RESALE PRICE MAINTENANCE IN CHINA: ONE COUNTRY, TWO SYSTEMS

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At first blush, Article 14 of the 2007 Anti-Monopoly Law of the People's Republic of China ("AML") appears straightforward — resale price maintenance ("RPM") is strictly prohibited in China.[1]

Not so fast.

In China, the legality of RPM depends on the plaintiff. While China's RPM enforcement agency, the National Development and Reform Commission ("NDRC"), utilizes a "*per se* illegal"-like approach in public enforcement of RPM, courts in China have established a more moderate "rule of reason"-like approach for RPM cases brought by private plaintiffs. The two conflicting approaches mirror the different RPM perspectives adopted in the United States ("rule of reason" approach) and the European Union ("*per se*" approach). Graced with an opportunity to unify the two standards in 2017, the Hainan High People's Court unfortunately solidified the divergence in *Yutai v. Hainan Provincial Price Bureau*.[2]

As a result, product manufacturers doing business in China must recognize China's contradictory approach to RPM when determining what, if any, RPM programs to adopt in China.

PUBLIC (NDRC) ENFORCEMENT

The NDRC is the Chinese antitrust agency primarily responsible for public enforcement of RPM policies. Although the AML became law in China in 2007, the NDRC's interest in RPM violations has heightened in the last five years. Since the NDRC ramped up enforcement of RPM, the NDRC's approach to RPM has become clear and is now recognized as the "prohibited in principle, and exempted individually" or "prohibition + exemption" approach.

The "prohibition + exemption" approach mirrors the *per se* rule utilized by the European Union.[3] Like the European Union's *per se* rule, the NDRC does not assess or have to prove the anti-competitive effect of an alleged RPM policy. The NDRC may simply deem the existence of an RPM arrangement a violation of the AML as a monopoly agreement.

As the second half of the name suggests, the NDRC does recognize exemptions to its per se prohibition to RPM. Article 15 of the AML allows a company utilizing RPM to rebut the presumption of illegality if it can demonstrate certain rationales underlying its policy. The recognized exemptions include, but are not limited to: "improving technologies, researching and developing new products"; "upgrading product quality, reducing cost, improving efficiency"; and "achieving public interests such as conserving energy [and] protecting the environment."[4] However, while Article 15 of the AML provides for such exemptions to Article 14's restriction of RPM, the NDRC

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has not once recognized a successful exemption to date.[5] If the investigated party cannot demonstrate an exemption, then the RPM policy is prohibited under the AML.

Companies employing RPM must be wary of public enforcement in China. However, while the NDRC has taken a hard line with regard to RPM enforcement, its investigations thus far have focused on companies with high market share.

PRIVATE ENFORCEMENT

Despite the NDRC's harsh stance, Chinese courts have taken a more moderate approach to RPM. This approach, like the "rule of reason" applied in the United States, analyzes the economic effects of the RPM policy.[6]

The Shanghai High People's Court's decision in *Rainbow v. Johnson & Johnson* established the analytical framework to RPM that is used today.[7] The key distinction between the private and public approaches to RPM is that Chinese courts have found that RPM arrangements are only illegal when they have the effect of eliminating or restricting competition. The courts base this requirement on Article 13 of the AML, which states that a "'monopolistic agreement' in this law refers to agreements, decisions or concerted actions which *eliminate or restrict competition*."[8] Ultimately, the Court in *Rainbow* identified four distinct factors for analyzing RPM: (1) the competitiveness in the relevant market, (2) the market share of the entity employing the RPM policy, (3) the purpose and/or motivation for RPM, and (4) the effect of the RPM policy, including a weighing of pro-competitive and anti-competitive effects.[9] The plaintiff bears the burden of establishing the illegality of an RPM arrangement.

Therefore, in civil RPM cases in China, the mere existence of an RPM policy does not itself establish liability under the AML.

YUTAI V. HAINAN PROVINCIAL PRICE BUREAU

On December 21, 2017, the Hainan High People's Court issued a much-anticipated judgment in the first judicial review of the NDRC's approach to RPM. While many believed that the Court would end the five-year-long divergence between the NDRC and Chinese courts, the Court instead recognized and affirmed the different public and private approaches.

While the 2017 *Yutai* case represents a failed opportunity to unify the divergent public and private approaches to enforcement of RPM policies, it did provide guidance as to the future of RPM in China: two distinct enforcement standards persist, at least for now, depending on the plaintiff.

