US-China Business Council Comments on Antimonopoly Law Amendment Questionnaire

December 18, 2015

The US-China Business Council (USCBC) and its member companies appreciate the opportunity to participate in the consultation process for revisions to the Antimonopoly Law (AML), and to provide feedback on the questionnaire issued by the China University of Political Science and Law's Center for Competition Law (CCCL). USCBC has approximately 210 member companies with significant investment and operations in China across all industry sectors. USCBC and its members support China's right to foster a fair and competitive market that enhances economic efficiency and safeguards consumer and public interests.

USCBC is pleased to provide constructive recommendations and share international best practices to support the continued improvement of China's competition enforcement framework. USCBC and its member companies appreciate the inclusion of AML revisions in the 2015 State Council Legislation Work Plan. CCCL's outreach reflects an ongoing effort to provide greater transparency in the formulation of policy and legislation as well as improve China's competition regime.

Competition has been a priority for foreign and domestic companies over the past several years. While China's efforts to draft AML-related regulations and strengthen competition enforcement indicate regulators are working to achieve China's antitrust goals, they have also prompted significant attention and concern from global stakeholders, including US companies. In USCBC's 2015 business environment survey, for example, 85 percent of survey respondents from our member companies indicated that they are somewhat or very concerned about China's antitrust environment. That statistic includes companies that have directly experienced AML enforcement as well as those with strategic concerns.

Many foreign-company concerns about AML enforcement are similar to those raised by domestic Chinese companies, including lack of transparency and due process, unclear criteria for how cases are decided, and inclusion of non-competition factors in competition decisions. We believe that those concerns can be addressed through revisions to the AML and related regulations.

USCBC recommends that the AML be revised to align with international best practices and with specific Chinese commitments made at the Joint Committee on Commerce and Trade (JCCT) and Strategic and Economic Dialogue (S&ED). Revisions should be based on the fundamental principles established at the 2014 S&ED to ensure that competition enforcement is "fair, objective, transparent, and non-discriminatory" by clarifying vague provisions that create uneven enforcement; adding language to boost effective, predictable and unified enforcement; and refining the law to be consistent with international best practices.

The comments in this submission represent the views of leading US companies engaged in business across all industries and sectors in China. USCBC respectfully submits the following specific responses for consideration and is happy to discuss these views further and to continue to be a resource for CCCL and China's competition regulators.

I. General Principles:

Question 1: With a deepening understanding of AML theory and further development of the relevant law enforcement work, how should we optimize Article 1, dealing with the AML's legislative intent?

At the 2014 S&ED, the United States and China affirmed that "the objective of competition policy is to promote consumer welfare and economic efficiency rather than promote individual competitors or industries, and that enforcement of their respective competition laws should be fair, objective, transparent and non-discriminatory." USCBC suggests that the revised AML include language that emphasizes this objective, stating that the law's intent is to protect consumer interests—not competitors—through competition.

We also recommend that the law limit administrative intervention in the market to a reasonable level, in order to let the market play a decisive role. Suggested language should read, "Protecting the fairness and the freedom of the market competition."

Question 2: How should the AML's current enforcement system be evaluated? Do you have any suggestions for short-term, medium-term, and long-term reform of the law enforcement system?

To ensure consistency in antimonopoly law enforcement, it is necessary to set unified rules to avoid conflicting criteria from different agencies as well as broad interpretation of laws and regulations. Most jurisdictions outside of China feature a clearly unified system, either with a single competition agency or closely aligned policies and practices that unite multiple agencies. To increase consistency across law enforcement, several countries like France, England, and Spain have consolidated antitrust agencies into a single entity.

Although adjusting the organizational structure of AML regulators might be a long-term effort, the Anti-Monopoly Commission (AMC) under State Council, in the short term, should coordinate the enactment of unified enforcement rules to increase transparency in the process and reasoning in cases. This would help companies better understand the requirements and ensure rigorous compliance policies.

