decided under the LAUC.<sup>14</sup> Even though it was decided under the LAUC, the Beijing court applied an informed competitive effects analysis focusing on market power. The court invoked language that was reminiscent of competition law. However, the court did commit the mistake of confusing single-firm dominance and elimination of competition by an agreement, equating the two concepts.

The case concerned a number of firms providing locksmith service and a telephone directory service company. What transpired was that the locksmith service firms contracted with a company to provide a hotline, and the hotline service provider proceeded to sign an exclusive dealing agreement with a telephone directory service provider, which promised that all incoming calls asking for a locksmith referral will be transferred to that hotline.<sup>15</sup> According to the opinion, telephone directory inquiries are the main source of business for locksmiths.<sup>16</sup> And after this arrangement became operational, the telephone directory service provider terminated a similar existing arrangement with two other locksmith firms, which consequently suffered significant loss of business.<sup>17</sup> The two firms brought suit, arguing that the whole arrangement among all the parties involved restricted competition and was hence illegal under the LAUC.<sup>18</sup>

The court began its analysis by defining monopolization, which from subsequent language seems to be intended by the court to refer to restriction of competition by an agreement.<sup>19</sup> The court said monopolization refers to when a legal entity or legal entities, through unilateral or concerted conduct, obtain or maintain a controlling position in the market, thereby restricting other competitors from entering the market.<sup>20</sup> The court in turn defined a controlling position as a situation in which a firm possesses the economic capability to restrict or prevent effective competition in a relevant market.<sup>21</sup> The court proceeded to define the issue in the case as whether the aforementioned

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<sup>14</sup> *Beijing Anjiu Locksmith Co. Ltd. v. Beijing Telecom Co. et al.*, Westlaw, (Beijing Intern. People's Ct. No. 1, 6 Oct. 2004).

<sup>15</sup> *Ibid.*

<sup>16</sup> *Ibid.*

<sup>17</sup> *Ibid.*

<sup>18</sup> *Ibid.*

<sup>19</sup> *Ibid.*

<sup>20</sup> *Ibid.*

<sup>21</sup> *Ibid.*

arrangement among the locksmith firms, the hotline service provider, and the telephone directory service provider restricts competition and excludes competitors.<sup>22</sup>

Even though the court mentioned the relevant market a number of times, it did not define it. However, the court proceeded to assess the market power of the various participants in the arrangement.<sup>23</sup> The court observed that with the liberalization of the Chinese telecom market and the entry of new players, the 114 telephone directory service provided by one of the defendants no longer held a dominant position.<sup>24</sup> The court continued by asserting that the exclusivity agreement between the telephone directory service provider and the hotline service provider did not restrict competition either because locksmith inquiries would only be directed to the hotline if they were open-ended, meaning that the caller did not specify a locksmith.<sup>25</sup> The plaintiffs would continue to get business from callers who specifically looked for them.<sup>26</sup> The court added that the plaintiffs always had the option of joining the hotline service, which was open to other locksmith firms and the plaintiffs provided no evidence that they attempted to join the service but were refused.<sup>27</sup> The court concluded the analysis by pointing out that telephone directory service is but one source of business for locksmiths.<sup>28</sup> There were opportunities for the development of other avenues of information that would provide business to locksmiths. Therefore, the arrangement did not restrict competition.<sup>29</sup>

Even though the court's analysis was by no means faultless – it did overlook actual evidence that the plaintiffs' business suffered greatly as a result of the arrangement – it was methodical in the way it examined the arrangement layer by layer and analysed competitive alternatives for the plaintiffs. Its implicit premise was that the presence of alternatives meant that competition was not foreclosed. The plaintiffs could still thrive, at least in theory, despite the arrangement. The court's examination of competitive alternatives perhaps could have been more thorough. It could have looked into the proportion of calls into telephone directory services that were open-ended and the proportion of a typical locksmith's business accounted for by referrals from telephone directory. Nonetheless, the Beijing court did a credible job of the analysis, especially considering the level of awareness of competition law in China at the time – the AML had not even been

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<sup>22</sup> *Ibid.*

<sup>23</sup> *Ibid.*

<sup>24</sup> *Ibid.*

<sup>25</sup> *Ibid.*

<sup>26</sup> *Ibid.*

<sup>27</sup> *Ibid.*

<sup>28</sup> *Ibid.*

<sup>29</sup> *Ibid.*

passed. The difference is particularly stark when one compares the Beijing court's analysis with that contained in the agencies' subsequent enforcement decisions.

### 3.1[b] *Cases Under the AML*

This author has managed to locate eight court cases decided under the AML or in which the legality of an agreement under the AML was implicated. All of them involved cartel conduct; thus far there does not seem to have been any non-cartel horizontal agreement court cases in China. Six of them featured trade associations. Trade associations are a very regular culprit in the cartel cases, both in public enforcement and civil litigation. This is in a way a positive development as the Chinese trade associations tend to be quite open about their price fixing endeavours. This renders detection much easier than in typical secretive cartel cases that are seen in other jurisdictions.

In terms of analysis of the jurisprudential development, there are two main lines of inquiry. The first one is how the courts have interpreted and applied the concept of restriction of competition to determine whether an agreement infringes Article 13 of the AML. With respect to the meaning of restriction of competition, the overriding question over which the courts presiding over the cases have differed is whether there is any need to prove restrictive effects when a cartel is alleged. In other words, whether an effects analysis is necessary for cartel agreements. The overwhelming consensus seems to be that such an analysis is unnecessary for cartel agreements. All but two courts have summarily condemned cartel agreements absent a detailed investigation of competitive effects. The main anomaly are the two courts in the *Shenzhen Pest Control* case, both of which insisted on an assessment of market power, hinting that even a cartel agreement is unlikely to harm competition without market power on the part of the participants. In this sense, the two courts seem to be of the view that falling within one of the six enumerated conduct in Article 13 of the AML does not result in an automatic infringement. They seem to take the proviso at the end of Article 13 that monopolistic agreements are agreements that restrict or eliminate competition as a required element of proof in every AML agreements case.

The second line of inquiry is how the courts have reacted to and handled possible defences and justifications for a putatively anticompetitive agreement. Defendants in these cartel cases have attempted to offer a variety of defences for their agreements, ranging from the argument that the agreement resulted in reasonable prices to that collusion is necessary to maintain quality or safeguard public health. With the exception of two cases, the Chinese courts have generally exhibited a hostile attitude toward justifications for these attempts to justify cartel conduct.

## 3.1[b][i] Restriction of Competition

A majority of the Chinese courts have concluded that cartel agreements require no elaborate effects analysis. These include the *Suzhou Construction Materials* case, the *Nanjing Concrete* case, the *Beijing Scallops* case, the *Chenzhou Construction Waste Transport* case, and the *Xinjiang Brickmaker* case. The conduct covered includes price fixing, market allocation, bid rigging, group boycott, and no-poach agreements. The Courts' analysis does not seem to differ much by the type of agreement. Hardcore cartel conduct seems to be treated the same way regardless of its precise form.

The *Suzhou Construction Materials* case, which is the first court case concerning a monopolistic agreement this author is able to locate, concerns an agreement between two construction materials companies in Nantong in the Jiangsu Province in eastern China.<sup>30</sup> The agreement is a catalogue of hardcore cartel offenses; in it the parties agreed to fix prices, to allocate markets, and to rig bids.<sup>31</sup> In addition, they also agreed not to hire management personnel and production workers from each other.<sup>32</sup> The dispute arose when one party discovered that the other party had entered into a sales contract in contravention of the cartel agreement.<sup>33</sup> The aggrieved party brought suit to enforce the agreement, which was nullified by the court on the grounds that it contravened the AML.<sup>34</sup> On appeal, the Nantong Intermediate People's Court upheld the lower court's decision.<sup>35</sup>

The Nantong court began by stating that there are two questions to consider when determining the existence of a monopolistic agreement: (1) whether there is a competitive relationship between the two parties, and (2) whether the agreement restricts or eliminates competition.<sup>36</sup> The first question did not detain the court for long as the parties were direct competitors.<sup>37</sup> The court proceeded to define horizontal price fixing as an agreement between competitors to fix prices through whatever means.<sup>38</sup> The court declared that price competition is the most fundamental and basic kind of competition and that price fixing is a serious anti-competitive conduct inflicting the greatest harm on competition and is detrimental to consumer welfare.<sup>39</sup> It is noteworthy that the court did not inquire

<sup>30</sup> *Suzhou Juxing Light Construction Materials Co. v. Nantong Feilun Light Construction Materials Co.*, Chinalawinfo.com, (Nantong Interm. People's Court, 2010).

