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## KDI FOCUS

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## China's Stronger Enforcement of the Anti-Monopoly Law and Korea's Response\*

Jaehyung Lee, Specialist at KDI

**"Tougher enforcement of the anti-monopoly law in China is expected to open markets and bolster the competition environment. In response, Korean companies must make efforts to take full advantage these changes to expand their business into the Chinese market while avoiding the risk of violating the stricter laws."**

### I. Enactment and Significance of China's Anti-monopoly Law

**China's enactment of the anti-monopoly law is considered a leap forward towards a market economy.**

A symbol of its efforts to accelerate the transition into a market economy via the establishment of competition as a fundamental of market activities, China's anti-monopoly law(反壟斷法)<sup>1)</sup> was enacted on August 30, 2007 and entered into effect on August 1, 2008.

The "socialist market economy" China is pursuing is substantially different from the common notions of a market economy in terms of basic principles and goals. However,

\* This study is based on Jaehyung, Lee, "China's Strengthening of Competition Law Enforcement and Korean Companies' Opportunities," in Kyungsoo Choi (ed.), *China's Economic Structural Changes and Korea's Opportunities*, Korea Development Institute, 2015 (forthcoming).

1) Competition law aims to build competitive market conditions by prohibiting monopolistic practices and stimulating competition, similar to Korea's Monopoly Regulation and Fair Trade Act, the US' Antitrust Laws, Japan's Antimonopoly Act and EU's Competition Law.

the latter is utilized as a means, albeit to the necessary extent, to eliminate the negative vestiges of socialism past and bolster efficiency based on free market competition.

Since the enactment of the law, China has imposed anti-monopoly sanctions on several global multinationals including Qualcomm, Google, Coca-Cola, Western Digital, Nestle, Samsung, LG, Mitsubishi Electric, Panasonic and even state-owned telecommunications companies such as China Telecom and China Unicom.

To expand business opportunities in China, taking full advantage of the broader openness and liberalization and minimizing the increasing risk of stronger sanctions, Korean companies must be able to foresee the future changes in market competition. As such, gaining an accurate and better understanding of China's competition laws, ranging from the overall mechanism to enforcement trends of the anti-monopoly law, is crucial.

## II . China's Anti-monopoly Law and the Mechanisms of Competition Law

### 1. Competition Environment

China adopted a market economy, but still emphasizes the role of government.

China's socialist market economy is a composite of socialism politically and a market system economically and vastly differs from the general perceptions of a market economy. And while the market economy is commonly adopted as a means and ends to achieving efficient resource allocation and consumer benefit protection, China views it as a mere tool in achieving economic development; essentially justifying government intervention when the market economy drifts away from socialist goals. China's market competition environment has two distinctive characteristics.

China's market structure is highly competitive although there exists institutional imperfections that disturb the efficiency of market functions.

First is excessive government intervention in the market and imperfect competition as a result of an immature market economy. Although China's economy has become more liberalized, companies still face severe restrictions<sup>2)</sup> as the government maintains a strong grip of the market, and free competition is limited by the lack of market transparency and predictability resulting from excessive administrative discretion.<sup>3)</sup>

Second is a highly competitive market structure due to the relatively small number of large enterprises compared to the huge land mass and population. A competitive market structure is the underlying condition for free competition, however, many Chinese markets exhibit considerably large imperfections, implying that the presence of a competitive market structure does not necessarily entail active competition. Nevertheless,

2) For instance, in the Chinese market, the government has the right to price all products supplied by state-run enterprises and, where necessary, also those made by private companies.

3) OECD's Indicator of Product Market Regulation (PMR) describes the degree of governmental regulations on the market using a scale from 0 to 6. In 2003, most OECD countries' PMR recorded between 1 and 2, whereas China's PMR was 2.9, the highest among the surveyed countries.

&lt;Table 1&gt; Anti-competitive Practices and Relevant Laws

	Anti-trust law	Price law	Anti-unfair competition law
Abuse of market dominance	○	○	
Business combinations	○		
Cartels	○	○	
Unfair transactions			○
Administrative monopoly	○		○

expectations are high that with the institutional, administrative and business culture conditions in place, this will become the impetus for dynamic competition in the Chinese market.

## 2. A Key Pillar of Competition laws

China's competition laws are comprised of three separate laws: the anti-monopoly law restricts the abuse of market dominance, cartels, business combinations and administrative monopoly; the pricing law controls price-related misconduct; and the anti-unfair competition law suppresses unfair business practices. However, while the anti-monopoly law is in the realms of general competition law, the pricing law and anti-unfair competition law serves as the basis for government intervention on price movements and in banning unfair competitive practices, although certain aspects of the latter are included in the competition laws.

The anti-monopoly law is enforced by three institutions. Under the watch of the Anti-monopoly Committee of the State Council, the National Development and Reform Commission (NDRC) regulates price-related antitrust practices, the State Administration for Industry & Commerce (SAIC) regulates non-price related antitrust practices and the Ministry of Commerce regulates business combinations.