TAKEAWAY

RPM enforcement in China is difficult to predict. In the wake of *Yutai*, product manufactures in China must grapple with two completely different standards of RPM legality. In light of such an unpredictable landscape, product manufacturers must understand the risk-reward balance for adopting RPM programs. Manufacturers with a high market share raise the risk of being on the NDRC's radar for an enforcement action under the "*per se*"-like "prohibition + exemption" standard. However, manufacturers with a lower market share are likely to avoid public

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enforcement and only face private enforcement under the "rule of reason"-like approach. Where these manufacturers have a business justification for an RPM program, the use of RPM is a measured risk with significant business benefits.

Moreover, manufacturers can attempt to lower their risk of enforcement by adopting Unilateral Policies, one type of RPM.[10] A Unilateral Policy involves a manufacturer's unilateral *announcement* of (1) the minimum advertised or resale price of select goods, and (2) the refusal to deal with resellers advertising or selling below those prices. The AML specifically prohibits "monopoly *agreements*,"[11] and the essence of a Unilateral Policy is that it is *not* an agreement. Therefore, Unilateral Policies may prove to be a safer avenue for product manufacturers to implement RPM under either standard of RPM enforcement in China.

Notes

[1] Article 14 of the AML states: "Any of the following agreements among business operators and their trading counterparts are prohibited: 1) fixing the price of commodities for resale to a third party; 2) restricting the minimum price of commodities for resale to a third party; or 3) other monopoly agreements as determined by the Anti-monopoly Authority under the State Council." Article 14 of the AML (adopted August 30, 2007, at the 29th Meeting of the Standing Committee of the 10th National People's Congress, effective August 1, 2008).

[2] The judgment is available at: http://wenshu.court.gov.cn/content/content?DocID=23889d51-88d8-4e87-aaa4-a85c01845f73&KeyWord=%E9%94%90%E9%82%A6.

[3] "In deciding whether an agreement is prohibited under Article 81(1) EC, there is … no need to take account of its actual effects once it appears that its object is to prevent, restrict, or distort competition within the common market." Case C-209/07 *Competition Authority v. Beef Industry Development Society and Barry Brothers* [2008] ECR I-8637, paragraph 16.

[4] Article 15 of the AML (adopted August 30, 2007, at the 29th Meeting of the Standing Committee of the 10th National People's Congress, effective August 1, 2008).

[5] The NDRC has drafted guidelines to clarify these exemptions, which may be enacted a some point in 2018.

[6] In the United States, various forms of agreements or other restraints are reviewed under the rule of reason. "Appropriate factors to take into account include specific information about the relevant business and the restraint's history, nature and effect. Whether the businesses involved have market power is a further, significant consideration." *Leegin Creative Leather Prods., Inc. v. PSKS, Inc.*, 551 U.S. 877, 885–86 (2007) (internal quotations and citations omitted).

[7] The judgment is available at: http://wenshu.court.gov.cn/content/content?DocID=effe7905-b647-11e3-84e9-5cf3fc0c2c18&KeyWord=%E9%94%90%E9%82%A6.

[8] Article 15 of the AML (adopted August 30, 2007, at the 29th Meeting of the Standing Committee of the 10th National People's Congress, effective August 1, 2008) (emphasis added).

[9] See http://wenshu.court.gov.cn/content/content?DocID=effe7905-b647-11e3-84e9-5cf3fc0c2c18&KeyWord=%E9%94%90%E9%82%A6.

[10] However, recent developments in China hint that Unilateral Policies may not provide a solution to resale price maintenance. In 2016, the NDRC provided the Consultation Draft of Guidance for the Automotive Industry, which states: "The key to assessing monopolistic behavior is the effect of restricting competition actually produced by the behavior. According to its competitive effect, *formal unilateral acts such as business policies* may be identified as constituting a vertical monopoly agreement regulated by the [AML]." Article 2, § 3.1 of the Consultation Draft of

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Guidance for the Automotive Industry (Draft for Comments March 23, 2016) (emphasis added). Although the Consultation Draft would only be applicable to the automotive industry if finalized and published, such guidance may provide an indication of the NDRC's approach moving forward with regard to the use of Unilateral Policies in other industries.

[11] Article 14 of the AML (adopted August 30, 2007, at the 29th Meeting of the Standing Committee of the 10th National People's Congress, effective August 1, 2008) (emphasis added).

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