<sup>31</sup> *Ibid.*

<sup>32</sup> *Ibid.*

<sup>33</sup> *Ibid.*

<sup>34</sup> *Ibid.*

<sup>35</sup> *Ibid.*

<sup>36</sup> *Ibid.*

<sup>37</sup> *Ibid.*

<sup>38</sup> *Ibid.*

<sup>39</sup> *Ibid.*

into whether the price fixing arrangement had had any impact on the market price. It was illegal because it eliminated price competition between the two parties.

The court equally swiftly condemned the market sharing and the bid rigging arrangements. The court noted that even though the market sharing arrangement did not eliminate or restrict competition from other firms, it violates Article 13 of the AML because it restricts free competition between the two parties.<sup>40</sup> Thus it is clear that market-wide impact is not required. Elimination of competition between the two firms sufficed. The court also struck down the bid rigging arrangement on the ground that it eliminated and restricted competition between the two firms.<sup>41</sup> Again, no further proof of impact on competition in general is necessary. Lastly, it is worth noting that the appellant made the perhaps risible argument that the cartel agreement between itself and the appellee was in fact a joint venture aimed at independent profit maximization.<sup>42</sup> This argument provided the court with an opportunity to clarify the boundary between a legitimate joint venture and an illegal cartel agreement. After all, the agreement did provide for joint bidding by the two parties in some circumstances and thus the argument was not completely groundless. However, the court declined the invitation and simply ignored the argument.

The same analytical approach continues to be adopted in the *Nanjing Concrete* case.<sup>43</sup> This case in fact emanated from public enforcement by the Price Bureau of the Jiangsu Province. What subsequently transpired was rather unusual in a Chinese public enforcement case. The Jiangsu Price Bureau had fined the Nanjing Concrete Association and a few other concrete companies for price fixing.<sup>44</sup> The trade association and at least one of the firms had at one point initiated administrative litigation to review the Price Bureau's decision, but subsequently abandoned the suit.<sup>45</sup> Even then, the parties refused to pay the fine and the Jiangsu Price Bureau initiated court proceedings to compel the parties to pay.<sup>46</sup> It is very rare for parties to seek administrative review of a decision by one of the enforcement authorities, even though it was aborted eventually. Nor is it common for parties to refuse to pay a fine and for the enforcement authority to seek judicial assistance to collect it. In a very short decision affirming the fine on the trade

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<sup>40</sup> *Ibid.*

<sup>41</sup> *Ibid.*

<sup>42</sup> *Ibid.*

<sup>43</sup> *Jiangsu Province Price Bureau v. Nanjing Concrete Association*, Judicial Opinions of China, (Nanjing Interm. People's Court, 13 Aug. 2014); *Jiangsu Province Price Bureau v. Nanjing Jiahao New Construction Materials Co.*, Judicial Opinions of China, (Nanjing Interm. People's Court, 13 Aug. 2014); *Jiangsu Province Price Bureau v. Nanjing Dadi Concrete Co. Ltd.*, Judicial Opinions of China, (Nanjing Interm. People's Court, 7 Nov. 2014).

<sup>44</sup> *Ibid.*

<sup>45</sup> *Ibid.*

<sup>46</sup> *Ibid.*

association, the court noted that the fact that members of the association had reached agreement on price at its meetings was sufficient to sustain a finding of a monopolistic agreement under the AML.<sup>47</sup> This is despite two defences pled by the trade association, which will be discussed in the subsequent section.

The *Beijing Scallops* case adopted the same analytical approach, albeit with slightly more elaboration.<sup>48</sup> In that case, the Beijing Fisheries Wholesale Association had adopted a handbook that provided that failure to sell products at prices stipulated by the association would be considered unfair competition and would result in a fine.<sup>49</sup> In addition, the association had agreed not to sell scallops in whole pieces to non-members that competed with members in the same seafood market (this apparently would make it more difficult and costly for the non-members to resell the scallops).<sup>50</sup> The plaintiff was an owner of a seafood retail business that had been fined on a number of occasions by the association for failure to abide by the stipulated prices and eventually left the association.<sup>51</sup> It brought suit to nullify the provisions in the handbook that allowed the association to punish members for failure to follow the stipulated prices and to seek damages.<sup>52</sup>

The Beijing Intermediate People's Court No. 2 held that the price fixing and the group boycott agreements were monopolistic agreements in violation of the AML.<sup>53</sup> In striking down the price fixing agreement, the court stated that the agreement was intended to prevent competition among members of the association and affect the normal fluctuation of prices, thereby raising the members' profit.<sup>54</sup> Without citing any evidence, the court proceeded to assert that the agreement produced the objective effect of restricting competition.<sup>55</sup> This is slightly different from the approach taken by the court in the *Nanjing Concrete* case, which concluded that the fact that the parties had agreed to fix prices was sufficient to support a finding of a monopolistic agreement. In the *Beijing Scallops* case, the court took a step further and made reference to the effects of the agreement. However, this is to be distinguished from the evidence of restriction of competition required in the *Shenzhen Pest Control* case – to be discussed below – where the courts demanded concrete evidence of price increase or quality reduction. The kind of objective effects referred to by the Beijing Intermediate People's Court – prevention of

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<sup>47</sup> *Ibid.*

<sup>48</sup> *Beijing Fisheries Wholesale Association v. Lei Binglin*, Judicial Opinions of China, (Beijing High People's Court, 9 Apr. 2014).

<sup>49</sup> *Ibid.*

<sup>50</sup> *Ibid.*

<sup>51</sup> *Ibid.*

<sup>52</sup> *Ibid.*

<sup>53</sup> *Ibid.*

<sup>54</sup> *Ibid.*

<sup>55</sup> *Ibid.*

competition between competitors and limitation of the fluctuation of price – are the necessary consequence of every price fixing agreement. The court in effect did not seem to be requiring much more than the proof of a price fixing agreement to find a contravention.

The Beijing court also held the group boycott arrangement to be a monopolistic agreement under the AML. Even though concerted refusal to trade is expressly prohibited under Article 13(5) of the AML, the court did not condemn the group boycott in the case outright.<sup>56</sup> Instead, the court linked the group boycott to the price fixing agreement, and characterizing it as a mechanism to enhance the effectiveness of the price fixing agreement by limiting competition from the non-members.<sup>57</sup> If the non-members had been able to obtain whole scallops, they would have been able to compete with the members and possibly undercut the prices set by the association.<sup>58</sup> The court further noted that if the non-members had been able to obtain the whole scallops from the members, the incentives of the former to join the association would be reduced, thereby allowing them to continue to operate outside of the association and free from the price constraints imposed by the association.<sup>59</sup> Thus between these three cases, the Chinese courts have summarily condemned practically every type of cartel agreement.

Finally, there were three cases, the *Chenzhou Construction Waste Transport* case,<sup>60</sup> the *Xinjiang Brickmaker* case,<sup>61</sup> the *Longxi Concrete* case,<sup>62</sup> in which the

<sup>56</sup> *Ibid.*

<sup>57</sup> *Ibid.*

<sup>58</sup> *Ibid.*

<sup>59</sup> *Ibid.*

<sup>60</sup> *Yunfa Construction Waste Transport Company and Xinjun Construction Waste Transport Company v. Longsheng Construction Waste Transport Company*, itslaw.com, (Chenzhou Intermediate People's Court, 30 May 2015). In this case, the Chenzhou Intermediate People's Court was confronted with the question of the enforceability of a cartel agreement between the only four authorized construction waste transporters in Chenzhou in Hunan Province. The four transporters had entered into a cartel agreement under the rubric of a trade association. Under the agreement, the four companies agreed to take on all projects together, fix a minimum price for their service, and share profits among themselves. One of the parties breached the agreement and accepted a construction waste removal project on its own. The remaining parties brought suit over the breach of contract. Again, in summary fashion, the Court concluded that the agreement restricted and eliminated competition and was in violation of the AML. The agreement was therefore null and void. The only elaboration the Court provided on how the agreement restricted competition was that it was detrimental to fair competition, market order and the healthy and sustainable development of the industry. In no way did the Court explore concrete evidence of anticompetitive effects in the market.

<sup>61</sup> *Qv Chuanyu v. Sun Fudong et. al.*, itslaw.com, (Fuhai County People's Court, 15 Dec. 2015). In this case, the Court invalidated a subcontracting agreement on the grounds that the agreement amounted to output restriction and hence contravened the AML. Again, the Court was able to reach this conclusion without any elaborate analysis of competitive effects. It readily concluded that output restriction would result in the stabilization of or increase in prices for red bricks.

<sup>62</sup> *Longxi Yufang Concrete Mixing Company vs. Longxi Concrete Trade Association*, Judicial Opinions of China, (Xuancheng Intermediate People's Court, 28 Sept. 2015). In this case, the Court similarly invalidated a market allocation agreement which required members of a concrete manufacturer

Court was asked to determine the enforceability of an agreement in light of its incompatibility with the AML. The detailed facts of the cases need not detain us. Suffice it to say that all three cases were concerned with the enforceability of a cartel agreement. In all three cases, the Courts were able to reach their conclusion invalidating the agreement without an elaborate effects analysis.