Question 3: Do you think the content in Article 4, 5, and 7 with Chinese characteristics needs to be revised or deleted? Please provide explanations and suggestions.

Unfair treatment and discrimination are among the biggest issues companies face when competing against domestic companies, including (but not limited to) state-owned enterprises (SOE). Article 7 of the current AML says that for "industries controlled by the state-owned economy and concerning the lifeline of the national economy and national security," the state "lawfully regulates and controls their business operations and the prices of their commodities and services." This language seems to exempt these sectors from the normal scrutiny companies in other sectors face. However, the scope of sectors in this provision is very broad; some of these sectors no longer operate as true monopoly sectors, but instead are competitive with both state and non-state companies. As written, these provisions could apply to these sectors in ways that could harm competition and hinder Chinese government efforts to promote industry development. The AML should be clear on the extent of its application to SOEs and its affiliates to ensure consistent competition law is being applied. Thus, it is necessary to narrow the scope of the industries exempt from the AML in Article 7 to only traditional monopoly industries. In this regard, it is also important to clearly define the scope of "legitimate business activities."

Question 4: Do you have other suggestions about revisions to the first chapter on AML general principles?

In addition to the three fundamental pillars regulated by the AML (monopoly agreements, abuse of dominant market position, and enterprise concentrations), the AML also addresses abuse of administrative power. NDRC recently investigated several cases of abuse of administrative power at local and provincial levels to restrict competition. To reflect the importance of this tool, USCBC suggests that Chinese authorities merge Article 8 into Article 3 as sub-article 4 in line with international trends and practices such as the European Union's State Aid Controls.

II. Monopoly Agreements

Question 1: Should other kinds of factors be added to Article 13 (1) of the AML? Are specific identifying factors and principles required? Is it necessary to stipulate the burden of proof for relevant parties? Please explain briefly.

Given the evolution of economic activity, international regulators must consider whether new activities may promote or restrict competition. In confronting these cases, common international practice is to carefully weigh the merits of new types of conduct before making a determination, as opposed to making broad determinations that these behaviors are pro- or anti-competitive. Therefore, drafters should be cautious when considering whether to add other factors to Article 13(1).

Regarding horizontal monopoly agreements, one of the key questions unaddressed is whether such agreements are deemed illegal *per se* or whether they would be judged based on their impact. We encourage revisions to clearly state that regulators must weigh the competitive impact of such behaviors in these cases, and also to stipulate the identifying factors and burden of proof of the parties to avoid the broad discretion of authorities. Doing so would allow greater predictability and certainty for both regulators and companies, and would better allow domestic and foreign companies to determine risks and better comply with rules.

The revised AML does not need to stipulate the burden of proof because such issues should be covered within the scope of procedural law. In addition, other regulatory documents, including the Supreme People's Court's (SPC) Application of Laws in the Trail of Civil Disputes, already have clarified the burden of proof in the AML cases that they consider.

Question 2: Should the courts be added to the sixth item of Article 13 (1) [as an organ that can recognize] other [prohibited] monopoly agreements alongside the State Council antimonopoly enforcement agencies? Please explain briefly.

Article 13(1) addresses the types of monopoly agreements prohibited under the AML, including "other monopoly agreements as determined by the antimonopoly authority under the State Council." This clause allows administrative agencies to determine that a given monopoly agreement should be prohibited, but does not currently give that power to the courts. AML enforcement should fall under the scope of administrative enforcement, with the three main enforcement agencies as the main decision-makers. The courts should retain the important role of handling the administrative appeals process, but allowing the courts to label monopoly agreements as prohibited could create additional challenges, and add another layer of inconsistency to AML implementation. As such, we do not suggest adding the courts to this provision.

Question 3: Should the definition of the Monopoly Agreement stipulated by the Article 13(2) of the AML be separated from Article 13? Does the definition need to be improved? Should it be more specific about the exclusion or restriction on competitive effects or goals? Do you have any comment about "resolution" and "other cooperative behavior"? Please explain briefly.