China's anti-monopoly law is a medium for "the sound development of a socialist market economy." In this type of economy, the government has a pivotal role and function, and uses the anti-monopoly law as a vehicle to intervene in the market in order to boost competition and enhance market mechanisms. Notably, the government's role and function will always prevail when they collide with market principles. Moreover, while competition laws in general market economies aim to boost competition i.e. eliminate anti-competitive practices and consider "fair trade" a supplementary judging criteria, "impartiality" is vital in China's anti-monopoly law.<sup>4)</sup>

Anti-monopoly law, price law and anti-unfair competition law constitute China's competition laws.

China's anti-monopoly law is a medium through which to develop a socialist market economy.

4) While fairness refers to the legitimacy of the processes or means in economic activities, impartiality is a broader concept which embraces the legitimacy of the outcome. For instance, problems of impartiality may arise even in cases that involve no unfair practices between the two parties, but one party has a larger profit than the other.

China's anti-monopoly law corresponds to global standards but "impartiality" has become the highest legal purpose and the basis for illegality.

The basic framework for competition laws has been globally standardized and the ultimate mission is to protect the competition system by prohibiting ① the abuse of market dominance, ② business combinations ③ cartels and ④ unfair trade practices. And like most countries, who conform and adapt to these standards, China has also followed suit as its anti-unfair competition law tackles anti-competitive practices.

However, China's anti-monopoly law, although seemingly aligned with global standards, applies a slightly different criteria when it comes to judging illegality. In prohibiting the abuse of market dominance, advanced market economies tend to focus on "obstructive" behavior whereas China targets "exploitative" behavior, with respect to impartiality.<sup>5)</sup> And, when reviewing business combinations, China stresses industrial policy considerations and conducts security reviews for the M&A of domestic enterprises and foreign investors.

China has shown strong willingness to correct administrative monopolistic practices, but the institutional mechanisms to make this happen are not yet properly established.

Another important difference is the regulation on administrative monopolistic practices such as market blockades and discriminate treatment of outside companies. This is common among countries undergoing regime change such as Russia and parts of Eastern Europe, and can be understood as a willingness to minimize government intervention in the market. But, it has been widely expected that the institutional mechanism necessary to put the law into action has yet to be fully realized.

Lastly, unlike the US, Korea and Japan, China imposes only administrative and civil penalties, not criminal penalties, for violations of the anti-monopoly law and the administrative penalty is extreme by global standards.

### 3. Characteristics of Anti-monopoly Law Enforcement

In general, China's competition laws afford the enforcers much discretion with regards to intervention, and due to the many elements that need to be considered, the intensity is often determined by the enforcer's commitment and not by the law itself. Since 2010, however, with general enforcement systems for the anti-monopoly law finding their place and case processing techniques improving, China's implementation of the anti-monopoly law has become much more stricter than anticipated. Recent trends in enforcement can be seen in the following.

First, violations are met with harsh cumulative penalties: ① ceasing of all activities; ② imposing of fines,<sup>6)</sup> as an administrative penalty; and ③ confiscation of unlawful earnings. In February 2015, the NDRC accused Qualcomm of abusing its market dominance and fined the company approximately RMB 6 billion or 1.37 trillion Korean won.

Illegal practices are subject to severe sanctions; Qualcomm was fined approximately RMB 6 billion (1.37 trillion won).

5) Exploitive behaviour refers to practices conducted by market dominators that push for more profit from its trading partners (e.g. high pricing) while obstructive behaviour refers to practices that restrain or limit the business of its trading partners or competitors.

6) China's anti-monopoly law imposes administrative penalties (罰款) for violations of the anti-monopoly law. Similarly, Korea and Japan impose penalty surcharges (課徴金). Korea's has two roles 1. to confiscate illegally earned profits and 2. punish while Japan's has one role, confiscate illegally earned profits.

&lt;Table 2&gt; Penalty Scale of Major Anti-monopoly Cases

Case	Fine	Decision
Shandong Weifang Shuntong Pharmaceutical Co. Ltd. for the abuse of market dominance	7	2011
Insurance companies in Hunan for market segmentation and price-fixing cartels in the auto insurance market	2	2012
LCD manufacturers for price-fixing cartels*	353	2013
Foreign powdered milk manufacturers for resale price maintenance*	669	2013
Premium liquor producers, Maotai and Wuliangye, for resale price maintenance	467	2013
Japanese auto-part makers for price manipulation*	1,235	2014
Japanese bearings manufacturers for price-fixing cartels*	194	2014
Qualcomm for abusing market dominance*	7,610	2015

Note: RMB 1 = 177 won as of Apr. 12, 2016.

\* denotes cases involving foreign companies.

Source: For detailed cases refer to Lee Jaehyung (2015).

Second, when an anti-competitive practice falls under more than one competition law, the anti-monopoly law will generally take precedence. As for gray areas where there is an overlap in jurisdiction of all three laws i.e. anti-monopoly law, pricing law, anti-unfair competition law, it is often the case that the penalty will again be determined by the anti-monopoly law, which has the harshest penalties.

Third, impartiality is at the core of the anti-monopoly law and this is often reflected in the enforcement. In abuse of market dominance cases, in particular, the government will consider excessively high prices, themselves, a violation. In fact, the majority of violations cases are for excessive pricing.