In a case that stands out in its approach to cartel agreements, the Guangdong High People's Court upheld a price fixing agreement by the Shenzhen Pest Control Association.<sup>63</sup> In this case, the Shenzhen Pest Control Association and its members had reached the 'Shenzhen Pest Control Service Integrity Self-Discipline Pact', in which the members agreed that any member which tendered service at less than 80% of the recommended price announced by an official body in 1997 would be deemed to have engaged in unfair competition.<sup>64</sup> Offenders can be subject to a range of penalties, including disqualification from the provision of service.<sup>65</sup> The plaintiff was a customer of one of the member companies.<sup>66</sup> It argued that it had overpaid for pest control service as a result of the price fixing agreement.<sup>67</sup>

At trial, the Shenzhen Intermediate People's Court upheld the price fixing agreement on various grounds, most of which focus on the limited restrictive effects of the agreement. First and foremost, the court concluded that the effect on competition of the agreement was limited due to the moderate market share of its members.<sup>68</sup> After defining the relevant product market as pest control and the relevant geographic market as Shenzhen, the court ascertained the market share of the association's members as 32%.<sup>69</sup> Given this market share, and the fact that there were similar trade associations as the Shenzhen Pest Control Association in the city, the effect on competition of the price fixing agreement would be limited. The court also defended the price fixing agreement on the ground that it did not fix a price; the price could still fluctuate within the confines of the minimum price.<sup>70</sup> This is an argument that had been roundly rejected in other jurisdictions, such as

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association to pay a deposit to the association to ensure compliance with the allocation scheme. The deposit was calibrated based on the members' allocated market share. After the agreement was terminated, the association returned the deposit to all but one member, which then sued for its deposit. The Xuancheng Intermediate People's Court ordered the return of the deposit on the ground that the agreement was invalid. The Court did not discuss the competitive effects of the agreement and simply asserted the illegality of the market allocation provisions.

<sup>63</sup> *Shenzhen Hui'erxun Tech. Co. Ltd. v. Shenzhen Pest Control Association*, China IPR Judgments & Decisions, The PRC Supreme People's Court (Guangdong High People's Court, July 2012).

<sup>64</sup> *Ibid.*

<sup>65</sup> *Ibid.*

<sup>66</sup> *Ibid.*

<sup>67</sup> *Ibid.*

<sup>68</sup> *Ibid.*

<sup>69</sup> *Ibid.*

<sup>70</sup> *Ibid.*

the US in the *Socony-Vacuum Oil* case.<sup>71</sup> In a move that could prove to be highly problematic for future plaintiffs in cartel cases, the court held that the plaintiff is expected to come forward with evidence that the price fixing agreement produced restrictive effects on competition, such as evidence that the number of pest control service providers had decreased, the price of pest control service had risen or the quality of pest control service had fallen.<sup>72</sup> This directly contradicts the courts in the *Suzhou Construction Materials* case and the *Nanjing Concrete* case, which held that in cartel cases, there is no need to define the relevant market and to provide evidence of restrictive effects on competition.

Unfortunately for the development of competition law in China, the Guangdong High People's Court endorsed practically all the conclusions of the Shenzhen court and upheld the decision.<sup>73</sup> The Guangdong court agreed with the Shenzhen court that the price mechanism in the relevant market had not been severely distorted as the price was not completely fixed, but could fluctuate to a fairly substantial extent.<sup>74</sup> The Guangdong court concurred with the Shenzhen court that there is a need to show restriction of competition even in a price fixing case.<sup>75</sup> The Guangdong court actually reached a lower market share percentage for members of the association, at 22.31%, and again concluded that the impact on competition was limited.<sup>76</sup> The court reiterated that there was no direct evidence of restriction of competition in the form of exclusion of competitors outside the price fixing arrangement, increase in price, or deterioration in quality.<sup>77</sup>

In a case that was arguably even more misguided than the *Shenzhen Pest Control* case, the Enshi Miao Autonomous Region Intermediate People's Court upheld a cartel agreement on the ground that it prevented vicious competition. In the *Badong Shenlong Travel Agencies* case,<sup>78</sup> the Court was asked to determine the legality and hence validity of an agreement among travel agencies in a trade association to fix prices, adopt common service standards, and centralize promotion. While acknowledging that the agreement fixed prices, the Court upheld it on the ground that it was beneficial to the healthy development of an operating environment.<sup>79</sup> The Court suggested that allowing the member agencies to adjust their prices independently would result in vicious competition.<sup>80</sup> At least the

<sup>71</sup> *US v. Socony-Vacuum Oil Co.*, 310 US 150 (1940).

<sup>72</sup> *Shenzhen Pest Control* case, *supra* n. 63.

<sup>73</sup> *Ibid.*

<sup>74</sup> *Ibid.*

<sup>75</sup> *Ibid.*

<sup>76</sup> *Ibid.*

<sup>77</sup> *Ibid.*

<sup>78</sup> *Badong County Sanxia International Travel Agency v. Badong Shenlongxi International Travel Agency*, itslaw.com, (Enshi Miao Autonomous Region Intermediate People's Court, 17 Dec. 2015).

<sup>79</sup> *Ibid.*

<sup>80</sup> *Ibid.*

Shenzhen and Guangdong courts accepted that price fixing harmed competition; they only required proof that the agreement at issue had restrictive effects. The Enshi court worryingly endorsed the idea that free competition was detrimental to market order and price fixing was the antidote for unfettered competition.<sup>81</sup> Furthermore, it did not require price fixing to be justified by social welfare considerations. It simply accepted that the very effect of price fixing was beneficial to the orderly development of the market.<sup>82</sup> One sincerely hopes that this case represents an anomaly and does not represent the views of most Chinese courts.

### 3.1[b][ii] Defences

The Chinese courts were confronted with a variety of justifications and defences for cartel agreements. Some of them were premised on the notion that the agreement did not seriously restrict competition, while some others were based on purported benefits from the suppression of competition. The courts were mostly hostile towards them. However, the courts in the *Shenzhen Pest Control* case unfortunately adopted a sympathetic attitude towards some defences that could have far-reaching implications if a similar attitude were to be adopted by future courts.

In the *Suzhou Construction Materials* case, the appellant put forward an argument that was reminiscent of those often advanced in the early US price fixing cases, which is that price fixing should be legal if the agreed-upon price is reasonable.<sup>83</sup> The court firmly rejected the argument, noting that even though the agreement only fixed a minimum price, the price should be above that set by the least efficient operator in the market.<sup>84</sup> In a response that is also reminiscent of that made by the US courts in the early antitrust cases, the Nantong court further noted that there is no other benchmark for determining the reasonableness of price than competition itself.<sup>85</sup> Because the agreement fixed prices, it is certainly possible to conclude that the agreed-upon price is unreasonable. The court also rejected the argument that the agreement is legal because the price fixing arrangement did not affect other competitors, arguing that competition with other competitors is inevitably affected when the two companies fixed prices between each other.<sup>86</sup>

A slightly different defence was offered in the *Beijing Scallops* case. The defendant in that case did not argue that their agreement did not restrict

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<sup>81</sup> *Ibid.*

<sup>82</sup> *Ibid.*

<sup>83</sup> See *United States v. Trans-Missouri Freight Association*, 166 US 290 (1897); *United States v. Addyston Pipe & Steel Co.*, 85 F. 271 (6th Cir. 1898), aff'd 175 US 211 (1899).

<sup>84</sup> *Suzhou Construction Materials* case, *supra* n. 30.

<sup>85</sup> *Ibid.*

<sup>86</sup> *Ibid.*

competition, or that the price they had set was reasonable, but that it was only implemented in response to the supplier's demand.<sup>87</sup> Specifically, the association argued that the price fixing agreement was merely an attempt to implement the supplier's decision to fix resale prices.<sup>88</sup> Instead of condemning the resale price maintenance (RPM) scheme as illegal, the Beijing High People's Court merely noted that the supplier only stipulated a minimum resale price, and did not require the seafood wholesalers to fix actual prices.<sup>89</sup> One may infer from this treatment of the defence that RPMs are not illegal per se under the AML, which, as it turns out, is also the view held by the Shanghai courts, which will be discussed below.

Beyond these are a range of defences in which the defendant attempted to argue that price fixing was necessary to secure some other benefits, such as better quality, social welfare, or public benefit. In the *Nanjing Concrete* case, the defendants argued that concrete is a special material and therefore a minimum price is necessary to ensure quality.<sup>90</sup> This argument did not detain the Court for long and was rejected summarily. However, the courts in the *Shenzhen Pest Control* case demonstrated a markedly different attitude toward similar defences and seemingly endorsed the argument that price fixing is justified because cut-throat competition will lead to deterioration in quality.

