Key Takeaways From China's Amended Anti-Monopoly Law

By Yi Ying, Amigo Xie and Francesco Carloni (August 9, 2022)

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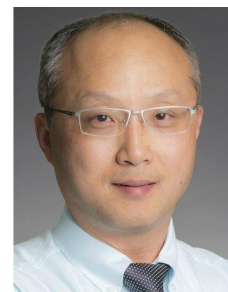
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The People's Republic of China's antitrust regime is aiming to update its overarching framework to address issues identified and to reflect market and economic trends, 14 years after the Anti-Monopoly Law came into effect.

This article highlights and analyzes the most important changes made by the amended Anti-Monopoly Law, in terms of merger control and vertical restraints, in light of the equivalent rules in the U.S. and the EU competition laws. It will do so from the perspective of a market stakeholder.

Merger Control

Implementation of Hefty Monetary Penalty

In recent years, we have seen an increase in active enforcement on issues of improper preclosing coordination in China, often known as gun jumping.

For instance, there have been 215 gun-jumping cases investigated and penalized by China's anti-monopoly enforcer, the State Administration for Market Regulation, or SAMR, to date.[1] Of the 215 gun-jumping cases, 152 penalty decisions have been issued by the enforcer since 2021.

It is easy to see why the existing penalty structure has been accused of lacking a deterrence effect. Under the old regime, fines against gun-jumping violations were capped at 500,000 yuan (about $72,000).

In addition, despite that the enforcer is entitled to unwind transactions that failed to report, it did not force any restoration of an M&A deal until last year.[2] Rather, undertakings are more concerned about the adverse impact on relations with the SAMR in terms of their future filings and cases pending before the same agency.

In contrast, the amended Anti-Monopoly Law increases the fines against relevant antitrust violations, especially for gun jumping, to match the level of fines in other major antitrust regimes such as the EU and the U.S.[3]

The amended Anti-Monopoly Law indicates a fine up to 10%, and potentially 50% in the event of an extremely severe violation, of the gun-jumping violator's revenue in the last financial year if the concentration has or may have an anti-competitive effect.[4]

Even without any anti-competitive impact on the relevant market, a gun-jumping undertaking could be fined up to 5 million yuan (about $720,000),[5] and potentially 25 million yuan (approximately $3.6 million) in the event of an extremely severe violation,[6] which is already 10 times the monetary penalty capped in the old Anti-Monopoly Law.[7]

The penalty mechanism adopted by the amended Anti-Monopoly Law is akin to the practice in the EU. The European Commission may impose fines against gun-jumping undertakings

of up to 10% of their aggregate worldwide turnover in the last financial year, as well as force restoration of the transaction.[8]

Unlike the EU competition law, China's amended Anti-Monopoly Law does not clarify whether its gun-jumping fines are based on violators' global or domestic revenue, although practitioners in China generally believe the latter would be applicable.

In the U.S., a large merger or acquisition subject to the Hart-Scott-Rodino Act[9] may not close until the expiration of the applicable waiting period, or until the government has granted early termination of the waiting period. Failure to comply can result in a fine of up to $43,792 per day — adjusted annually — in addition to orders to unwind the transaction in question.[10]

To-Be-Increased Filing Threshold

China has not adjusted its merger filing revenue threshold since the Anti-Monopoly Law first came into effect in 2008. The following comparison with EU's merger filing turnover threshold may shed some light on why the existing revenue requirement in China is outdated and may catch too many small concentrations without substantive impact on the relevant markets.

The chart also includes a proposed filing threshold set out in a draft merger filing regulation,[11] which solicited public comments in this July in China.

