

## SAIC's First Cartel Case and Final Rules Under the Chinese AML

China's State Administration for Industry and Commerce ("SAIC"), the agency primarily responsible for enforcing the Chinese Anti-Monopoly Law (the "AML") with regard to non-price-related conduct, recently announced its first cartel decision<sup>1</sup> and adopted final implementation rules under the AML, including creation of a new leniency regime.<sup>2</sup> These developments suggest that SAIC is now ready to step up its enforcement activities under the AML, which entered into force in August 2008.<sup>3</sup>

SAIC's decision concerned a non-price cartel organized by a construction material and machinery trade association among concrete producers in Jiangsu Province. SAIC fined the trade association and five cartel participants, but granted immunity to eleven participants. Interestingly, this approach appears to be inconsistent with SAIC's own leniency program as set out in the new implementing rules.

SAIC's implementing rules include (i) the Rules of the Administrative Authority for Industry and Commerce on the Prohibition of Restrictive Agreements (the "Restrictive Agreements Rules");<sup>4</sup> (ii) the Rules of the Administrative Authority for Industry and

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<sup>1</sup> See [http://www.saic.gov.cn/ywdt/gsyw/dfdt/xxb/201101/t20110126\\_103772.html](http://www.saic.gov.cn/ywdt/gsyw/dfdt/xxb/201101/t20110126_103772.html).

<sup>2</sup> The final rules adopted by SAIC follow its May 2010 release of draft rules (the "2010 Draft Rules"). For a detailed review of the 2010 Draft Rules, please refer to our alert memorandum of June 24, 2010, which may be found at [http://www.cgsh.com/saic\\_issues\\_new\\_draft\\_rules\\_under\\_the\\_chinese\\_anti-monopoly\\_law/](http://www.cgsh.com/saic_issues_new_draft_rules_under_the_chinese_anti-monopoly_law/).

<sup>3</sup> In addition, SAIC is reported to have received a complaint from Hudong, an online encyclopedia, which alleged, among other things, that Baidu has abused its dominant position by downgrading and unfairly blocking Hudong's natural search results in favor of Baidu's own encyclopedia service, Baidu Baike. Hudong also requested that a fine of RMB 790 million (US\$ 120 million) should be imposed on Baidu. On March 1, 2011, Hudong announced that it has sued Baidu for allegedly unfair competitive conduct in a court in Beijing. Meanwhile, SAIC has moved the matter to its Anti-Monopoly and Anti-Unfair Competition Enforcement Bureau, which indicates that SAIC may have accepted the case. See <http://w.hudong.com/10840a9a7ef449938cce64d86776b25b.html>.

<sup>4</sup> See [http://www.saic.gov.cn/zcfg/xzgzjgfwj/fgs/201101/t20110107\\_103375.html](http://www.saic.gov.cn/zcfg/xzgzjgfwj/fgs/201101/t20110107_103375.html).

Commerce on the Prohibition of Abuse of Dominant Market Positions (the “Dominance Rules”);<sup>5</sup> and (iii) the Rules of the Administrative Authority for Industry and Commerce on the Prohibition of Acts of Abuse of Administrative Power to Eliminate or Restrict Competition (the “Administrative Power Rules”; together, the “SAIC Final Rules”).<sup>6</sup>

The SAIC Final Rules are unclear in a number of respects and are likely to give rise to many practical questions. As noted, however, SAIC seems poised to increase its AML enforcement activities, as does the National Development and Reform Commission (“NDRC”), which also recently finalized its implementing rules for investigating possible price-related antitrust violations and adopted its own, somewhat different, leniency program.<sup>7</sup> SAIC’s and NDRC’s overlapping jurisdiction in cases involving both price- and non-price-related conduct, and the differences between their rules, create a potential for inconsistent enforcement.<sup>8</sup>

## **I. CONCRETE CARTEL DECISION**

SAIC’s decision sanctioning the concrete cartel is SAIC’s first published cartel enforcement decision.<sup>9</sup> The cartel was organized by the construction material and machinery trade association in Jiangsu and resulted in sixteen concrete producers reaching an agreement with the association to divide concrete sales markets. Thereafter, the agreement was actively enforced. For example, the association requested participants to register their sales contracts and fined companies for failing to comply with the agreement.