In that case, the Shenzhen court defended the price fixing agreement on the basis of social welfare. The court declared that the AML does not espouse pure price competition at the expense of social welfare.<sup>91</sup> Misconstruing the Rule of Reason, the court proclaimed that the rule for determining the legality of an alleged monopolistic agreement is the Rule of Reason, even though the agreement at issue concerned price fixing.<sup>92</sup> The court argued that if an agreement between operators pursues a proper objective, it would escape condemnation even if it restricts competition among competitors.<sup>93</sup> The court proceeded to characterize pest control as a service of public benefit, arguing that the toxic chemicals used in pest control could affect public health, the health of the employees of the service providers, and the environment, and that pest control is closely related to disease control.<sup>94</sup> Furthermore, the recommended price promulgated by the official body had been in existence for thirteen years, during which labour costs had undergone significant inflation.<sup>95</sup> In light of this low recommended price, if service providers

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<sup>87</sup> *Beijing Scallops* case, *supra* n. 48.

<sup>88</sup> *Ibid.*

<sup>89</sup> *Ibid.*

<sup>90</sup> *Nanjing Concrete* case, *supra* n. 62.

<sup>91</sup> *Shenzhen Pest Control* case, *supra* n. 63.

<sup>92</sup> *Ibid.*

<sup>93</sup> *Ibid.*

<sup>94</sup> *Ibid.*

<sup>95</sup> *Ibid.*

offered a price that was substantially below this price, they would struggle to recoup their labour costs and would be forced to resort to lower quality products, thereby jeopardizing public health.<sup>96</sup> Therefore, the proper objective pursued by the price fixing agreement was presumably the assurance of quality service and the protection of public health.

It is not entirely clear what is the significance of the court's characterization of pest control as a service of public benefit. In any case, the court's definition of a service of public benefit is unduly broad. At most, pest control can only be characterized as a service with public health implications. The court's analysis can be construed as saying that for any product or service that has a public health dimension, unfettered price competition could lead to a deterioration of quality and a consequent threat to public health. For these products and services, price fixing to ensure quality could be justified. Even a narrower reading of the court's analysis could suggest that fixing of a price that is sufficiently low that below which the firms cannot recover their costs and ensure a minimum level of quality would be permitted under the AML. Both readings would lead to unwelcomed consequences for the prosecution of cartels in China. The court's view that unfettered competition would lead to a deterioration of quality is inconsistent with overseas jurisprudence, for example the US *National Society of Professional Engineers* case.<sup>97</sup>

Lastly, in the *Nanjing Concrete* case, the Nanjing court dealt with a defence that could have widespread implications in China. This defence concerned to what extent price fixing is justified by price regulation by government entities. The defendants argued that the agreed-upon price was below the recommended price made by the municipal Commission of Housing and Urban-Rural Development and was therefore justified.<sup>98</sup> The local commission apparently had made price recommendations for concrete.<sup>99</sup> The court's implicit rejection of the defence – the court did not explicitly address it – is noteworthy because of the prevalence of price recommendations by Chinese official bodies of various kinds.<sup>100</sup> It is not an entirely meritless argument that a price agreed upon by private parties that is below what officials have deemed to be appropriate is less problematic. After all, from the official point of view, anything below the recommended price should be acceptable. But in a move that will be highly beneficial to AML enforcement and upholding free competition in China, the court did not deem official price recommendation as a valid justification for price fixing.

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<sup>96</sup> *Ibid.*

<sup>97</sup> *Nat'l Soc'y Prof'l Engineers v. US*, 435 US 679 (1978).

<sup>98</sup> *Nanjing Concrete* case, *supra* n. 60.

<sup>99</sup> *Ibid.*

<sup>100</sup> *Ibid.*

### 3.1[c] *Conclusion*

Overall, one can conclude from the case law that the Chinese courts generally hold the view that cartel agreements, such as price fixing, market allocation, and bid rigging, constitute illegal monopolistic agreements without the need for elaborate proof of anticompetitive effects. In other words, cartel agreements can be considered to be illegal per se. The Chinese courts also seem to reject defences for price fixing such as reasonableness of price and assurance of quality. Despite the small sample size, thus far one can consider the *Shenzhen Pest Control* and the *Badong Shenlong Travel Agencies* cases to be an anomaly. If that is true, the Chinese courts' approach to cartel agreements would be largely consistent with that of the major jurisdictions. However, a confident conclusion about this will need to await further judicial decisions.

### 3.1[d] *Supreme People's Court's Judicial Interpretations*

In May 2012, the Supreme People's Court issued the *Judicial Interpretations Related to Issues Arising in Civil Litigation under the Anti-Monopoly Law* (hereinafter *Judicial Interpretations*).<sup>101</sup> In Article 7 of the *Judicial Interpretations*, the Supreme People's Court promulgates that if an agreement falls within one of the five enumerated categories in Article 13, the burden of proof shifts to the defendant to show that the agreement does not restrict or eliminate competition.<sup>102</sup> The *Judicial Interpretations* were issued after the *Shenzhen Pest Control* case was decided and upheld. It is highly likely that the Shenzhen and Guangdong courts would have handled the case differently under the *Judicial Interpretations*. Instead of asking the plaintiff to provide concrete evidence of actual anticompetitive effects, the courts would have required the defendant to show the contrary, which the defendant arguably did with reference to its low market share and the existence of competitors.

It is not entirely clear how closely the lower courts implement the *Judicial Interpretations*. The *Beijing Scallops* case was decided after the *Judicial Interpretations* were issued. However, the Beijing court did not shift the burden of proof in that case and instead focused on enumerating the anticompetitive effects of the agreement. There was no mention in the judgment whatsoever of the defendant being asked to adduce evidence of a lack of anticompetitive effects. One question left

<sup>101</sup> 關於審理因壟斷行為引發的民事糾紛案件應用法律若干問題的規定 [Judicial Interpretations Related to Issues Arising in Civil Litigation under the Anti-Monopoly Law] (promulgated by the Supreme People's Court, 8 May 2012) (P.R.C.), <http://news.sina.com.cn/c/2012-05-08/141824384755.shtml>.

<sup>102</sup> *Ibid.*, at Art. 7.

open by the *Judicial Interpretations* is whether in addition to showing a lack of anticompetitive effects, the defendant would be allowed to proffer justifications for a monopolistic agreement which are not enumerated in Article 15, such as the public benefit defence put forward by the Shenzhen and Guangdong courts in the *Shenzhen Pest Control* case. In other words, the question is whether the list of possible justifications for monopolistic agreements under Article 15 is meant to be exhaustive. How the *Judicial Interpretations* will affect the Chinese courts' approach remains to be seen.

### 3.2 RESTRICTION OF COMPETITION IN HORIZONTAL AGREEMENT CASES ISSUED BY THE ENFORCEMENT AUTHORITIES

A review of the agency decisions in China would seem to endorse the view that cartels are illegal per se under the AML. It is not always easy to decipher the analysis undertaken by the agencies when deciding a case as they release very little information about their analytical approach. Oftentimes they only issue a press release. Even if they do release a decision, it tends to be relatively short. And sometimes information is only available through Chinese press reports. However, from the materials available, it is quite clear that the NDRC and the SAIC do not believe that a detailed competitive effects analysis is necessary in order to condemn a cartel. Cartels are generally found to be illegal after establishing their existence.

The NDRC and the SAIC and their local counterparts have issued many more decisions regarding monopolistic agreements, especially cartels, than the courts. Again, many of them involved trade associations, and most of them involved domestic companies only. Foreign companies were fined in a number of cases, such as the *LCD Display* case,<sup>103</sup> the *Automobile Spare Parts and Ball Bearing* case,<sup>104</sup> and the *Automobile Manufacturers and Dealers* case.<sup>105</sup> While domestic companies have featured in the bulk of the cases, foreign companies have been liable for a disproportionate share of the fines. The LCD display makers were fined

<sup>103</sup> 六家境外企业实施液晶面板价格垄断被依法查处 [Six Foreign Enterprises Punished for Price Fixing in LCD Display] (NDRC Price Supervision and Anti-Monopoly Bureau, 17 Jan. 2013) (P.R.C.), [http://jjs.ndrc.gov.cn/gzdt/201301/t20130117\\_523203.html](http://jjs.ndrc.gov.cn/gzdt/201301/t20130117_523203.html).

<sup>104</sup> 日本十二家企业实施汽车零部件和轴承价格垄断被国家发展改革委罚款12.35亿元 [Twelve Japanese Enterprises Fined by NDRC for RMB 1.235 billion for Price Monopoly in Automobile Spare Parts and Ball Bearing] (NDRC Price Supervision and Anti-Monopoly Bureau, 20 Aug. 2014) (P.R.C.), [http://jjs.ndrc.gov.cn/gzdt/201408/t20140820\\_622756.html](http://jjs.ndrc.gov.cn/gzdt/201408/t20140820_622756.html).

