



Conduct Rules Under China's Anti-Monopoly Law Throw Out Your Old Rulebook...

27 August 2009

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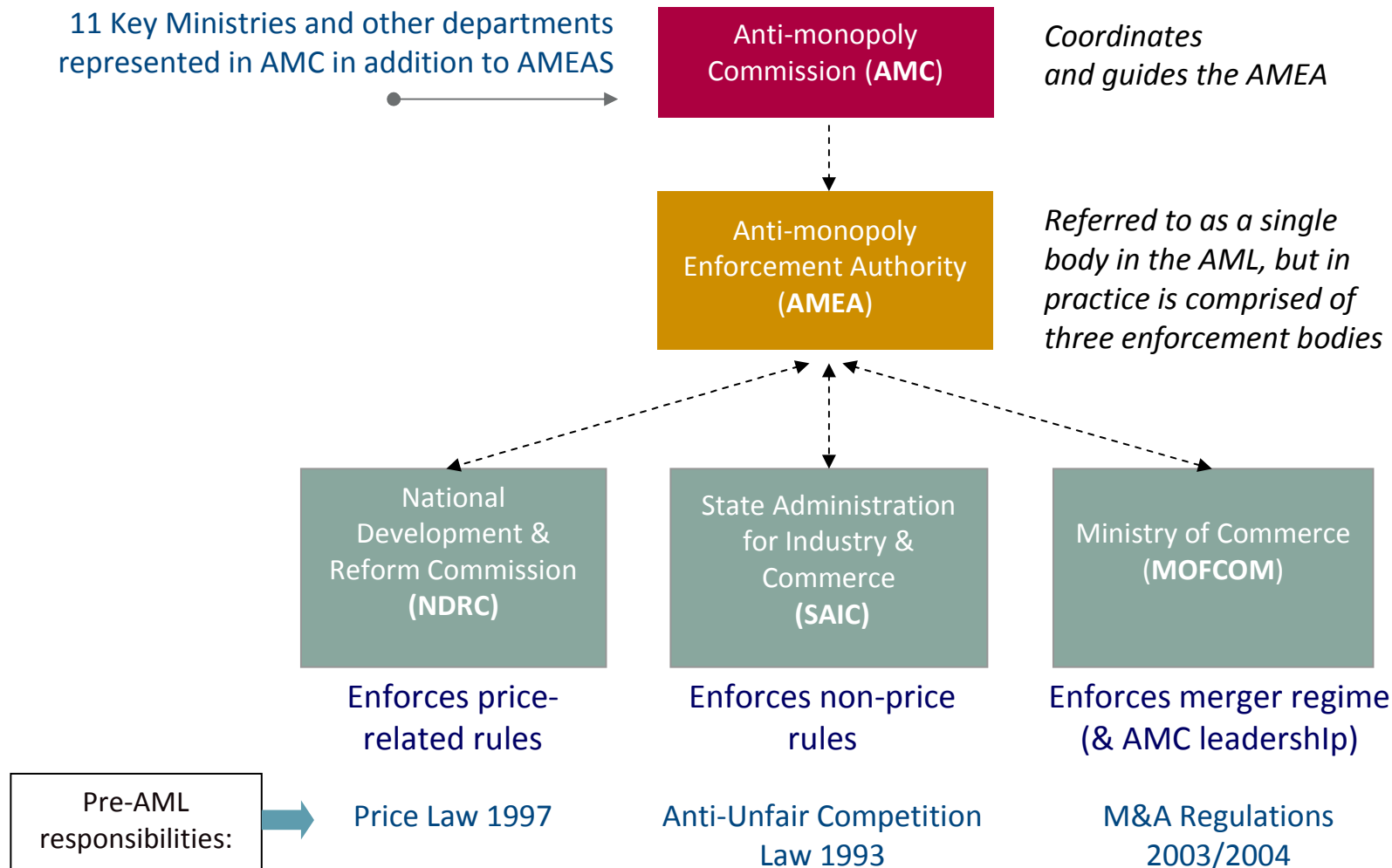
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Agenda

