

# Suggestions on Regulatory Compliance with the New Anti-monopoly Law for Multinational Companies in China

Authors Michael Zhang and William Zheng believe that China's new anti-monopoly law will effectively ensure fair competition, if enforcement authorities implement the legislation with the help of companies via industry associations. Their discussion of the new law considers aspects and issues that could help legal departments of foreign companies in China to better understand the new law and legally maximize their interest under the restrictions of the AML.

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On August 30 2007, the National People's Congress passed the Anti-monopoly Law of the People's Republic of China (AML). Its passage marks a historical moment in China's legal history. After over 10 years of drafting and preparing an anti-monopoly law, China has finally joined the ranks of countries with advanced antitrust legal provisions. The AML will come into effect on August 1 2008 and, based upon its language, should succeed in its aim of ensuring fair competition in the Chinese market.

## INTERNAL PRICE FIXING ARRANGEMENTS

The AML defines two types of anticompetitive agreements:

- (i) Between the competing undertakings (Horizontal Monopoly Agreement); and
- (ii) Between the undertaking and certain transaction party (Vertical Monopoly Agreement).

The Horizontal Monopoly Agreement deems that so-called "hard core cartels" in the market shall be strongly prohibited and investigated. However, findings of a Vertical Monopoly Agreement shall be reviewed by the Anti-monopoly Enforcement Authorities (AEA) and made on a case-by-case basis. As a general practice, some international brands or multi-national groups may have their subsidiaries conclude special internal arrangements as a strategy of developing their own brands or controlling costs. The current competition laws of China do not strictly prohibit such conduct; however, it is likely that such arrangements will be on the radar of the AEA once they meet the criteria of a Vertical Monopoly Agreement. If a certain agreement is for reasonable commercial purposes and does not cause harm to the market competition, the company shall focus on providing and preparing

the evidences that the fixed purchase price or required minimum price:

- (i) Does provide sufficient profitability space to the subsidiaries;
- (ii) Is made based on reasonable value of the products; and
- (iii) Only applies to the subsidiaries or affiliates under one group or one brand system.

It is strongly recommended that legal departments of multi-national companies with complicated supply-purchase chains in China should commence necessary internal review and inspection on pricing arrangements in a timely manner. Since there is still an 11-month window before the enforcement of the AML, continuous communication with the relevant AEA during this time period regarding internal pricing arrangements and policies in controlling the supply chain will be very helpful for future regulatory compliance.

According to reliable sources in the State Council, the government is considering establishing an agreement pre-consultation system. Under such a system, parties can voluntarily submit proposed agreements to the government for pre-judgment. If the pre-consultation system is adopted, it could be a "safety belt" for international companies and brands, and their in-house counsel would work closely with outside attorneys to submit any arrangements that might be considered internal price fixing agreements to the Ministry of Commerce (MOFCOM) and confirm their exemption from being labeled as having a Vertical Monopoly Agreement.

## CONSPIRACY WITHIN INDUSTRY ASSOCIATIONS

Price fixing is extreme monopolistic conduct that is specifically aimed at by the AML. According to a MOFCOM official, any conspiracy towards price fixing among the companies that are in a competing market or industry will no doubt be deemed as illegal. Therefore, any commercial activities among the management of the companies from the same industry shall be extremely sensitive in discussing pricing matters or anything directly concerning the value and price of products or services. Further, any indirect discussion or agreement on factors related to the product or service price is highly likely to be investigated as price fixing by the enforcement agencies.

There exist many commercial activities, seminars and periodical meetings among members held by certain industry associations which take an active role in organizing and coordinating competition in industries such as food, beverages, steel making, medical instruments and automobiles. Though the AML has not yet come into effect, the State Development and Reform Committee, which should be part of the AEA, has actively disclosed and punished price fixing activities held or encouraged by various industry associations in China, such as the instant noodle association. The special punishment provided for in the AML targeting industry associations was added in the latest review

by the People's Congress, which reflects the attention by Chinese government on punishing obvious conspiratorial conduct by industry associations.

The enforcement against conspiracy will surely not be limited to those which are obviously monopolistic conduct, as proven by several officials who have made speeches in several AML seminars and conferences. The AEA will pay special attention to indirect conspiracy or agreement on controlling prices and eliminating competition in the market. The same official emphasized that such meetings involving management, sales representatives or marketing officials of member companies shall not, in any manner, touch on the topics of controlling costs or expenses, the impact of increasing prices of raw materials, average labor compensation or seasonal price floating. Thus, international companies shall continuously alert their representatives in various public activities of any improper discussion or announcements related to price fixing. Furthermore, such restrictions shall uniformly be enforced and required on their lower level employees who will occasionally meet and discuss during marketing activities.

#### **CRITERIA FOR NOTIFICATION OF CONCENTRATION**

The current AML does not clearly provide the criteria of exemption to those concentrations that may not notify the AEA. However, it has been confirmed that the AEA will issue detailed criteria of the notification qualifications in coming implementation rules. "Sales Amount", "Assets" or "Market Margin" are likely to be adopted as a major part of the criteria, which have been proven in the existing pre-merger notification requirements issued by MOFCOM. Due to the huge size of most multinational companies investing in China, it is suspected that such criteria for domestic companies and international companies may be different. Upon confirmation of the officials from MOFCOM and People's Congress, such differences will not be adopted by the AML and its implementation rules. Further, the AEA is considering the different criteria for various industries, of which the current market amount and company size will be largely different in various industries, such as telecommunications, the automotive industry, and public transportation.

It is highly likely the AEA will conduct a wide market investigation and survey to decide upon the criteria before the enforcement of the AML.

Multi-national companies and industry associations shall take active roles in assisting in the market survey conducted by the AEA, while the AEA should consult the companies and industry association to conclude the differences among various industries.

#### **OPPORTUNITIES IN INDUSTRIES WITH A NATURAL MONOPOLY**

The AML is not strictly aimed at existing monopolistic situations in industries that have historical reasons for a monopoly, or where there is only one stated-owned company in the market due to the nature of the industry. Such industries would usually be referred to as a "natural monopolized industry". With respect to such industries, the AML is unlikely to break up a monopoly, for reasons of economic development and social considerations. However, as confirmed by the official of AEA, these industries will have to improve upon their monopolized situations in the market through cooperation with outside companies, regardless of whether they are foreign-invested or domestically owned. Such a trend might provide opportunities to be explored by foreign investors, by engaging in previously restricted but less sensitive industries, such as basic telecommunications, mineral exploration and transportation. Foreign investors with developed technologies and mature management skills and experiences should prepare themselves for opportunities of cooperating with those monopolized enterprises for improvement of the market competition situation, which might be of great importance to their global development strategy.

Generally, during the absence of the implementation rules and guidelines of the AML, there might still be some uncertainty in the detailed requirements of enforcement and procedures. However, it is very important that the legal departments of multi-national companies and various foreign-invested enterprises in China take full advantage of the time window before the effectiveness of the AML, commencing review of existing price and market arrangements and re-valuing internal policies of commercial behavior.

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