<sup>105</sup> 一汽-大众销售有限责任公司及部分奥迪经销商在湖北省实施价格垄断被查处 [FAW-Volkswagen and Audi Dealers Punished for Price Monopoly in Hubei Province] (Hubei Province Price Bureau, 11 Sept. 2014) (P.R.C.), <http://www.hbpic.gov.cn/chn201201110924533/article.jsp?articleId=45084>; 克莱斯勒及上海地区部分经销商实施价格垄断被依法查处 [Chrysler and Shanghai Dealers Punished for Price Monopoly] (Shanghai Price Bureau, 11 Sept. 2014) (P.R.C.), <http://www.chinadevelopment.com.cn/qgigzs/2014/09/691583.shtml>.

RMB 353 million,<sup>106</sup> the automobile spare parts and ball bearing manufacturers RMB 1.23 billion,<sup>107</sup> and the automobile manufacturers and dealers RMB 313 million.<sup>108</sup> This is a reflection of the fact that the foreign companies that have been fined were largely major multinational corporations such as Mercedes-Benz and Samsung, while the punished domestic firms were mostly local or regional firms engaging in local cartels through trade associations. The turnover of these domestic firms is necessarily smaller. In only two cases did the fines imposed on the domestic companies exceed RMB 100 million; in most cases, the fines were no more than RMB 1 million.

In none of the press releases and decisions released by the NDRC and the SAIC did the two enforcement authorities describe a detailed competitive effects analysis. In the early cases, such as the *Guangxi Vermicelli* case,<sup>109</sup> the *Fuyang Paper* case,<sup>110</sup> and the *Guangdong Sea Sand* case,<sup>111</sup> the releases from the authorities only outlined the factual background to the price fixing scheme and proceeded to conclude straight away that there was a violation of the law (some of these earlier cases implicated the Price Law because the AML had not come into effect when the conduct took place). In some subsequent cases, there were a few statements regarding how the cartel arrangement allowed the participants to control prices, thereby harming the legal rights of other operators and consumers.

In the decisions issued in the *Zhejiang Insurance* case, which was the first case in which the NDRC issued a more detailed decision for every firm involved in the case, there were a few more statements about the competitive effects of the price fixing scheme.<sup>112</sup> The NDRC asserted that the scheme directly eliminated price competition between the competitors, reduced the operators' incentives to improve service quality in order to attract consumers, took away consumers' right to choose, solidified market shares among competitors, reduced market efficiency, and harmed consumer welfare.<sup>113</sup> However, on none of these effects did the NDRC provide concrete evidence that it actually materialized. These seemed to be treated more as the theoretical effects of price fixing in general rather than what had actually transpired in the case.

In the decisions issued in the *Automobile Spare Parts and Ball Bearing* case, the NDRC again recited that the price fixing scheme directly resulted in higher prices

<sup>106</sup> LCD Display Manufacturers Fined by NDRC, *supra* n. 18.

<sup>107</sup> Automobile Spare Parts and Ball Bearing Manufacturers Fined by NDRC, *supra* n. 19.

<sup>108</sup> Automobile Manufacturers and Dealers Fined by Hubei and Shanghai Price Bureaus, *supra* n. 20.

<sup>109</sup> *Nanning Vermicelli Price Fixing* case, *supra* n. 10.

<sup>110</sup> *Fuyang Paper Manufacturer Price Fixing* case, *supra* n. 10.

<sup>111</sup> *Guangdong Sea Sand Producers Price Fixing* case, *supra* n. 10.

<sup>112</sup> 國家發展和改革委員會行政處罰決定書 [2013] 4, 7-29號 [NDRC Administrative Penalty Decision [2013] No. 4, 7-29] (NDRC, 30 Dec. 2013), <http://jjs.ndrc.gov.cn/fjgld/index.html>.

<sup>113</sup> NDRC Administrative Penalty Decision No. 7.

for the spare parts and indirectly raised the prices for automobile, thereby harming the welfare of the downstream automobile manufacturers and consumers.<sup>114</sup> Again, the NDRC did not adduce concrete evidence that the increase in spare part prices was passed on to consumers. Therefore, it is fair to conclude that the enforcement authorities find it sufficient to merely state the theoretical effects of cartel conduct in order to condemn it. Given that every price fixing scheme carries the theoretical possibility of raising prices and reducing consumer choice, the enforcement authorities' approach is tantamount to a per se rule for cartel conduct.

#### 4 THE MEANING OF RESTRICTION OF COMPETITION IN VERTICAL AGREEMENT CASES

Most of the vertical agreement cases decided by the courts and the enforcement authorities have involved RPM. This author's research yielded three vertical agreement court cases, two involving vertical territorial allocation and the other RPM. Meanwhile, there have been a number of high-profile public enforcement decisions involving RPM, such as the *Moutai-Wuliangye* case,<sup>115</sup> which remains the case imposing the heaviest fines on domestic firms, the *Baby Formula* case,<sup>116</sup> the *Optical Lens Makers* case,<sup>117</sup> and the *Automobile Manufacturers and Dealers* case. Heavy fines were imposed in all these cases. Two Shanghai courts have expressed their approval for a Rule of Reason-type analysis for RPMs in the *Ruibang v. Johnson & Johnson* case. Meanwhile, from the meagre amount of information available from the NDRC and its local counterparts, the enforcement authorities seem to take a more hardline approach to RPMs that borders on the per se rule. Different rules applied by the authorities and the courts are clearly unsatisfactory as it may lead to the prospect of forum shopping. If a private party can persuade the NDRC to take on its case, it is obviously more beneficial to the plaintiff's cause when public enforcement is involved, especially when the plaintiff is not primarily concerned with claiming damages.

<sup>114</sup> Automobile Spare Parts and Ball Bearing Manufacturers Fined by NDRC, *supra* n. 104.

<sup>115</sup> 五粮液公司实施价格垄断被处罚2.02亿元 [Wuliangye Fined RMB 202 million for Price Monopoly] (Szechuan DRC, 22 Feb. 2013), <http://www.scdrc.gov.cn/dir25/159074.htm>; Zhong Jingjing, 茅台、五粮液价格垄断被罚4.49亿 [Moutai, Wuliangye Fined RMB 449 million for Price Monopoly], (Bjnews, 20 Feb. 2013), <http://www.bjnews.com.cn/finance/2013/02/20/248977.html>.

<sup>116</sup> 合生元等乳粉生产企业违反《反垄断法》限制竞争行为共被处罚6.6873亿元 [Biostime and Other Baby Formula Manufacturers Fined RMB 668 million for Anticompetitive Conduct] (NDRC, 7 Aug. 2013), [http://www.ndrc.gov.cn/xwzx/xwfb/201308/t20130807\\_552991.html](http://www.ndrc.gov.cn/xwzx/xwfb/201308/t20130807_552991.html).

<sup>117</sup> 部分眼镜镜片生产企业维持转售价格行为被依法查处 [Optical Lens Manufacturers Fined for Resale Price Maintenance] (NDRC, 29 May 2014), [http://www.ndrc.gov.cn/xwzx/xwfb/201405/t20140529\\_613554.html](http://www.ndrc.gov.cn/xwzx/xwfb/201405/t20140529_613554.html).

## 4.1 RESTRICTION OF COMPETITION IN NON-PRICE VERTICAL AGREEMENTS CASES

This author has located three cases in the enforcement record of the AML that have involved vertical agreements other than RPM, although one of them also involved a horizontal price fixing element and therefore it was not clear what is the significance of the exclusive distribution agreements involved in that case.

The *Nanjing Alcohol Distribution* case involved a vertical territorial distribution agreement between an alcohol wholesaler and its distributor.<sup>118</sup> The wholesaler had signed an agreement with the distributor to allow the latter to sell some alcohol products within a designated geographic area.<sup>119</sup> The wholesaler had previously entered into an agreement with the supplier of the products that required the former to enforce vertical territorial allocation.<sup>120</sup> Failure to comply would result in a fine and forfeiture of rebates.<sup>121</sup> The downstream distributor sold the products outside of its designated territory, which was discovered by the supplier.<sup>122</sup> The supplier proceeded to impose a financial penalty in excess of RMB 800,000 on the wholesaler.<sup>123</sup> The wholesaler sued the distributor for breach of contract and for the financial loss the former had sustained as a result of the latter's conduct.<sup>124</sup> The lower court ruled in favour of the wholesaler, awarding damages. The distributor appealed the decision, arguing that the vertical territorial allocation arrangement violated the AML.

