COMPETITION AND NEW FRONTIERS (ii): CHINA

by John McLellan

Perhaps the most significant piece of documentation affecting competition legislation in China in recent years was its signing of the WTO Accession Protocol. Prior to China's accession to WTO, its industries were dominated by large state-controlled enterprises. The WTO accession documentation, combined with efforts by the Chinese government to embrace a social market economy (albeit it one with Chinese characteristics), have seen a gradual relaxation in the number of industries allowed to enter through foreign investment and a gradual withdrawal of state support and encouragement of competition and efficiency. There are important exceptions to this relaxation of foreign investment: the media industry (television, publishing and distribution) remains prohibited to foreign investment or is heavily regulated.

Whilst there is piecemeal competition legislation currently scattered through China's current legal framework, there has been a decade-long gestation period of a specific set of competition laws, being the Anti-Monopoly Law (*Fanlongduanfa*), the first draft being published in 2002 (with revisions in April and July 2005). It is due to pass into law within the current legislative plan of the 10th National People's Congress, whose five-year term ends in March 2008.

The draft law draws quite heavily upon existing EU legislation. However, it has been subject to significant scrutiny by a number of foreign organisations, including the American Bar Association.

Scope of the law

The draft is stated to apply to domestic conduct and to foreign activities that "*restrict or affect*" competition within China and identifies four types of anti-competitive conduct. I will now look at each in turn.

(1) Monopoly agreements

The draft prohibits any "*agreements, decisions or other co-ordinated activities*" amongst business operators with the "*object or effect*" of eliminating or restricting competition.

(2) Abuse of market dominance

The draft identifies "*market domination status*", as existing with the "*capability of one or more operator to control price or eliminate or restrict competition in a given market*". This

rather broad definition is quite typical of Chinese legislation and gives significant latitude to the administrative authorities charged with investigation (an Anti-Monopoly Authority will be established by the State Council). The draft goes on to identify situations which will give rise to an inference of market dominance – i.e. where one firm's market share equals or exceeds one-half or more of an industry sector's overall market share; or where two business operators collaterally hold two-thirds or three-quarters of market share.

What actually constitutes instances of *"abuse"* includes predatory pricing, exclusive dealing requirements and unfair trade conditions – much in line with EU regulations.

(3) Merger review

The draft provides for prior notification to the Anti-Monopoly Authority of onshore and offshore concentration of business operators which fall within identified thresholds. Four triggers are specifically identified:

(i) where the market share of any transaction exceeds 20% in China;
(ii) where the consolidation will lead to the market share of any party in China exceeding 25%;
(iii) where the transaction value exceeds Rmb200 million (US$24 million);
(iv) where the combined worldwide assets for sales of the transaction parties exceed Rmb3 billion (US$364 million), at least one party has assets of annual sales in China exceeding Rmb1.5 billion (US$192 million) and the transaction value exceeds Rmb50 million (US$6 million).

(4) Administrative monopoly

Perhaps recognising the historical ties between government and industry, to try to allay fears voiced by foreign enterprises of administrative support of Chinese domestic industries, the draft law targets the possible abuse of government support by actions which may eliminate or restrict competition. These include: compulsory purchases from destinated vendors; restricting proper business activities or market entry; and formulating measures that exclude or restrict competition.

Quite how this legislation will impact upon the entertainment industry has yet to be

seen but a few points are worth noting:

1. In light of the intended new law, the State Administration for Industry and Commence conducted an investigation and produced a report entitled *"The Competition Restricting Behaviour of Multi-National Companies in China and Possible Counter Measures"*. It identified a number of industries where free competition may be threatened by the increasing dominance of multi-nationals within China. On the list were software industries (along with mobile phones, cameras and soft packaging). The report was essentially a warning that foreign business groups are beginning to establish monopolies in those areas in China due to significant advances in technology, skill and capital to achieve competitive advantages and monopoly power, to the possible detriment of local companies and consumers. Given that the media and entertainment industry is one of the most highly regulated industries in China, it is hard to conceive that any of the multi-nationals could exert anywhere near monopolistic control or exhibit anti-competitive behaviour in the market.

2. It remains to be seen whether or not the legislation will bite on domestic operators. The corollary of the high degree of regulation of the media and entertainment industry means that, whilst some degree of decentralisation has taken place, in particular industries such as television, there remain strong and dominant (if not monopolistic) local players. For example, the China International Television Co-operation (CITVC) is a state-owned enterprise which is the only institution licensed by the government to sell overseas satellite television programmes in China. It also, however, produces domestic television content for distribution. Similarly the state-owned broadcaster, China Central Television (CCTV), is the only national broadcaster and, as such, exerts a considerable degree of control over that industry. It is also one of the largest producers of TV programming in China and is in direct competition with a number of domestic and foreign producers. Clearly, the conditions would seem ripe for abuse of clearly dominant positions by both CITV and CCTV. Whilst the law seems not to distinguish between domestic and foreign operators, would the Anti-Monopoly Laws be applied to state-controlled enterprises?

3. The thresholds for merger reviews seem very low, with the result that almost any

merger or acquisition outside of China is likely to trigger referral to the Anti-Monopoly Authority. This raises the spectre that Beijing will join Brussels and Washington as destinations for lobbyists to any significant M&A activities in the media and entertainment industry. Certainly, had the Sony BMG merger taken place post-passage of the Anti-Monopoly Laws, the thresholds would have been triggered, despite the fact that neither company holds a significant market position in China.

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The laws are still in draft form and further revision seems likely – in particular, the threshold for referrals seem to be too low. It does seem, however, that the laws are destined for passage, the key imponderable (as with most laws in China) being the interpretation.

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