- General Update - The AML One Year On
 - Enforcement structure
 - Progress towards finalising regime rules
- Conduct Rules
 - Current state of enforcement
 - Recent private actions / allegations
 - What we know about permitted / prohibited conduct
 - Minimising risks in a climate of uncertainty
- Merger regime
 - MOFCOM's record to date
 - Latest information & insights

General update - AML enforcement structure



General update - Progress towards finalising regime rules

		Drafting & closed consultation	Public consultation	Finalisation
MOFCOM	• Mandatory notification turnover thresholds			
	• Types of transactions qualifying for review			
	• Required contents of a notification			
	• Turnover calculation for financial institutions			
	• Guidelines for consultation and notification			
	• Evidence gathering - smaller scale transactions			
	• Evidence gathering - failures to notify			
	• Guidelines for MOFCOM reviews			
NDRC	• Identifying price-related AML violations			
	• Investigations and prosecutions			
SAIC	• Identifying non-price-related AML violations (x2)			
	• Investigations and prosecutions			
All AMEAs	• Guidelines for defining the relevant market			
	• Intellectual Property Guidelines			
COURTS	• Judicial interpretation for civil disputes			

Conduct rules - Current state of enforcement

- The AML is operative, and may be enforced at any time, but...
 - SAC & NDRC reluctant to act for now
 - Stalling likely until guidance documents finalised
 - Reports that >1000 complaints already received
 - Regulatory 'interventions', but not AML enforcement/penalties
 - BHP/Rio Tinto production joint venture
 - Limited scope for MOFCOM merger review may spur the SAIC & NDRC into action
 - Typically limited enforcement of the pre-AML rules is continuing
 - Statistics show a further reduction in cases handled under these laws in 2008
 - PRC businesses have demonstrated willingness to bring private action
 - Likely to play significant enforcement role (& negotiation leverage tool)
- Benefits of delay
 - Significant efforts to train enforcement personnel, readying enforcement processes

Conduct rules - Recent private actions / allegations

- Significant numbers reported, but minimal hearing/review progress

- Recent examples:

Cartels

- Alleged price-fixing re bank card / deposit fees & charges against the Bank of China, Bank of Communications, China Agriculture Bank, etc. (complaint lodged with NDRC in July 09)

Vertical agreements

- Distributors allege Nokia is imposing unlawful vertical resale restrictions (allegations submitted to NDRC, reports in August 09 that court proceedings are also being instituted)

Abuse of dominance

- Defendant - Beijing Breach of China Netcom, alleged to have misused its dominant position by imposition of discriminatory terms (in July 09 entered trial stage before Beijing No. 2 Intermediate People's Court)
- Defendant - Shanda Interactive Entertainment Limited (and sub), alleged to have imposed terms preventing a customer dealing with another company (in July 09 entered trial stage before Shanghai No.1 Intermediate People's Court)

Conduct rules - Existing compliance guidance

- **Pricing** (NDRC has enforcement responsibility)
 - Price-fixing
 - Will be a prime enforcement target, as it is non-controversial & officials can leverage off work by foreign regimes
 - Exercise caution if parallel pricing is common in your industry.
 - Greater care will be required re competitor communications (NDRC has broad powers to draw inferences of 'tacit collusion')
 - Businesses in 'risk' sectors will bear the onus of having records which indicate that trade association meetings and correspondence with competitors did not address the issue of pricing
 - Resale price maintenance
 - Cite pro-competitive reasons for resale price restrictions within agreement & relevant communications
 - Justifications may include maximising the effectiveness & efficiency of the distribution channel and supporting retailers' investments in product promotion
 - Where you face limited competition, 'recommended' resale pricing should be used unless legal advice has been obtained that relevant arrangements qualify for AML exemptions

Conduct rules - Existing compliance guidance (cont'd)

• Pricing

—Unfair high pricing (by dominant firms)

- Note the move away from assessment by 'formula' to factors allowing review of whether the price bears a 'reasonable relation to the economic value of the supply' (as per EU approach)
- NDRC's historical price regulator role will likely mean an emphasis on 'comparative' assessment
- Risk of misapplication, and misuse by private litigants?