In somewhat cryptic language, the Nanjing Intermediate People's Court held that the vertical territorial allocation arrangement did not violate the AML.<sup>125</sup> The court seemed to have misunderstood the nature of the arrangement. It noted that Article 13 of the AML applies to agreements between competitors whereas Article 14 concerns agreements between a business operator and its transactional counterpart, and proceeded to characterize the vertical territorial allocation arrangement as an agreement between an upstream and a downstream operator on price and the market, therefore falls outside the prohibition of Articles 13 and 14.<sup>126</sup> What the court essentially said was that Article 14 governed vertical agreements, and the arrangement at issue was a vertical agreement on price and market allocation, and therefore was not covered by Article 14. Admittedly, vertical territorial allocation is not one of the enumerated conduct expressly prohibited by Article 14. But the

<sup>118</sup> *Cao Yanmei v. Nanjing Yakeqin Trading Co. Ltd.*, Judicial Opinions of China, (Nanjing Interm. People's Court, 23 Sept. 2013).

<sup>119</sup> *Ibid.*

<sup>120</sup> *Ibid.*

<sup>121</sup> *Ibid.*

<sup>122</sup> *Ibid.*

<sup>123</sup> *Ibid.*

<sup>124</sup> *Ibid.*

<sup>125</sup> *Ibid.*

<sup>126</sup> *Ibid.*

court's pronouncement effectively means that vertical agreements are per se legal. It is not entirely clear based on the court's understanding, what sort of vertical agreement would fall within the ambit of Article 14. Whatever the broader implications of the decision, what is clear is that the Nanjing court deemed vertical territorial allocation to be legal without any need for a competitive effects analysis.

The *Lianyungang Mobile Phone* case also implicated a vertical territorial distribution agreement.<sup>127</sup> The case involved an agreement under which the plaintiff authorized the defendant to be a distributor for a certain brand of mobile phone at a particular retail location in the city of Lianyungang in Jiangsu Province.<sup>128</sup> The agreement provided for financial penalties on the distributor should he fail to abide by the territorial restriction imposed on him.<sup>129</sup> The distributor was found to have violated the territorial restriction and the mobile phone supplier sued to recover the financial penalties stipulated in the distribution agreement.<sup>130</sup> The trial court had invalidated the agreement on the ground that it amounted to market allocation and was hence illegal under the AML. The Lianyungang Intermediate People's Court overturned the lower court's conclusion, and held that the agreement amounted to nothing more than the supplier's attempt to secure orderly distribution of its product and hence did not restrict competition.<sup>131</sup> The Court did not undertake a full competitive effects analysis to study the impact of the distribution agreement on the market. In fact, it did not even define the market. It is entirely possible that the supplier had so little market power that the agreement could not create meaningful anticompetitive effects. Instead, the Court seemed to premise its conclusion on the legitimacy of the defence put forward by the plaintiff.<sup>132</sup> It seemed to believe that it was within the supplier's right to impose territorial restrictions on its distributors.<sup>133</sup> The Court's approach seems to suggest that in light of a legitimate pro-competitive justification, the Court would not even look into the competitive effects of the conduct. The case law thus far suggests that the Chinese courts take a very lenient approach toward vertical non-price restraint cases.

Another case in which a vertical agreement was implicated was the *Shandong Pharmaceutical* case.<sup>134</sup> It was an enforcement decision by the NDRC. In that case, two distributors of pharmaceutical ingredients had signed an exclusive

<sup>127</sup> *Lianyungang Junmei Electronics v. Hong Bo*, itlaws.com, (Lianyungang Intermediate People's Court, 16 Dec. 2015).

<sup>128</sup> *Ibid.*

<sup>129</sup> *Ibid.*

<sup>130</sup> *Ibid.*

<sup>131</sup> *Ibid.*

<sup>132</sup> *Ibid.*

<sup>133</sup> *Ibid.*

<sup>134</sup> 两医药公司垄断复方利血平原料药受到严厉处罚 [Two Pharmaceutical Companies Severely Punished for Monopolizing Market for Ingredients for Compound Reserpine Tablets] (NDRC, 15 Nov. 2011), [http://jjs.ndrc.gov.cn/gzdt/201111/t20111115\\_444599.html](http://jjs.ndrc.gov.cn/gzdt/201111/t20111115_444599.html).

distribution agreement with the only two domestic manufacturers of a key ingredient of an important hypertension drug respectively.<sup>135</sup> The drug was listed on the National Essential Drug Catalogue. Upon entry of the agreements, the two distributors raised the price of the ingredient from between RMB 200 and RMB 300 per kilo to RMB 1350 per kilo.<sup>136</sup> Unable to bear the inflated price, a number of the manufacturers ceased production of the hypertension drug, resulting in a shortage in the market.<sup>137</sup> The NDRC found an infringement of the AML without elaborating whether the exclusive distribution agreements without what is obviously a cartel arrangement between the two distributors would be deemed illegal. However, it is noteworthy that in addition to imposing fines, the NDRC also required the two distributors to terminate their exclusive distribution agreements.<sup>138</sup> Two exclusive distribution agreements that account for the entire market supply of a product would probably be highly problematic. The fact that the NDRC required the termination of the distribution agreements suggests that it held a similar view. But given the closely intertwined nature of the cartel and the exclusive distribution agreements in the case, it is difficult to determine what precisely is the NDRC's view on the legality of exclusive distribution agreements. Meanwhile, in the *Guangdong Football* case,<sup>139</sup> the Supreme People's Court seems to suggest that exclusive dealing would only be dealt with as an abuse of dominance and does not fall within the rubric of the monopolistic agreement provisions of the AML. In fact, the Court seems to equate monopolistic agreements with horizontal agreements, which may be interpreted to mean that Article 14 of the AML only applies to RPM. This would also seem to be consistent with the decisional practices of the authorities.

#### 4.2 RESTRICTION OF COMPETITION IN RPM CASES

Somewhat surprisingly, RPM has attracted a great deal of attention in AML enforcement. After cartels, RPM accounts for the greatest number of enforcement cases of which this author is aware. Moreover, RPM has resulted in very hefty fines. Two of the three highest levels of fines imposed in a case came from RPM cases, the *Baby Formula* case and the *Moutai-Wuliangye* case. The most elaborate judicial opinion on monopolistic agreements has also been issued on RPM, the *Ruibang v. Johnson & Johnson* case. Thus far, the NDRC has taken a fairly literal

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<sup>135</sup> *Ibid.*

<sup>136</sup> *Ibid.*

<sup>137</sup> *Ibid.*

<sup>138</sup> *Ibid.*

<sup>139</sup> *Guangdong Yuechao Sports Development Company v. Guangdong Football Association*, Wolters Kluwer, (Supreme People's Court, 14 Dec. 2017).

approach to the prohibition of RPM, eschewing detailed competitive effects analysis and shunning pro-competitive justifications. The two Shanghai courts that decided the *Ruibang* case both undertook detailed competitive effects analysis and recognized pro-competitive justifications for RPM. Only time will tell how this divide between the courts and the enforcement authorities will be resolved, possibly in an administrative review lawsuit over an NDRC decision.

In the *Ruibang* case, the products at issue are suturing products used in surgery.<sup>140</sup> *Ruibang* had been a distributor of Johnson & Johnson's suturing products until it was terminated for failure to comply with the minimum resale price stipulated by Johnson & Johnson.<sup>141</sup> *Ruibang* brought suit, claiming damages from the termination. The Shanghai Intermediate People's Court No. 1 had ruled in favour of Johnson & Johnson. It asserted that under Article 14 of the AML, it is not sufficient to show that an RPM arrangement existed, it is necessary to show that it restricted or eliminated competition in a relevant market.<sup>142</sup> It listed three factors to be considered for determining whether competition has been restricted, including the market share of the product under the RPM arrangement, the level of competition in the upstream and the downstream market, and the impact on the product's price and quantity exerted by the RPM arrangement.<sup>143</sup> The court proceeded to conclude that the plaintiff had failed to adduce evidence on these three factors.<sup>144</sup> On the contrary, the defendant was able to show that many other suppliers existed for suturing products in the Mainland.<sup>145</sup> The implicit conclusion was a lack of market power on the part of Johnson & Johnson, which required dismissal of the suit.

The Shanghai High People's Court reversed the lower court. However, it endorsed the effects-based approach adopted by the lower court. The court affirmed that under Article 14, the plaintiff must show that an agreement restricts or eliminates competition in order to sustain a finding of infringement.<sup>146</sup> The court reasoned that if Article 13, which applies to horizontal agreements, requires a showing of restriction of competition to prove a violation, it is only natural that the same requirement applies to Article 14, given that vertical agreements are less likely to be anticompetitive.<sup>147</sup> The court proceeded to outline four factors to be considered in determining whether an RPM restricts competition: (1) whether competition in the relevant market is sufficient, (2) whether the defendant

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<sup>140</sup> *Ruibang v. Johnson & Johnson*, Chinalawinfo.com (Shanghai High People's Court, 1 Aug. 2013).