SAIC found that the association and the sixteen companies violated Article 13 of the AML (prohibiting restrictive agreements among horizontal competitors) by dividing the sales market and restricting competition. Article 16 of the AML prohibits trade associations from organizing members to engage in anti-competitive conduct. Consequently, the

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<sup>5</sup> See [http://www.saic.gov.cn/zcfg/xzgzjgfwj/fgs/201101/t20110107\\_103376.html](http://www.saic.gov.cn/zcfg/xzgzjgfwj/fgs/201101/t20110107_103376.html).

<sup>6</sup> See [http://www.saic.gov.cn/zcfg/xzgzjgfwj/fgs/201101/t20110107\\_103377.html](http://www.saic.gov.cn/zcfg/xzgzjgfwj/fgs/201101/t20110107_103377.html).

<sup>7</sup> For a detailed review of the NDRC rules, please refer to our alert memorandum of January 17, 2011, which may be found at <http://www.cgsh.com/news/List.aspx?practice=2&geography=46>.

<sup>8</sup> Note that the agencies have indicated that they will be working closely with each other and they have experimented setting up a case coordination mechanism. See [http://www.nera.com/nera-files/PUB\\_ATSource\\_SAIC\\_0311.pdf](http://www.nera.com/nera-files/PUB_ATSource_SAIC_0311.pdf).

<sup>9</sup> SAIC officials have indicated informally that the agency has investigated several cases, including one involving a multi-national company.

association was fined RMB 200,000 (~ \$30,000; €22,000), reflecting a discount for the association's cooperation with the investigation. Eleven of the sixteen participating companies received immunity from fines as a result of their cooperation with the investigation. The remaining companies were fined, but the amount of the fines was not specified in the decision.

Interestingly, SAIC's decision seems inconsistent with its own leniency program, as described further below. SAIC's leniency program provides for immunity only for the undertaking that first reports the violation, while subsequent reporters may receive only reduced penalties. Here, eleven companies received immunity. As the decision pre-dated the new rules, SAIC may have believed that they were not bound by the new leniency rules. On the other hand, as the new rules do not specify how to determine the "first applicant," SAIC may have applied the term to a group of applicants providing important evidence simultaneously or within a short period of time. Such a broad application of immunity could reduce the leniency program's effectiveness, since potential leniency applicants may be more likely to wait to see what other cartel members will do before filing an application if they think that they may still receive full immunity.

## **II. SAIC FINAL RULES**

The SAIC Final Rules are similar to NDRC's Anti-Pricing Monopoly Rules (the "NDRC Pricing Rules") published on January 4, 2011. Like the NDRC Pricing Rules, the SAIC Final Rules leave many open issues and provide SAIC with significant discretion.

### **A. THE RESTRICTIVE AGREEMENTS RULES**

Article 2 of the Restrictive Agreements Rules prohibits any horizontal agreements, decisions, or other concerted actions that eliminate or restrict competition by restricting output or sales, dividing sales or raw material markets, restricting the purchase or development of new technologies or equipment/products, and engaging in group boycotts. Article 9 prohibits trade associations from organizing restrictive agreements among their members. As noted in Article 15 of the AML, these prohibitions do not apply to certain categories of agreements that have pro-competitive purposes and will not materially limit competition. Notably, the rules do not refer to vertical agreements.

#### **1. Types of Prohibited Agreements**

The provisions regarding horizontal restrictive agreements and group boycotts remain the same as those in the 2010 Draft Rules. Unlike the 2010 Draft Rules, the SAIC Final Rules do not cover vertical agreements that eliminate or restrict competition and harm

consumer's interests. The removal of the ambiguous language in the 2010 Draft Rules is an improvement, but the fact that vertical agreements are not specifically covered may not mean that SAIC considers such agreements to be outside the AML; SAIC may still find a vertical agreement unlawful by applying the catch-all provision in Article 8 of the Restrictive Agreements Rules and Article 14(3) of the AML, which allow SAIC to prohibit "other types of restrictive agreements."