—Predatory pricing (by dominant firms)

- Focus is below-cost pricing - but no guidance on how 'cost' should be calculated
- Ensure prices > Average Variable Cost (variable costs ÷ units of output) unless exemptions apply
- No focus on recoupment - unlawful without having to prove will be detrimental to consumers
- Key will be to have processes requiring assessment wherever prices are reduced significantly - to determine risk levels & whether 'justifications' apply (matching competitor pricing, etc). Record keeping also important

—Discriminatory pricing (by dominant firms)

- Pricing differences clearly attributable to variable supply costs (bulk purchases, geographic location of customer, etc) should pose no issues
- Where substantial price differences are negotiated, then consider: (1) Does the differential pricing harm purchaser's ability to compete in its downstream market? (2) Is the purchaser left without options in terms of sourcing the product elsewhere? If 'yes' to both - potential issue

Conduct rules - Existing compliance guidance (cont'd)

- Cartels (dealings with competitors)

(NDRC & SAIC share enforcement responsibility)

- Familiar types of activity addressed
 - Includes price-fixing, market-sharing, output limitations, joint boycotts
 - These 'hardcore cartels' should be per se illegal
 - Except for certain activities of PRC firms, the prospects of qualifying for exemptions almost nil
 - NDRC/SAIC broad discretion to 'infer' cartel agreements & strong investigation powers
- Note the danger of 'guilt by association'
 - Trade associations - ensure staff briefed on risks & when to excuse themselves/record objections
- Leniency regime creates incentives for businesses to 'dob in' competitors
- Think outside the box
 - JVs, settlements & patent disputes = examples of where competitors may 'inadvertently' collude

Conduct rules - Existing compliance guidance (cont'd)

- Vertical arrangements (dealings with trading partners & customers)

(NDRC & SAIC share enforcement responsibility)

- Limiting the territory into which they can sell, or customers with whom they may trade
 - Attempt by SAIC to broaden its powers? If this is retained, additional guidance (e.g. safe harbours) needed
 - Risks if competition detrimentally impacted (should require legal team's prior approval)
- Refusing to sell or to trade in normal market conditions (by dominant firms)
 - A form of the 'essential facilities' doctrine to be applied - application to IPRs?
 - Includes a Supplier offering a Purchaser (P) prices that prevent P trading profitably (and yet no focus on efficiency of P)
- Discriminating against a customer or supplier through the adoption of different commercial or operational conditions (by dominant firms)
- Tying/bundling
- Dictating with whom trading partners can or cannot deal, including via exclusivity terms