Articles 13 (horizontal monopoly agreements) and 14 (vertical monopoly agreements) define prohibited monopoly behavior for business operators, but do not further define whether such behavior is illegal *per se* or is deemed illegal after considering rule of reason. Thus, more clarification is needed in this regard to be consistent with international practice.

Question 4: How should the relationship between Article 13 and Article 15 be interpreted, and how should it be applied? Does the regulations on Article 15 reasonable? If not, how to improve it? Please explain briefly.

Article 13 lists types of horizontal monopoly behaviors that are prohibited, and Article 15 lists exemptions based on the circumstances of the case. Article 15 will not be considered if Article 13 is not applicable.

It is necessary to clarify the determining factors of anticompetitive behavior either within Article 15 or in other relevant regulations and guidelines. Criteria listed in Article 15 that would exempt an agreement from the prohibitions listed in articles 13 and 14 lack explicit standards. Because of this vagueness, a company cannot use Article 15 as a defense when confronted with AML investigations or private lawsuits.

To be more specific, Article 15 needs to clearly state whether the types of factors under consideration refer to the purpose or the effects of the agreement. If it refers to the effects of a given behavior, we suggest providing specific assessment criteria. For example, in regard to the first item "to improve technology, research and develop new products," it would be helpful to add criteria to weigh whether the products are new or a barometer for improvement of technology. USCBC suggests further clarification on the assessment criteria reading "substantially restrict competition in relevant market" and "enable consumers to share the interests derived from the agreement."

Question 5: Currently, there are no specific regulations in the AML on vertical non-price agreements. Does this create uncertainties for daily business operations? Is it necessary for the AML to add new provisions on vertical non-price agreements? What are the main types of vertical non-price agreement commonly signed by businesses in addition to that listed by the Article 14 (1), 14 (2) of the AML? Are there types of vertical non-price agreements that need to be prohibited in principle, as with fixing vertical price and setting minimum resale price? Currently, European Union has the most comprehensive regulations on vertical non-price monopoly agreements. For example, Article 4 and Article 5 of the Block Exemption Agreement of the vertical agreement (2010) issued by the European Commission stipulate the "core restriction" and "excluded restrictions." Should we learn from the experience of European Union? How should we draw lessons from the European Union on proscriptive vertical non-price monopoly agreements? Should we follow their paths indiscriminately or absorb selectively? Is it

necessary to distinguish between core restrictions and excluded restrictions? How should we learn from the Europe Union experience on those points? Please briefly explain.

From an international perspective, regulations on vertical restrictions vary among different jurisdictions. In China, the AML's Article 14(1)(3) has a "catch-all" clause that could deem non-price vertical agreements to be anti-competitive. In practice, vertical agreements are not necessarily anticompetitive: they can sometimes have pro-competitive effects and improve economic efficiency. In addition, provisions related to non-price vertical agreements already appear in other regulations, such as 2006 Administrative Measures for Fair Transactions Between Retailers and Suppliers, 2004 Judicial Interpretation of the Law Applied to Disputes Arising from Technology Contracts, Regulation on the Administration of Import and Export of Technologies (2001) , and the Provisions on the Prohibition of Regional Blockades in Market Economy Activities (2001). The need for a regulation specifically targeting vertical agreements (especially non-price related) should be carefully assessed. Given the complexity of this issue, USCBC suggests a separate guideline for assessing the competitive impact of various types of vertical agreements.

In addition, USCBC encourages the AML drafters to require the use of a "rule of reason" for vertical agreements and to specify the determining factors for ruling these agreements as pro- or anti-competitive. International best practice is instructive in this case: US regulators use a "rule of reason" approach when weighing vertical monopoly agreements that include price-related agreements. The EU competition regime looks at "hard-core restraints," but includes multiple exceptional circumstances. Even in the EU multiple factors are assessed when determining vertical monopoly agreements to be illegal, pointing to an applied "rule of reason" rather than an approach that renders such agreements *per se* illegal. To assess impact on the competition, China should consider elements such as competition in the relevant market, economic efficiency, and consumer benefits in respects of price, quality and pre- or post-sale services.