<sup>141</sup> *Ibid.*

<sup>142</sup> *Ibid.*

<sup>143</sup> *Ibid.*

<sup>144</sup> *Ibid.*

<sup>145</sup> *Ibid.*

<sup>146</sup> *Ibid.*

<sup>147</sup> *Ibid.*

possesses a strong market position, (3) what are the defendant's motives for imposing the RPM, and (4) what is the competitive impact of the RPM.<sup>148</sup> These factors are slightly different from the factors identified by the lower court, but both sets of factors emphasize the degree of competition in the relevant market. The Shanghai High People's Court is more sophisticated in its approach in that it does not focus on market share, but on market position, which in the analysis undertaken seems to refer to market power. A slight surprise on the list is motives of the defendant. In modern competition law analysis, the defendant's intent or motives generally play very minor role in the analysis. However, the court seemed to have used motives as a yardstick to predict the likely impact of the RPM, which is to prevent a fall in prices.

The court proceeded to undertake very meticulous and thorough analysis of the four factors to hold that the RPM scheme imposed by Johnson & Johnson restricted competition. On the extent of competition in the relevant market, the court stated that four factors are relevant: (1) the degree of concentration in the relevant market, (2) substitutability of the product at issue, (3) entry barriers to the relevant market, and (4) competitiveness of the downstream market.<sup>149</sup> The court began by defining the relevant market as that for suturing products in China.<sup>150</sup> This market definition was uncontroversial in the case. The court examined both demand substitutability and supply substitutability, concluding that due to uniqueness of the products, demand substitutability is low and manufacturers of related products would face significant difficulty switching to the production of suturing products.<sup>151</sup> The court declared that if a credible relevant market can be defined based on demand substitutability and supply substitutability, there is no need to resort to the hypothetical monopolist test.<sup>152</sup>

The court concluded that competition is insufficient in the suturing products market for a variety of reasons. First, price elasticity of the product is low because suturing products only account for a very small portion of surgical expenses and the hospitals pass on the total costs of suturing products to patients.<sup>153</sup> Moreover, patients are highly reliant on hospitals for surgical services.<sup>154</sup> The implication is that hospitals are unlikely to be cost-sensitive to the prices of suturing products and patients are highly unlikely to choose a hospital based on the prices of its suturing products. Second, there is a high degree of brand loyalty, because suturing products are an experience product. Johnson & Johnson has invested heavily to

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<sup>148</sup> *Ibid.*

<sup>149</sup> *Ibid.*

<sup>150</sup> *Ibid.*

<sup>151</sup> *Ibid.*

<sup>152</sup> *Ibid.*

<sup>153</sup> *Ibid.*

<sup>154</sup> *Ibid.*

train doctors and nurses on the use of its products and thus healthcare professionals have become highly reliant on them.<sup>155</sup> They are hesitant to switch to unfamiliar products. Third, there are high barriers to entry due to a variety of reasons.<sup>156</sup> First, regulatory requirements are stringent.<sup>157</sup> Second, as mentioned earlier, brand loyalty is high.<sup>158</sup> Third, Johnson & Johnson has had long-standing relationships with its customers.<sup>159</sup> Fourth, the court was convinced that Johnson & Johnson had a high degree of freedom to set prices in spite of its competitors.<sup>160</sup> The court noted that the prices for its products had remained largely the same over fifteen years, despite the entry of many new products.<sup>161</sup> This conclusion is admittedly somewhat questionable given that whether the stability in price is indicative of Johnson & Johnson's price setting power would crucially depend on its competitors' prices. If its competitors' prices were lower than Johnson & Johnson's, then the court's conclusion is justified. But if the competitors' prices were in fact higher than Johnson & Johnson's, then the stability of prices tells us nothing of Johnson & Johnson's price-setting power.

The court also concluded that Johnson & Johnson had a very strong market position in the relevant market. The first controversy regarding market position/power is Johnson & Johnson's market share in the relevant market. Johnson & Johnson had provided an estimation of its market share at 20.4% at the lower court based on its own sales figures and statistics on the total use of suturing products across China taken from an official almanac.<sup>162</sup> In a move that perhaps can be taken as reversing the burden of proof on market share – a move inconsistent with other court cases which have consistently held that the plaintiff bears the burden to provide market share information and evidence on market power – the Shanghai court argued that Johnson & Johnson must possess information at its disposal to arrive at an accurate estimation of its market share in China.<sup>163</sup> The court based its argument on the fact that Johnson & Johnson had calculated global market shares for its suturing products, and inferred that if the company had sufficient information to calculate global market shares, it must have the information to calculate domestic market shares.<sup>164</sup>

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<sup>155</sup> *Ibid.*

<sup>156</sup> *Ibid.*

<sup>157</sup> *Ibid.*

<sup>158</sup> *Ibid.*

<sup>159</sup> *Ibid.*

<sup>160</sup> *Ibid.*

<sup>161</sup> *Ibid.*

<sup>162</sup> *Ibid.*

<sup>163</sup> *Ibid.*

<sup>164</sup> *Ibid.*

The court did not indicate how much higher than 20.4% would suffice to indicate sufficient market power on the part of the defendant in an RPM case. The only conclusions that can be drawn are that higher than 20.4% is sufficient and that lower than 20.4% is probably insufficient. Otherwise the court would have concluded that Johnson & Johnson had sufficient market share to constitute the requisite market power based on that estimation alone. In other words, 20.4% can be treated as a safe harbour in RPM cases. This conclusion leads to the anomaly that conceivably 21% would constitute sufficient degree of market power in an RPM case, but not so in a horizontal agreement case, as held by the Guangdong High People's Court in the Shenzhen Pest Control case.

In addition to market share, the court concluded that Johnson & Johnson held a leading position in the relevant market. Again, in a move that can be construed as reversing the burden of proof, the court held that in light of Johnson & Johnson's failure to provide market share statistics for its competitors, the lack of sufficient competition in the domestic market, and the company's leading position in the global market, it can be inferred that the Johnson & Johnson held a leading position in the domestic suturing products market.<sup>165</sup> The court seemed to be suggesting that having established that there is a lack of sufficient competition in the domestic market and that the company holds a leading position globally, the burden shifts to the defendant to provide market share statistics to rebut the presumption that it holds a leading position domestically as well. The court further emphasized that Johnson & Johnson held a very high market share with the leading (three top) hospitals in China, which tended to have outsized competitive significance in the domestic market, as they tended to influence the practices at lower-tiered hospitals.<sup>166</sup> Furthermore, the court inferred from Johnson & Johnson's high degree of price-setting power and its strong brand reputation that it held a very strong market position.<sup>167</sup>

Lastly, the court asserted that the degree of control Johnson & Johnson had over its distributors was also indicative of its strong market position.<sup>168</sup> The court noted that Johnson & Johnson required exclusivity of all its distributors, prohibiting them from carrying competitors' products.<sup>169</sup> The rationale presumably is that if Johnson & Johnson did not command a sufficient market share, the distributors would not have agreed to exclusivity as they would not obtain sufficient business from merely carrying Johnson & Johnson products.<sup>170</sup> In addition, the distributors

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<sup>165</sup> *Ibid.*

<sup>166</sup> *Ibid.*

<sup>167</sup> *Ibid.*

<sup>168</sup> *Ibid.*

<sup>169</sup> *Ibid.*

<sup>170</sup> *Ibid.*

were also subject to territorial restrictions. A distributor must receive permission from the company before it could sell to a hospital.<sup>171</sup> The distributors were also only given short-term distribution contracts, which to the court also gave Johnson & Johnson additional leverage over its distributors.<sup>172</sup>

The court further held that the motive behind Johnson & Johnson's RPM scheme was to prevent price decreases. The court began its discussion by clarifying that motives are relevant because it sheds light on the likelihood of anticompetitive effects.<sup>173</sup> If Johnson & Johnson intended to use the RPM scheme to restrict competition, anticompetitive effects are more likely to materialize. The court proceeded to infer from a number of contractual provisions that Johnson & Johnson was very focused on preventing price competition. It commented that when faced with an adverse competitive environment, it would rather respond by strengthening customer relationships than by cutting prices.<sup>174</sup> The court's reasoning here is somewhat puzzling, because it is self-evident that a supplier is motivated by a desire to prevent price decreases when imposing an RPM. Showing that the defendant wants to prevent price decreases does not shed much light on the anticompetitive nature of the conduct. The question is not whether this primary motivation is present – it is present in every RPM case – but whether this motivation is spurred by a secondary or ultimate desire to increase the competitiveness of its products or by a desire to reap greater profit by exercising its market power to prevent intra-brand competition. On this issue the court did not approach it from a perspective of motivation, but from a perspective of effects.