China's old filing threshold	European Union's existing filing threshold	China's proposed filing threshold
• The total worldwide turnover of all undertakings concerned in the transaction in the previous financial year exceeds RMB 10 billion (approximately €1.42 billion), and the PRC turnover of each of at least two undertakings concerned in the transaction in the previous financial year exceeds RMB 400 million (approximately €57 million); or The combined PRC turnover of all undertakings concerned in the transaction in the previous financial year exceeds RMB 2 billion (approximately €280 million), and the PRC turnover of each of at least two of the undertakings concerned to the transaction in the previous financial year exceeds RMB 400 million (approximately €57 million).	*Primary filing threshold* • The global turnover of all the parties exceeds €5 billion in the last financial year; and • The EU-wide turnover of each of at least two parties exceeds €250 million in the last financial year; and • Neither of the parties achieves more than two-thirds of its EU turnover within one Member State. *Secondary filing threshold* • The global turnover of all the parties exceeds €2.5 billion in the last financial year; and • The EU-wide turnover of each of at least two parties exceeds €100 million in each of at least three Member States in the last financial year; and • A turnover of over €25 million for each of at least two parties in each of the three Member States listed above in the last financial year; and • The EU-wide turnover of each of at least two parties exceeds €100 million in the last financial year; and • Neither of the parties achieves more than two-thirds of its EU turnover within one Member State.	• The total worldwide turnover of all undertakings concerned in the transaction in the previous financial year exceeds RMB 12 billion (approximately €1.71 billion) and the PRC turnover of each of at least two undertakings concerned in the transaction in the previous financial year exceeds RMB 800 million (approximately €114 million); or • The combined PRC turnover of all undertakings concerned in the transaction in the previous financial year exceeds RMB 4 billion (approximately €570 million) and the PRC turnover of each of at least two of the undertakings concerned to the transaction in the previous financial year exceeds RMB 800 million (approximately €114 million). • In the event that the above threshold is not met, (a) one undertaking's revenue in the previous financial year in the PRC exceeds RMB 100 billion (approximately €14.2 billion), and (b) any of other merging undertaking(s) or target (i) has a market value or valuation of RMB 800 million (approximately €114 million) or more, and (ii) more than one third of its worldwide revenue was generated from China in the previous financial year.

Meanwhile, the U.S. adopted a combination of the size-of-the-transaction test and the size-of-the-parties test. The HSR Act requires the Federal Trade Commission to adjust both the transaction-size and the party-size thresholds annually based on the country's change in gross domestic product.

For instance, in 2022, the HSR size-of-the-transaction threshold increased from $92 million to $101 million, while the HSR size-of-the-parties threshold was adjusted to $202 million and $20.2 million, respectively, from the previous year's $184 million and $18.4 million, respectively. In addition, the size-of-the-parties test cap grew from last year's $368 million to $403.9 million in 2022.

Killer Acquisitions

In a so-called killer acquisition, powerful incumbents acquire emerging competitors with a relatively small revenue basis, but significant competitive potential in the relevant market. This type of acquisition may result in a winner-takes-all situation and ultimately market dominance.

The amended Anti-Monopoly Law addresses the killer acquisition issue by allowing the SAMR to call in the transaction and require the parties to file, even if the transaction falls below the filing thresholds.

Under the draft merger review provisions, if a below-threshold concentration is closed without a filing, instead of initiating an investigation under the current provisions, the SAMR may request the undertakings involved to file within 180 days and stop implementation of the concentration or take other necessary mitigation measures before the filing is clear.

Moreover, concentrations conducted by undertakings with over 100 billion yuan ($14.8 billion) revenue within China may be subject to merger review if the conditions outlined in the chart above are met. The SAMR appears to be targeting killer acquisitions carried out by large-scale companies, such as internet tycoons or those in sectors where undertakings are small in number yet high in market share and concentration; for example, the active pharmaceutical ingredients sectors.

Nevertheless, it has been criticized that China's antitrust regime lacks transparency in terms of how the enforcer treats general below-threshold transactions.

This is not surprising because the SAMR has yet to publicly investigate or penalize any transaction that does not meet the filing threshold. On the other hand, the more references to below-threshold transactions in the legislation, rather than in low-tier regulations and administrative guidelines, the more scrutiny we may see from the SAMR into such transactions, including the killer acquisitions.

As such, it has become more critical for business undertakings to assess potential anti-competitive effects when planning a transaction, even if the transaction and the relevant parties' revenues do not amount to China's filing threshold.

Major jurisdictions such as the EU and the U.S. have also expressed concern regarding killer acquisitions and are proactively updating their merger control mechanisms to allow enforcers to intervene if deemed necessary.

In 2021, the European Commission found that, in certain industry sectors, particularly in the

pharma and digital sector, killer acquisitions may have flown under the radar. Thereafter, the European Commission published guidance on a new policy, Article 22 of the EU Merger Regulation, which encourages EU member states to request an examination of a concentration that does not meet the national merger filing threshold by the European Commission.[12]

In other words, under the new policy, the European Commission can review transactions that may have a significant impact on the market but fall below the EU and national merger filing thresholds.