Question 6: Is it necessary to specify a safe harbor for vertical agreements? Is it reasonable to define safe harbor according to market share? What percentage of market share is reasonable for safe harbor? Is it necessary to specify the process and major factors for the law enforcement departments to analyze and consider the issue in addition to vertical agreements outside the safe harbor?

USCBC encourages Chinese authorities to consider applying the concept of "safe harbors" to vertical agreements as a means of fostering stronger market competition. Vertical agreements can have pro-competitive effects and increase economic efficiency within a relevant market. For example, vertical agreements can limit "free rider" activity, promote competition in the market, and ensure high quality of pre-sale and after-sale services. While vertical agreements can largely eliminate competition among distributors who sell products from the same producer, they might

not have an obvious anticompetitive effect if there is sufficient competition among similar producers.

Thus, permitting safe harbors can stimulate the positive impact generated by vertical agreements while still ensuring fair market competition. The safe harbor can also save enforcement resources by allowing regulators to focus on cases with more competitive impact. This is an important factor as to why regulators in the United States and Europe have adopted such a model: both the European Commission and United States adopt 30 percent as the safe harbor threshold. We recommend that Chinese regulators consider adding safe harbor provisions to the AML or to follow-up provisions, using international practices as a guide.

III. Abuse of Dominant Market Position

Question 2: Should some adjustment be made to the content and phrasing of provisions covering all kinds of behaviors that abuse market dominant position under the AML's Article 17(1)? Is it necessary to make it more in line with other articles in the AML?

Behaviors prohibited under Article 17(1) for an operator with a dominant market position should be limited to conduct shown to have an unreasonably restrictive effect on competition. Terms such as "unfairly high" or "unfairly low" are very subjective, which could lead to uneven enforcement between competition regulators and allow officials to promote local protectionism.

Thee use of the word "unfair," appears inconsistent with the intent of competition laws and could be used to foster protectionism. The term implies that there is an appropriate value for products other than the prices set by a competitive process, which invites regulatory interference with ordinary business processes and is likely to raise consumer costs. We suggest careful consideration of these terms and concepts to determine if they are appropriate, or if there are alternatives that allow for robust enforcement.

As a general rule, US competition law does not prohibit monopoly pricing in blanket fashion, as it recognizes that monopoly pricing can have pro-competitive effects. Administrative decisions and courts have affirmed that efforts to aggressively innovate, promote, purchase inputs, and sell a product or service are strongly encouraged even if they result in a monopoly position. They have also affirmed that the ability to charge monopoly-level prices is lawful under the right circumstances, and can be an important element of an innovative, free-market system. The opportunity to charge monopoly prices—at least for a short period—attracts investment, by inducing the risk-taking and innovation that produces economic growth. Those high prices ultimately attract aggressive competitors that stimulate competition and erode a monopolist's position. Prohibition of all monopoly pricing forces a competition authority to act as a price regulator, a role that is antithetical to an efficiently functioning market system, is likely to harm competition and consumer interests, and increases the regulatory burden for Chinese agencies.

The prohibition in Article 17(1) on "imposing unreasonable trading conditions at the time of trading without any justifiable cause" is also vague and subjective. Absent harm to competition, trading conditions that another firm might regard as unfavorable or unreasonable may simply be evidence of aggressive competition. Similarly, Article 17(1)'s prohibition on refusals to deal, unless the dominant firm can show "justifiable cause," may be overly restrictive. For instance, it is recognized in US antitrust jurisprudence that a firm generally may refuse to deal with a potential trading partner, unless such refusal is shown to harm competition. If a refusal to deal does not result in harm to the competitive process itself, modern economic theory and competition policy suggest no reason for competition authorities to intervene. We suggest that competition experts carefully consider these points as they further revise this article.