Conduct rules - Minimising risk in a climate of uncertainty

- Risks

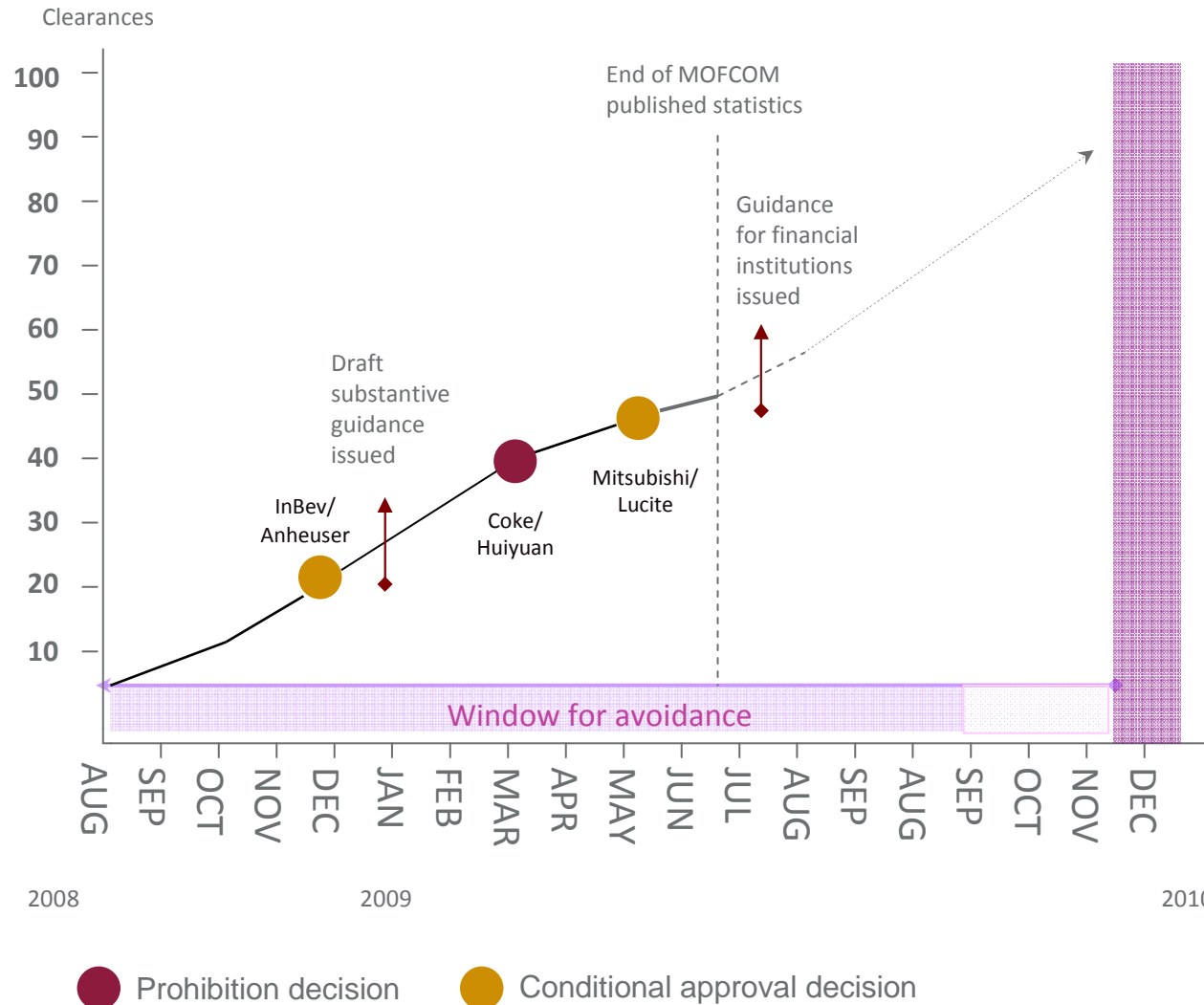
- Investigations based on complaints, regulator initiatives (dawn raids)
- Financial penalties (minimum fines?), confiscation of illegal gains
- Private actions

- Risk management priorities

- Cartels, resale price maintenance, accusations of unfair high prices or blocked access to products
- Training staff involved in price setting / negotiations / competitor communications
- Implementing policies to ensure legal review before the following proceeds:
 - Inclusion of exclusivity terms in contracts, or terms requiring trading partners to limit their area of operations/sales or with whom they deal
 - Requests for supply are rejected (other than for standard/justifiable reasons, e.g. credit)
 - New product offer structures are implemented

- Can you use the AML to your advantage?

Merger regime - MOFCOM's record to date



Under review:

- Sina Corp / Focus Media
- BHP / Rio Tinto ?

Future prospects:

- Finalisation of the substantive guidance
- Penalties for avoidance
- Expedited clearance mechanisms?
- Increase in filing turnover thresholds?

Merger regime - Latest information & insights

- Three key decisions and their implications
 - MOFCOM's decisions are brief and conclusory - little evidence of sophisticated economic analysis
 - Notifying parties will benefit from engaging economic experts & including comprehensive data in notifications
 - MOFCOM will set its own timetables for review (despite AML formalities)
 - Focus on portfolio effects/leveraging (more in common with EU than US)
 - Onus is on notifying parties to show why potential concerns about leveraging existing power into new markets is not justified
 - MOFCOM is consulting the decisions of other jurisdictions when making decisions
 - Foreign precedents should be submitted as helpful indicative reviews, not outcomes to which China should defer
 - MOFCOM favours the use of behavioural (i.e. "in future you will not acquire S...") or structural (i.e. "you agree to divest X now") remedies, rather than prohibiting deals outright
 - Pre-consideration and planning on acceptable remedies, and early engagement with MOFCOM on these, will be crucial when deals raise issues

Visit our dedicated AML resource page:
www.mayerbrown.com/chinaantimonopolylaw

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