The first case referred — first by France, and subsequently joined by Belgium, Greece, Iceland, Norway and the Netherlands — to the European Commission under this new policy is Illumina Inc.'s acquisition of Grail Inc.[13]

The Illumina-Grail deal caught the attention of the U.S. and has been scrutinized by the FTC. The FTC focuses on U.S. merger control laws and their ability to identify and prevent killer acquisitions — transactions that tend to eliminate overlapping research, development and innovation.

The U.S. enforcer also became cautious about well-designed transaction structures, such as patent acquisitions, to dodge the merger control requirements.

Vertical Restraints — Resale Price Maintenance

Rule of Reason Versus Illegal per se for Hardcore Vertical Restraints Including RPM

During the last decade, there has been a disagreement between China's antitrust enforcer and its judicial branch in evaluating hardcore vertical price restraints such as resale price maintenance, or RPM.

The SAMR tends to treat RPM as anti-competitive by nature and therefore illegal per se, while the relevant China courts have ruled that RPM should be subject to a rule-of-reason analysis.

The enforcer may be motivated to catch as much RPM-type conduct as possible, without leaving leeway for the alleged infringers to argue against potential harm to competition and to escape from scrutiny and penalties.

The courts, on the other hand, have taken a more balanced approach in civil litigation by looking at defendants' market share and whether they can demonstrate that their conduct did not give rise to anti-competitive effects.

Such divergent approaches have confused many undertakings doing business in China because the preamendment Anti-Monopoly Law does not explicitly provide how RPM should be evaluated. In contrast, the amended Anti-Monopoly Law clarified that RPM is presumably anti-competitive, but can be rebutted with evidence.

The statute is now aligned with the courts' stance. While the SAMR is entitled to assume, rather than prove, negative effects on competition due to RPM-type conduct, it must be prudent in initiating and examining RPM investigations from now on.

We have observed a similar hybrid approach in the U.S. on RPM issues: mainstream rule-of-

reason analysis plus presumptive anti-competitive effect. Since the 2007 Leegin Creative Leather Products Inc. v. PSKS Inc. ruling by the U.S. Supreme Court, even price-related vertical agreements such as RPM have been assessed under the rule of reason.[14]

However, in practice, the Leegin ruling does not completely shift the legal treatment of RPM to the rule of reason; rather, it adopts one of presumptive legality under the rule of reason to close to per se legality.

By contrast, the European Commission continuously treats both RPM and cartels as anti-competitive hardcore restrictions or "by object," an EU equivalent of per se illegality.

The European Commission and member states' national competition authorities aggressively enforce RPM, which is not block exempt by the European Commission Vertical Block Exemption Regulation[15] and the accompanying Guidelines on Vertical Restraints.[16]

According to the Vertical Block Exemption Regulation and accompanying Guidelines on Vertical Restraints, agreements that restrict a buyer's ability to set resale prices below a certain level, whether directly or indirectly, remain hardcore restrictions.[17]

Nevertheless, the Guidelines on Vertical Restraints recognize that efficiency justifications can be considered under Article 101(3) of the Treaty on the Functioning of the European Union,[18] with the supplier bearing the burden of proof. In this respect, the Guidelines on Vertical Restraints provide few examples of possible efficiency justifications, but state that these considerations are subject to demanding conditions.[19] Outside the scope of these efficiency justifications, RPM is unlikely to pass the test for individual exemption under Article 101(3) of the TFEU.

Safe Harbor

For the first time, market share-based safe harbor is introduced in the Anti-Monopoly Law to cover all industries. Previously, it provided a safe harbor ruling to certain industry sectors, such as the Auto Industry Antitrust Guidelines and the Intellectual Property Anti-Monopoly Guidelines.

The safe habor rule under Article 18 of the amended Anti-Monopoly Law specifically applies to potential vertical restraints.[20] Since the U.S. does not have a general exemption in terms of vertical agreements, the term is more similar to the approach adopted in the EU under the Vertical Block Exemption Regulation.

Although the amended Anti-Monopoly Law does not provide a precise market share threshold for the exemption, a draft regulation overseeing monopoly agreements[21] sets out a 15% safe harbor market share threshold. The proposed threshold disappointed certain market players because the thresholds provided in the auto and IP guidelines have been as high as 30%, which are at the same levels as those set out in VBER.