Question 4: How should the factors used to determine market dominant position in the AML's Article 18 be abridged, supplemented, or adjusted?

The list of factors used to determine whether the company has a market dominant position in Article 18 should be expanded to include a wider range of potential behaviors that better reflect Chinese competition realities. For instance, the ability of other firms in the relevant market to expand their output is a highly relevant consideration. Other factors include the existence of countervailing buyer power.

Question 5: Are the provisions on a presumed market dominant position in the AML's Article 19 necessary? Is it necessary to specify application conditions?

We suggest that Article 19 is not necessary, as determination of dominance can be based on actions as opposed to inherent position. While a company that represents a large market share may occupy a dominant position in the market, the real question is whether that company abuses its position to control prices, limit output, or exclude competition.

IV. Concentration

Question 1: Do you see any confusion in the provisions under the AML's Article 20 about enterprise concentrations? How should this be improved, if necessary?

Article 20—which defines concentrations—includes all mergers between business operators, which requires these transactions to file with MOFCOM. However, that language would also cover mergers between companies where there is no change of control. It is not clear whether this kind of merger is required to file with MOFCOM. In a hypothetical example, Company A holds 51 percent of shares of Company B prior to merger discussions. If Company A wants to acquire Company B, Company A retains control no matter this acquisition realized or not. Thus,

this concentration would not lead to a change of control and any substantial influence on the market competition. In this case, it should not be necessary for either party to notify the authorities, as there would be no real competitive impact.

Question 2: Is it necessary to set limitations in the AML's Article 26 to stop the clock on the review period to facilitate discussions with managers to discuss proposed additional restrictive conditions? If necessary, how should this be improved?

The Regulation on the Restrictive Conditions Imposed on the Undertakings' Concentration released by the Ministry of Commerce (MOFCOM) states that if MOFCOM determines that a concentration has anticompetitive effects and the parties cannot address those concerns, MOFCOM can reject the concentration. Considering the complexity and uncertainty of business activities, USCBC suggests providing a specific timeline for the review period, and allow enough time for preparation, negotiation, and engagement of the deal.

Question 3: Should provisions in the AML's Article 27 covering factors to be considered when reviewing enterprise concentrations be improved? If necessary, how should they be improved?

USCBC suggests that Chinese authorities revise Article 27 to add elements for consideration, including the company's development and investment plans and trends in the relevant market. If the company intends to reduce its investment in the relevant market, or if the overall relevant market is shrinking, a proposed concentration would not have an obvious anticompetitive impact.

V. Abuse of Administrative power to restrict or eliminate competition

Question 3: What do you think of the AML's Article 37? Based on foreign experience, is there a need to bring fair competition regulation system into the law? Please briefly explain.

Article 37 prohibits administrative entities from issuing regulations and rules in violation of the AML, a positive development in the creation of a unified competition regime and to protect against administrative monopolies. USCBC has concerns, however, about the ability of agencies to use this language to enforce such monopolies. For example, under the AML's Article 51, even if antimonopoly enforcement agencies use Article 37 to uncover an administrative monopoly, they can only make suggestions to the higher-level administrative entity. This reduces the antitrust authorities' power and ability to enforce Article 37 – a possible factor in the small number of administrative monopoly cases seen to date.

Article 37 does not explicitly define standards or consequences of administrative monopolistic behaviors, making it difficult to determine how to handle these cases.

USCBC suggests that AML revisions consider the State Council's concept of "fair competition

review regime" as a means to prevent the administrative monopoly.

Question 4: Have you followed the first lawsuits concerning "abusing administrative power in eliminating and restricting competition" after the AML's implementation? Do you think there have been any problems with these cases? Please briefly explain.

