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## Anti-monopoly law in China: how is it working?

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## This presentation

- Anti-Monopoly Law China 2007 operative 2008 (AML)
- Issues arising from political economy
- Brief comments on content of AML
- General observations on problems
- Focus on merger determinations to date/ Australia as counterpoint
  - Approach of regulators : MOFCOM (China)/ ACCC Australia
  - Procedures and guidelines
  - Market definition
  - Competition analysis
  - Conditions
- Trends

## Elements of political economy

- Move to market economy from 1978 when there was price setting and competition was an unknown concept
- Has picked up pace since 1998 when reform of SOEs intensified
- Accession to WTO in 2001
- Legal “ explosion ” but unsatisfactory enforcement; judges untrained
- Vague legal language and no real concept of competition makes it difficult for judges
- Poor systems of administrative review
- High levels of administrative monopoly
- Perceptions about unfair competition and excessive competition
  - industrial self discipline
- Fears about foreign incursions into market

## The AML prohibitions

- Abuse of dominance
  - market share thresholds, rebuttable presumption
- Monopoly agreements
  - many specifically identified and prohibited unless falling within exemptions
  - exemptions broad
- Mergers and acquisitions
  - compulsory notification over threshold turnover
- Administrative monopoly
- Recognition of the importance of competition as a market regulator

## Potential problems with AML

- Objects are varied and some are at odds with competition itself
  - “promoting the healthy development of the socialist market economy”
  - “ well-ordered market system”
  - - role of industry associations- also talks of protecting orderly competition
- Overlap with existing laws

## Potential problems with AML

- Large number of potential carve-outs
  - Sector specific laws and regulations
  - “Life line” industries (art 7)
  - Farmers
  - By State Council and law
- Broad discretions
- Enforcement- 3 bodies : MOFCOM, NDRC, SAIC
- **TO DATE:** Few cases under most provisions and most by individuals unsuccessful

## Merger law: key questions

- How is market defined?
- Who does the provision apply to?
- What is the test? What are you looking to prevent?
- Is there compulsory notification? What are the thresholds for notification?
- How is the test applied? Is there guidance?
- What is the process? Timing? Confidentiality? Procedural fairness and transparency?
- What are the implications of a refusal by the authority?
- Processes for negotiating an outcome? How formalised?

## Caution in comparisons: vastly differing political economies

### Australia

- purely economic objective:  
“enhancing welfare of Australians through promotion of competition, fair trading and provision for consumer protection” CCA s2
- Robust law, long history of merger analysis

### China

- Similarities with Australia but additional objectives:
  - promotion of socialist market economy (AML Art 1)
  - voluntary concentration improving market competition (AML Art 5)
  - role of SOEs in economy/industry policy
- Developments but not truly detailed determinations by MOFCOM

## China

### AML Art 28

- Prohibits concentrations which will or may eliminate or restrict competition
  - Merger factors
  - Will allow if parties prove that advantages exceed disadvantages
  - Additional national security review for foreign parties
- 
- Notify MOFCOM over threshold turnover levels
  - Phase I, Phase II review

## Australia

- S50 CCA
- Substantial lessening of competition test
- Merger factors
- Informal clearance, formal clearance, authorisation
- Self assessment of risk- no obligation to notify regulator
- Regulator may take court action to prevent a merger

## Notifications

### China

- 384 mergers from 2008 to the end of 2011
- many mergers are not notified hence new guideline on failure to notify

### Australia

- 345 mergers in 2010-2011 financial year without compulsory notification

### China

- Only obliged to issue written reasons if a merger is declined or conditions are imposed
- Very small number of decisions from which we can learn
- No learning, for example, on issue of public interest, or when the advantages of a merger might outweigh the disadvantages

## Merger analysis

How does Australia approach the analysis?

- Market definition (SSNIP test)
- Market shares/concentration (HHI, CR<sub>n</sub>)
- Competition effects in the absence of countervailing power
- Unilateral effects
- Co-ordinated effects
  
- Buyer power
- Entry( timeliness, likelihood, sufficiency)
- Efficiencies
- Failing firm test

## What is a market?

- Traditional view is that it is an area of close competition which assists in the determination of market power in a particular set of circumstances
- Other countries: product, geography, function and time
- Australia: “field of actual and potential transactions”
- AML “ product scope or territory where undertakings compete” with little more guidance (Art 12)
- Guidelines on Definition of Relevant Market
  - stress importance of methodical and appropriate definition
  - use “hypothetical monopolist test”/ HHI/SSNIP test

## Market: determinations of MOFCOM

### **InBev/ Anheuser Busch**

-“beer market in China” without additional comment

### **Pfizer/Wyeth, Panasonic/Sanyo, Novartis/Alcon**

-more detailed analysis but still limited information

- Undue emphasis on mere overlapping markets?