The court proceeded to identify three anticompetitive effects of the RPM scheme in the case. Importantly, the court did not simply identify these effects as theoretical possibilities, it substantiated its claims with actual evidence from the case. The court first declared that there was insufficient evidence to prove that the RPM scheme facilitated a manufacturer cartel.<sup>175</sup> However, the court concluded that the RPM scheme reduced both intra-brand and inter-brand competition, and prevented efficient distributors from benefiting from their efficiency.<sup>176</sup> On intra-brand competition, the court suggested that such competition is particularly important for suturing products as hospitals tended to choose products first based on quality and other considerations.<sup>177</sup> Once they have selected a brand, they expected to obtain the best price through competition among distributors.<sup>178</sup> The

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<sup>171</sup> *Ibid.*

<sup>172</sup> *Ibid.*

<sup>173</sup> *Ibid.*

<sup>174</sup> *Ibid.*

<sup>175</sup> *Ibid.*

<sup>176</sup> *Ibid.*

<sup>177</sup> *Ibid.*

<sup>178</sup> *Ibid.*

fact that the plaintiff cut prices to compete for a tender showed that such intra-brand competition would have taken place if Johnson & Johnson had allowed it.<sup>179</sup> Moreover, there was plenty of room for price competition to take place within the Johnson & Johnson brand as its products tended to be noticeably more costly than other brands.

On inter-brand competition, the court noted that even though hospitals tended to select brands based on non-price factors first, there was evidence that inter-brand price competition did take place.<sup>180</sup> The court noted a particular instance where one hospital resisted a price increase by Johnson & Johnson and the company eventually compromised with the customer and offered a lower price.<sup>181</sup> Therefore, customers are not completely price-insensitive. Moreover, the court noted the plaintiff's observation that when it lowered the price of its Johnson & Johnson products, the price of other brands' products dropped correspondingly.<sup>182</sup> The court thus concluded that with the RPM scheme, Johnson & Johnson removed pressure of price competition from Johnson & Johnson on other competing brands.<sup>183</sup> Lastly, the court observed that the fact that the plaintiff could reduce prices and still earn a profit shows that it was an efficient distributor.<sup>184</sup> Yet, it was prevented from competing based on its efficiency in light of the RPM scheme.<sup>185</sup>

The court dismissed claims of procompetitive effects in the case as not substantiated by evidence. The court acknowledged that product safety was particularly important for the products at issue, and accepted that the RPM scheme would have been justified if it contributed to product safety.<sup>186</sup> However, the court dismissed this justification on the ground of lack of evidence. First, the court observed that the defendant had failed to provide evidence that product safety had improved as a result of the RPM scheme.<sup>187</sup> The court also noted that none of the responsibilities of the distributors, such as product promotion, provision of price quotes, delivery of products, hospital visits, etc. were related to product safety.<sup>188</sup> Two segments of the distribution chain which may allow distributors to contribute to product safety, storage and transportation of the products, were not used by distributors to improve product safety.<sup>189</sup> Johnson & Johnson actually handled

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<sup>179</sup> *Ibid.*

<sup>180</sup> *Ibid.*

<sup>181</sup> *Ibid.*

<sup>182</sup> *Ibid.*

<sup>183</sup> *Ibid.*

<sup>184</sup> *Ibid.*

<sup>185</sup> *Ibid.*

<sup>186</sup> *Ibid.*

<sup>187</sup> *Ibid.*

<sup>188</sup> *Ibid.*

<sup>189</sup> *Ibid.*

storage of the products itself and imposed no specific requirements on the transportation of the products.<sup>190</sup> The court further noted that the distributors had no involvement in the two segments of the supply chain that were the most intimately related to product safety, production and training of healthcare professionals.<sup>191</sup> Johnson & Johnson was in charge of both activities. Therefore, it was clear that the RPM scheme could not be justified by its contribution to product safety.

Second, the court dismissed prevention of free riding as a plausible justification for the RPM scheme.<sup>192</sup> This is largely because a distributor can only sell to a particular hospital after authorization from Johnson & Johnson.<sup>193</sup> And no hospitals can obtain the suturing products from channels outside of the authorized distributors.<sup>194</sup> Moreover, the court believed that Johnson & Johnson exerted very tight control over the distributors.<sup>195</sup> There was really no room for the distributors to shirk their obligations.

Third, while acknowledging that promotion of new products and establishment of a new brand would justify the use of RPM, the court held that these two justifications had no application in this case.<sup>196</sup> Johnson & Johnson was a very well established brand for suturing products in China and suturing products were by no means new products.<sup>197</sup>

Lastly, the court rejected a range of other possible justifications for the RPM scheme in the case. First, the court argued that there was no need for Johnson & Johnson to use RPM to enhance brand reputation given the established brand name of the company.<sup>198</sup> Second, given the maturity of the product and the stability of demand, there is no need to use RPM to encourage stocking of inventory or to reduce market volatility.<sup>199</sup> Third, given that distribution of customers among distributors was completely dictated by Johnson & Johnson, and the number and scale of the distributors was tightly controlled by the company, there was no need to use RPM to protect or expand the distribution system.<sup>200</sup> Fourth, given that the distributors were exclusive to Johnson & Johnson, there was no need to use RPM to encourage them to focus their efforts on the company's products.<sup>201</sup>

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<sup>190</sup> *Ibid.*

<sup>191</sup> *Ibid.*

<sup>192</sup> *Ibid.*

<sup>193</sup> *Ibid.*

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<sup>196</sup> *Ibid.*

<sup>197</sup> *Ibid.*

<sup>198</sup> *Ibid.*

<sup>199</sup> *Ibid.*

<sup>200</sup> *Ibid.*

<sup>201</sup> *Ibid.*

What is noteworthy in the court's recognition of these justifications for RPM, at least in theory, is that these justifications are not found in Article 15, which provides for grounds for exempting agreements from Articles 13 and 14. The implication would be that Article 15 does not provide an exhaustive list of justifications for putative anticompetitive conduct and the courts may recognize other defences as justified by the conduct and the circumstances.

It is unmistakable that the Shanghai courts have adopted what is essentially a Rule of Reason analysis for RPM. The Shanghai High People's Court expended considerable effort to analyse the competitive effects of the RPM and the pro-competitive justifications. Although the analysis was by no means perfect – there were a few places in the opinion where the analysis was questionable – it was highly sophisticated, displaying a high degree of familiarity with the intricacies of the economics of RPM. For courts that had only begun to hear competition cases in 2008, the effort was highly commendable. From the opinion, it is clear that the court recognized that market power of the supplier is a basic consideration in determining the legality of an RPM scheme. However, the court somewhat artificially bifurcated the analysis by first assessing the competitiveness of the market and then the supplier's market position. And its focus on the motivations behind the RPM scheme is arguably superfluous, if not somewhat misguided. What impressed the most was the court's analysis of the anticompetitive effects and awareness of a wide range of procompetitive justifications for RPM. Unlike many other judicial opinions, in which the discussion of competitive effects remained in the abstract, the Shanghai court's discussion was well substantiated by evidence. The court also is to be commended for applying a critical approach to procompetitive justifications, including prevention of free riding, which is often claimed but seldom substantiated by evidence. In short, as far as the Chinese courts are concerned, restriction of competition with respect to RPMs requires a close analysis of actual competitive effects and the applicability of procompetitive justifications.

The same cannot be said about the NDRC's approach to RPM. The brevity of the NDRC's decisions and press releases makes it hard to assess accurately its approach. Its approach probably falls somewhat short of a *per se* approach; the NDRC has not declared that RPM is illegal because it falls within the literal language of Article 14. There are some discussions of anticompetitive effects in its press releases. However, there is hardly any evidence provided to substantiate its claims of restriction of competition. The NDRC's identification of restriction of intra-brand and inter-brand competition in the *Moutai-Wuliangye* case and the *Baby Formula* case probably can be applied to every RPM scheme. And in none of the press releases was there a discussion of possible procompetitive justifications for RPM. Therefore, it is not clear yet whether NDRC recognizes any

possible justifications for RPM. It is entirely possible that the NDRC's approach will evolve into something akin to a *per se* approach.

## 5 CONCLUSION

Given its relatively short history, the content of Chinese competition law is still rapidly evolving. While the bulk of the decided cases have come from the enforcement authorities, the relative brevity of their decisions and press releases means that much remains unknown about the authorities' precise approach to various monopolistic agreements. Despite being fewer in number, judicial opinions help to shed more light on how agreements are treated under the AML. At the moment, it seems that there is an emerging consensus that cartel agreements are illegal on their face. The *Shenzhen Pest Control* and the *Badong Shenlong Travel Agencies* cases remain the notable exceptions. There have been no known public enforcement or court cases involving non-cartel horizontal agreements under the AML (the *Beijing Locksmiths* case was decided under the LAUC). Meanwhile, there seems to be a split between the courts and the NDRC on their approach to RPM, with the courts taking a more effects-based approach while the NDRC applies a more literal prohibition. A continual split between the courts and the NDRC would be undesirable as it could potentially lead to forum shopping and create confusion in the law. On a more reassuring note, it seems that the notion of restriction of competition that has been developed thus far under the AML is largely consistent with the international consensus, although the Chinese courts thus far seem to be particularly lenient with vertical non-price restraints. Whether it will continue to be so remains to be seen.