## **2. Concerted Practices**

Like the NDRC Pricing Rules, Article 2 of the SAIC Restrictive Agreement Rules defines restrictive agreements as "agreements, decisions, or other concerted actions" that have the effect of eliminating or restricting competition. Unlike the NDRC Pricing Rules, the SAIC rules define "concerted actions" as actions "where a consensus has in fact been reached amongst business operators, notwithstanding that no agreement or decision has been expressly established, whether in written or oral form." To determine whether practices are "concerted," both agencies consider a range of factors.<sup>10</sup> In addition to the factors considered by NDRC, SAIC will consider prevailing industry conditions and whether the accused undertakings have legitimate reasons for the alleged consistent behavior.

The Restrictive Agreements Rules' ambiguous definition of "concerted action" may lead to legitimate competitive behavior being found in violation of the AML. Moreover, the differences between SAIC's and NDRC's treatment of "concerted actions" may lead to inconsistent enforcement in some cases, with SAIC potentially being less likely to find concerted actions in relation to non-price-related conduct (because it can consider a wider range of explanatory factors).

## **3. The Leniency Program**

Article 11 provides details regarding SAIC's leniency program. Its provisions are largely unchanged from the 2010 Draft Rules and provide that (i) penalties shall be waived for the undertaking that first reports the violation, produces "essential evidence" and cooperates fully and voluntarily and (ii) penalties may be reduced for other undertakings that voluntarily report the violation and produce essential evidence. The final rules clarify that reductions apply to administrative fines but not illegal gains.

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<sup>10</sup> The factors reviewed by both agencies are: (i) the degree of consistency in the relevant companies' behavior; (ii) whether there has been communication of intent among undertakings; (iii) the structure of the relevant market; and (iv) changes in the market.

The rules are ambiguous regarding which types of restrictive agreements are eligible for leniency and the extent of available reductions in penalties. The NDRC Pricing Rules are also vague regarding the scope of the program, but do make clear that the second applicant will receive not less than a 50% reduction, while subsequent applicants can receive no more than a 50% reduction. Furthermore, the requirements to qualify for leniency lack clarity, and it will be difficult for a party to be sure that it has done everything necessary to obtain leniency.

## **B. THE DOMINANCE RULES**

Consistent with the AML, the Dominance Rules prohibit a dominant company from engaging, without valid justification, in refusals to deal, exclusive dealing, tying, and discrimination. While the AML and the Dominance Rules do not require that antitrust authorities prove that the alleged abuse harmed consumers, they do provide that a dominant company can defend its allegedly abusive conduct by providing a “reasonable justification.” The AML does not define what constitutes a “reasonable justification,” but the Dominance Rules provide some general guidance.

### **1. Definition of a Dominant Market Position**

The definition of a dominant position contained in Article 3 of the Dominance Rules is identical to that found in Article 17 of the AML.<sup>11</sup> Like the NDRC Pricing Rules, the Dominance Rules further clarify the phrases “other transactional terms” and “ability to impede or affect other undertakings’ ability to enter the relevant market.”

### **2. Determination of a Dominant Market Position**

In addition to the market-share-based presumptions of dominance,<sup>12</sup> the AML (Article 18), the Dominance Rules (Article 10), and the NDRC Pricing Rules contain nearly identical lists of factors parties must consider when determining whether dominance exists.<sup>13</sup>

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<sup>11</sup> A “market position in which an undertaking has the ability in the relevant market to control the price or quantity of products, or other transactional terms regarding products, or to impede or affect other undertakings’ ability to enter the relevant market.”

<sup>12</sup> Consistent with Article 19 of the AML, Article 11 of the Dominance Rules provides for a presumption of dominance where one company has a 50% share, two companies together have a 66% share, or three companies together have a 75% share. These presumptions do not apply to companies with shares less than 10%.

<sup>13</sup> The factors include the market share of the allegedly dominant undertaking, its ability to control the market in which it is active, and barriers to entry.