### **Coca Cola/ Huiyuan Juice Group**

-Carbonated beverages

-“Chinese fruit juice industry”

-“fruit juice beverage market”

- No real discussion of the relationship between the two markets

## Market :determinations of MOFCOM

### **General Motors/Delph**

- Market for passenger cars and commercial vehicle
  - 10 auto parts markets
- “Chinese domestic market” but competitive impacts considered in the “global and Chinese auto parts market”

### **Uralkali and Silvinit**

- Potash (internationally traded commodity)
- market for imports or seaborne trading of all grades of potassium chloride to China

### **Savio and Alpha V**

- Electronic yarn clearers for automatic winders
- Same market proportions of the subsidiaries for both the world and China

## Market: determinations of MOFCOM

### **GE and Shenhua Coal**

- Joint venture
- Market for licensing coal gasification techniques in China

### **Samsung Electronics and Seagate**

- Worldwide hard disk drive (HDD) market
- Submarkets for different end uses such as servers, desktop computers, laptops and consumer electronics but no discussion of functional level
- Western Digital Corporation and Viviti Technologies**
- similar market definition

### **Henkel Hong Kong/Tiande Chemical**

- three upstream, midstream and downstream chemicals in the industrial production chain were separate product markets

## Conclusions on MOFCOM market definition

- National market is the most common finding
- MOFCOM routinely consults thoroughly with interested parties, and third party experts and parties have the opportunity to address specific MOFCOM concerns prior to final determination

**BUT**

- Undue emphasis on areas of overlap
- Very broad geographic markets always
- Views of 3<sup>rd</sup> parties and unsuccessful arguments not documented
- Despite apparent growing sophistication of decision making, reasons are still scant and comprise conclusions rather than reasoning

## Conclusions on MOFCOM market definition

- Latest decisions are more sophisticated
- More considered comments
- Still some emphasis on areas of overlap between the parties

BUT

- Reasons are slightly fuller and contain more detail although the emphasis is still on the conclusions of MOFCOM, and not on how they got there

## Market definition in Australia

- Quantitative and qualitative issues considered
- Markets may be small in the context of the national economy but substantial in the context of a State or regional economy

### *Product market*

- Coca Cola/Berri Juice

### *Geographic market*

- Australian Meat Holdings
- AGL

### *Functional market*

- QIW Retailers v Davids
- Re QIW
- ACCC v Metcash

# The law, merger guidelines and analysis: China

Article 27 prohibits concentrations which eliminate or restrict competition, but if advantages exceed disadvantages will be allowed

Merger factors:

- Market shares and market power
- Market concentration
- Effect of concentration on market access and technological progress
- Effect on consumers and other businesses
- Effect on national economic development
- Other factors that affect market competition at MOFCOM discretion

## Various guidelines

Including:

- Provisional Rules on Assessment of Competitive Effects of Concentration of Business Operators 2 September 2011 (operative 5 September 2011) (“Merger Guidelines”)
- Draft Interim Measures on the Investigations and Handling of Concentrations Not Notified in Accordance with Applicable Laws 13 June 2011

Foreshadowed at recent BRICS conference for next 12 months:

- Rules on imposing restrictive conditions on concentrations of operators
- Rules on investigation and handling of violation of notification obligations
- Rules on mergers below thresholds

## General comments on MOFCOM Competitive Effects Guidelines

- Recognise both unilateral and co-ordinated effects but little discussion on impacts of these
- Market share an important starting point but other factors important: current state of competition in market; whether parties close competitors; excess capacity; countervailing market power; financial and technological advantages of merging parties;
- HHI but no thresholds for safety, so no real guidance on possible outcomes
- Focus on heightened barriers to entry
- Merger may increase economic efficiency or have negative effects
- Concentration may increase competitive pressure in markets
- Healthy development of industry and national economic development (interplay between competition policy and industrial policy)
- Risk of insolvency without indication of how it will be treated

## Analysis in practice

### **InBev/ Anheuser Busch**

- very brief
- no real discussion of shareholdings and effect in determination except to say that the concentration was very big

### **Coca Cola/ Huiyuan Juice Group**

- rejected
- reliance on Australian determination
- denial that industry policy played a part

## Analysis in practice

### **Mitsubishi Lucite**

- market share of companies in MMA 64%
- dominant position and forced divestitures including right of purchaser to purchase MMA products for 5 years
- Structural conditions: Mitsubishi not to acquire or establish additional plants for 5 years, nor acquire producers of MMA, PMMA or cast sheets in China or establish plants for these products