Fourth, despite being in the incipient stage, the government has successfully enforced the anti-monopoly law beyond China's borders. Numerous multinational cartel cases involving foreign LCD manufacturers and Japanese auto-part makers were exposed and heavily fined. Additionally, as seen in Panasonic's acquisition of Sanyo, China is increasingly expanding its jurisdiction in offshore transactions (business combinations), signifying its growing intent to intervene in any such case that might have an impact on the Chinese market.

Fifth, China's anti-monopoly law has been met with criticism from the outside world, who are arguing that the law discriminates against foreign companies and is misused as means to implement industrial policy. Although it is difficult to prove that the law is discriminative in cartel and abuse of market dominance cases as the government has probed both domestic and foreign companies, it is markedly evident in business combination cases, almost all of which involve foreign companies.

Sixth, anti-monopoly law enforcers are particularly strict about intellectual property rights. In general market economies, this would not fall under the auspices of competition law and would only become a problem if a specific practice unfairly obstructs or excludes a certain company. On the contrary, China's anti-monopoly law imposes the same harsh regulations as those applied in market dominance abuse cases.

China has actively applied its anti-monopoly law to cases of international cartels and business combinations with foreign companies.

It has been pointed out that China's law enforcement has problems including lack of independence, forced investigations and excessive discretionary power.

Seventh, the actual enforcement of the law is riddled with procedural flaws. Doubts have been raised about the independence of the authorities. And there are concerns over their excessive discretionary power, forced investigations, transparency issues during processing and lack of protection of the rights of those under review.

### III . Assessment and Response

#### □ Outlook for China's Anti-monopoly Policy

Nine years have passed since the initiation of the anti-monopoly law in China. The government has successfully swept off initial concerns over whether the law could be enforced effectively, and has continuously strengthened its abilities, putting in consistent efforts to enhance relevant regulations, reinforce professionals and experts and upgrade the capabilities necessary for case reviews.

China plans to continue to strengthen the enforcement of the anti-monopoly law. President Xi Jinping's reform is focused on transforming the current government-driven economy into one that is equipped with more active market functions, and the anti-monopoly law will be central in this endeavor. In particular, it is highly possible that the government will reinforce the monitoring of monopolistic practices in state-run and foreign-invested companies, taking into account public opinions and consensus. And although little has been achieved in resolving administrative monopoly, it seems that a broad social consensus on the necessity for reform has already been established.

Marked or tangible outcomes may not be likely in the short-term due to certain barriers, but a gradual improvement is expected as the market economy matures, the anti-monopoly law is better enforced and social consensus grows against administrative monopolistic practices. Accordingly, there will be an undeniable ripple effect on the Korean economy as well as on Korean companies and it will serve as both a risk(short-term) and an opportunity(long-term). Given that there is no way to directly influence China's domestic laws, Korea must accept China's stronger enforcement of the anti-monopoly law as a changing condition in China-Korea economic relations(or in the Chinese economy) and explore the appropriate response measures.

#### □ Short-term Risk Factors and Responses

In the short-term, Korean companies will feel the increased burden. But, then again, the majority of violations included in China's anti-monopoly law have already been banned in most other countries. In this regard, Korean companies in China operating in compliance with the law will also be fulfilling their duty as a global company.

China will likely further strengthen the enforcement of the anti-monopoly law.

China's stricter anti-monopoly law must be viewed positively and Korea should actively work to adapt.

It should, however, be noted that China's criteria for judging illegalities differ, and hence all possible risks should be eliminated beforehand. For instance, while it is not difficult to avoid cartels as they are prohibited in most countries, avoiding abuse of market dominance could be more complicated as China's anti-monopoly law considers excessive profit (or high prices) a violation. As for business combinations, governmental reviews usually involve industrial policy considerations and a security review, meaning that it would be prudent to first broaden understanding and awareness of the relevant authorities and cases before attempting to conduct M&As in China.

Meanwhile, the public sector, including the Korean government, should provide domestic businesses with sufficient information on China's anti-monopoly law. In addition, companies should voluntarily initiate global compliance programs to enhance their understanding and reduce risks.

#### □ Long-term Opportunities

Eventually, stronger enforcement will provide more opportunities for Korean companies as it will help the Chinese market become more open and transparent with anti-monopolistic principles and regulations becoming the basic market order in China. It will also help reduce the costs of searching for and trading with Chinese companies.

Additionally, China's anti-unfair competition law strictly prohibits negative trade practices such as bribery and rebate, and imposes particularly heavy sanctions on any violations. As such, the stricter regulations on administrative monopolistic practices will work to increase Korean companies' access to the Chinese market since their business operations are currently constrained by practices that obstruct free competition and exclude foreign companies such as overly complicated licensing, local governments' market entry barriers, discrimination against foreign companies and closed administrative processes, amongst others.■

China's anti-monopoly law considers excessively high prices to be a violation, and business combinations are reviewed based on industrial policy considerations.

In the long-term, stricter enforcement will provide more opportunities for Korean companies as it increases openness and transparency and removes competition-restricting regulations in the Chinese market.