USCBC members have questions related to initial lawsuits against to administrative monopolies. First, there are no specific criteria to determine if an administrative behavior eliminates or restricts competition. In addition, even when agencies determine that an administrative monopoly exists, there is little clarity on the consequences for such behavior, including calculating losses. This makes it difficult for enforcement agencies to enforce administrative monopoly decisions, and creates uneven implementation among enforcement agencies. USCBC suggests clarification on both these points.

Question 5: How should the rights and interests of the victims of the behavior "abusing administrative power in eliminating and restricting competition" be safeguarded? Is there a need to include relevant provisions on lodging complaints and compensation? Please briefly explain.

The inclusion of language on administrative monopolies in the AML was an important step in tackling a common problem that companies and consumers face in China. USCBC suggests a judicial review could further that initiative by laying out methods to file lawsuits and obtain compensation. These rules could motivate victims of administrative monopolistic acts to protect their business.

VI. Legal Liabilities and Supplementary Articles

Question 1: Do you think criminal liabilities for serious monopoly acts should be included in the AML? If yes, how should these be stipulated?

The purpose of the law is to ensure fair competition to ultimately benefit consumers. Administrative penalties should fulfill this purpose. The AML's Chapter 7 on legal liabilities includes strong provisions allowing the issuance of orders to stop the illegal action, impounding illegal income, and imposing a fine in the amount between 1 to 10 percent of the preceding year's annual revenue. Existing cases have shown that the fines imposed under Article 46 could be quite large, not only to deterring anticompetitive behavior, but in some cases impacting the business's ability to remain a competitor in the market. Penalties should serve to restore competition, not reduce competition. Moreover, clarity on calculation of the fine is necessary to strengthen the credibility of enforcement actions.

Given the strength of existing language, USCBC suggests that AML violations remain subject to administrative penalties, but not criminal liability. This would also be in keeping with international legal practice, since competition law is commonly considered administrative law.

Question 3: How do you think civil compensation in the AML's Article 50 should be identified?

The purpose of the AML is to promote competition and development of the market; however, punitive damages would impose a heavy burden on companies and hinder operations. In addition, the purpose of fines are to help restore competition. USCBC members suggest that civil damages calculate damages designed to cover substantial damages.

Question 4: The AML's Articles 46 and 48 stipulate a fine of RMB 500,000 to those fail to perform agreed monopoly agreements, industry-wide monopoly agreements organized by industry associations, and illegal concentrations of undertakings. Do you think that this provision is reasonable? If not, how should it be adjusted? Is there a need to introduce a daily fine system for those who refuse or procrastinate on paying the fine? If yes, how should the fine amount be determined?

USCBC encourages the addition of defined thresholds for fines in AML investigations as a way of creating enforcement consistency. Unnecessarily high fines could impede the operations of companies in China. By setting a defined threshold for fines, enforcers can accomplish a deterrent function without unnecessarily harming the company's business.

High fines are not appropriate for every AML investigation. For example, when two parties create, but do not implement, a monopoly agreement, there should be no substantial damages.

Question 5: Do you think the AML's Article 55 regarding the relationship between the exercise of intellectual property and AML should maintain current provisions that carve out and separately define intellectual property or should not separately define intellectual property and instead simply apply a "rule of reason" principle during AML investigations. Separately, should Article 15 be restructured as an exemption while Chinese authorities issue another guide on intellectual property rights?

USCBC closely monitors the development and progress of the IP issue under AML and submits constructive comments to regulators and AMC as well as engages in dialogues with businesses and regulators through advocacy efforts. In those comments, USCBC has expressed concerns about numerous articles that need clarification to achieve the stated objectives, such as promoting competition and innovation and improving efficiency of the operation of the economy. Please see the separate attachment of the comment letter USCBC provided to NDRC on its latest draft IP guidelines.

More comprehensive comments are provided separately regarding Article 55 for your reference.

USCBC would be happy to further discuss these points and greatly appreciates this opportunity provided by CCCL. We look forward to continuing this cooperation.

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