However, the Dominance Rules and NDRC Pricing Rules clarify that the analysis must be based on the identification of a relevant market. In addition, unlike the NDRC Pricing Rules, SAIC's Dominance Rules provide short explanations of each of the factors.

### **3. Reasonable Justifications**

Article 8 of the Dominance Rules describes two factors that must be considered when weighing a proffered justification. The factors are: (i) whether the conduct in question is based on business customs, normal business operation and expected efficiencies or benefits; and (ii) the impact of the conduct in question on economic efficiency and social and public interests. The 2010 Draft Rules included a third factor, namely whether the behavior in question will result in eliminating or restricting competition and harming consumers' interests. Unlike the NDRC Pricing Rules, the Dominance Rules do not include examples of specific "reasonable justifications" for prohibited conduct.

### **C. THE ADMINISTRATIVE POWER RULES**

The Administrative Power Rules prohibit administrative authorities from engaging in certain anti-competitive or discriminatory conduct. The provisions are similar to those under the AML and shed no new light on the prohibitions. As per the AML, the Administrative Power Rules provide that SAIC may only make recommendations to the appropriate superior administrative authorities, but it is up to the superior authority to correct the situation.

Interestingly, under Article 5 of the Administrative Power Rules, it is not an acceptable defense for an undertaking to argue that its anti-competitive conduct was (i) ordered by administrative authorities; (ii) authorized by administrative authorities; or (iii) consistent with administrative laws or regulations promulgated by relevant authorities.

## **IV. CONCLUSION**

SAIC's recent enforcement action and its adoption of final implementing rules provide important guidance regarding SAIC's implementation of the AML. The decision and the rules are both vague, however, and they leave SAIC with substantial discretion. Notably, SAIC's first published cartel decision under the AML appears to be inconsistent with its own leniency program.

The SAIC Final Rules, while useful, raise many interpretive questions. The Restrictive Agreements Rules do not adequately distinguish between conduct that should be *per se* prohibited and conduct that should be analyzed based on rule of reason. Moreover, while SAIC's leniency program is intended to increase enforcement activity, the program's

effectiveness may be compromised by questions such as whether multiple entities may be considered together as a “first applicant” eligible for immunity and how much of a reduction the second and subsequent applicants may receive.

In addition, under its new rules, SAIC does not have to show that a restrictive agreement is in fact or likely to be anticompetitive; the undertakings concerned have the burden to show that their conduct is pro-competitive. Similarly, there are no specific requirements under the Dominance Rules that SAIC show that allegedly abusive conduct has an anticompetitive effect. The rules, instead, appear to place the burden on an undertaking to justify its allegedly abusive conduct. Compounding the problem, the categories of prohibited conduct are broadly defined.

Like the NDRC’s rules, the SAIC Final Rules do not deal with questions of concurrent jurisdiction.<sup>14</sup> In addition, the differences in the two agencies’ rules regarding similar conduct will make companies’ compliance efforts more difficult. As noted, however, Chinese agencies have indicated that they will be working closely with each other and they have experimented setting up a case coordination mechanism.

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If you have any questions, please feel free to contact any of your regular contacts at the firm or any of our partners and counsel listed under Antitrust and Competition in the “Practices” section of our website at <http://www.clearygottlieb.com>.

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<sup>14</sup> The question of concurrent jurisdiction arose also from MIIT’s publication of the Draft Internet Rules on January 14, 2011. Similar to Article 6 (1) of the Draft Internet Rules, Article 14 of the Anti-Unfair Competition Law also prohibits defamation of competitors’ products. As SAIC is the primary regulator of the Anti-Unfair Competition Law, it is unclear how SAIC and MIIT would handle the concurrent jurisdiction over a defamation case. For a detailed discussion of MIIT’s Draft Internet Rules, please refer to our alert memorandum, which is available at [http://www.cgsh.com/chinas\\_miit\\_solicits\\_comments\\_on\\_draft\\_internet\\_rules/](http://www.cgsh.com/chinas_miit_solicits_comments_on_draft_internet_rules/).

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