### **General Motors/Delphi**

- vertical merger
- Delphi a major supplier to many car mfrs/confidential information and might make switching difficult
- Behavioural conditions: after the concentration Delphi must continue to supply domestic customers without price discrimination or unreasonable conditions

## Analysis in practice

### **Pfizer/Wyeth**

- more complex consideration “HHI”, although always dependent on the correct market definition
- market seems to just include the areas of overlap on many occasions

### **Panasonic/ Sanyo**

- 3 separate battery markets ,
- importance of brands
- divestiture included part of jv share and renaming the jv without use of “Panasonic”

### **Novartis/Alcon**

- compounds market parties had large market share globally although only 1% in China- query whether this lessens competition in China
- care products- links between the parties made it more problematic

## Analysis in practice

### **Uralkali/Silvinit**

- considers unilateral effect, co-ordinated conduct, market position, position of competitors, barriers to entry, impact on customers and suppliers

### **Savio /Alpha V**

- Alpha V would have capacity to influence the operations of Uster (52.3%) and Loepke (47.7%), the only two manufacturers of the machinery worldwide
- Finding that there was a likelihood of co-ordinated conduct which would restrict or eliminate any competition

## Analysis in practice

### **GE/ Shenhua Coal**

- Water coal slurry gasification technology licensing jv
- Process transforms coal from its hard form to coal water slurry, which is processed to produce gas-only 3 in the market
- Shenhua was the largest producer of appropriate coal and vertically integrated with transport by road, rail and ship
- MOFCOM found that the technology, patents, and economies of scale meant barriers to entry were very high
- Behavioural conditions were imposed to prevent the tying of coal supply to technology and vice versa

## Analysis in practice

- Seagate/ Samsung
- - behavioural conditions imposed to keep businesses separate for a year, expand the Samsung business and not to force exclusivity arrangements on customers

# Conclusions on determinations

- There is generally no discussion in the determinations of how the merger factors are applied even though the concepts are sometimes mentioned
- There is no discussion of rejected arguments or other points considered, either of third parties or MOFCOM itself
- There appears to be an undue focus on market share and areas of overlap between the parties particularly in earlier determinations
- Industry policy may play a part despite denials but this is not well explained
- More recent determinations show a significant increase in sophistication with some reasoning now demonstrated

# Australia

## **Merger factors in s50(3) of the CCA explained in Australian Merger Guidelines**

- 70 pages of information on how the ACCC will consider the factors contained in s50(3)
- test of whether there is or is likely to be a substantial lessening of competition is “future with or without” the merger

## Australia: Merger factors

- Import competition s50(3)(a)
- Barriers to entry s50(3)(b)
- Concentration s50(3)(c)
- Countervailing market power s50(3)(d)
- Ability to increase prices or profit margins s50(3)(e)
- Availability of substitutes s50(3)(f)
- Dynamic characteristics innovation and product differentiation s50(3)(g)
- Removal of an effective and vigorous competitor s50(3)(h)
- Vertical mergers and vertical integration s50(3)(i)

Other issues : Failing firms

## Remedies imposed by regulators

### **Australia: court enforceable undertakings**

- Coca Cola / Berri – not acceptable
- Toll/Patrick- detailed and both structural and behavioural

### **China: relationship between harm and conditions often vexed issue**

- Potash case- structural and behavioural
  - open-ended
  - maintenance of current sales practices
  - continue full range of supply insufficient quantities
  - maintain existing negotiation practices

DO THESE CONDITIONS INHIBIT MARKET FLEXIBILITY?

**More recent determinations are more easily understood and better justified**

## National Security Review

### China

- AML Art 30
- Measures on Implementation of Security Review of Mergers and Acquisitions of Domestic Enterprises by Foreign Investors (Measures)  
25 August 2011
- Wide view of “national security” including economic security

### Australia

- Foreign Investment and Takeovers Act 1975
- Foreign Investment Policy
  - undertaken in parallel but outside competition law
  - rarely prevented but new rules on SOEs

## Trends

- China has made significant progress with AML
- Little successful general enforcement
- Only one administrative monopoly case reported
  
- MOFCOM more active
- MOFCOM approach developing significantly but more information is still needed such as:
  - more detailed analysis of market
  - details of submissions of competitors and third parties
  - rejected arguments and theories
  - more detailed conclusions on anti-competitive impact
  - reasons why imposed conditions would alleviate harm
  
- Establish a body of experience for education and understanding