Since the auto and IP guidelines on safe harbor scope and threshold are lower-tier enforcement guidance, it remains unclear whether they will be overturned by the Draft Monopoly Agreement Provisions or additional sector-based safe harbor rules.[22]

In order for the safe harbor rule to apply, in addition to the market share threshold, vertical agreements must meet other conditions to be issued by the SAMR. This requirement to meet other conditions does not expressly limit the scope of the safe harbor rule to non-RPM vertical agreements.

As such, it is unclear whether RPM as a hardcore vertical restraint may actually benefit from the safe harbor. Previously, the auto and IP guidelines explicitly excluded RPM-type vertical price restraints from their 30% safe harbor thresholds. Whether or not the safe harbor rule can be applied to all vertical agreements, including RPM, requires clarification by the SAMR.

Notably, when we calculate the market share for the purpose of the safe harbor rule, the scope of undertakings is smaller than the scope of undertakings when we calculate the market share in a business concentration. According to Article 15.2 of the Draft Monopoly Agreement Provisions, undertakings include parties to vertical agreements and entities under their respective control.

The SAMR has yet to clarify whether the calculation of an entity's market share includes the market share of its parent company and its sister companies.

In the context of a concentration, those entities are included in the scope of an undertaking and, accordingly, their market shares are counted.

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[1] Including 24 cases investigated and penalized by China's previous anti-monopoly authority, the Ministry of Commerce of the People's Republic of China.

[2] See K&L Gates China Antitrust Update: First Case Requesting Restoration to Pre-Concentration Status | HUB | K&L Gates (klgates.com).

[3] Antimonopoly Law of the People's Republic of China (amended and effective August 1, 2022) (Amended AML).

[4] Id., Art. 58.

[5] Id.

[6] Provisions on the Undertaking Concentration Review (Draft for Comments) 2022 (Draft Merger Review Provisions), available at https://www.samr.gov.cn/jzxts/tzgg/zqyj/202206/t20220624_348145.html.

[7] Id. It is notable that, according to the Draft Merger Review Provisions, the "previous" year for the purpose of determining the turnover basis to calculate the monetary penalty refers to the financial year immediately prior to the closing date of an M&A transaction.

[8] Council Regulation (EC) No. 139/2004 (the EU Merger Regulation), Article 14(2)(b).

[9] 15 U.S.C. § 18a, title II of the original law.

[10] Id.

[11] Provisions on the Undertaking Concentration Filing Protocols (Draft for Comments) 2022 (Draft Merger Filing Provisions), available at https://www.samr.gov.cn/jzxts/tzgg/zqyj/202206/t20220625_348150.html.

[12] EU Merger Regulation, Article 22.

[13] Illumina announced its US$8 billion acquisition of Grail in 2020. The latter built its platform on tests to early detect various cancers that lacked screening options in the United States. Grail was once spun out from Illumina, but it kept relying on Illumina's technology for its products. The acquisition could benefit patient consumers, providing Grail with more of Illumina's market access to reach patients who need an early cancer detection test. Nevertheless, U.S. and EU antitrust authorities believed the concentration would throttle Grail's competitors by their post-deal market shares. On 13 July 2022, the General Court of the EU upheld the EC's competence to review the Illumina/Grail transaction under the new policy. See EC's press release of 20 April 2021, https://ec.europa.eu/commission/presscorner/detail/en/MEX_21_1846 and the EC's Article 22 referral guidance of 26 March 2021, https://ec.europa.eu/competition/consultations/2021_merger_control/guidance_article_22_referrals.pdf. See also Case T 227/21, Illumina v. Commission, Judgment of the General Court (13 July 2022), https://curia.europa.eu/juris/document/document.jsf;jsessionid=11239CE3B3A52290FC2176C134EFB5DF?text=&docid=262846&pageIndex=0&doclang=en&mode=req&dir=&occ=first&part=1&cid=1737297.

[14] Leegin Creative Leather Prods., Inc. v. PSKS, Inc., 551 US 877 (2007) (finding a court evaluating a minimum resale price maintenance agreement must determine whether an agreement constitutes an unreasonable restraint on competition, taking into account "specific information about the relevant business" and "the restraint's history, nature, and effect."

[15] Commission Regulation (EU) 2022/720 (VBER). The new VBER came into force on 1 June 2022. Like the old one, the VBER exempts agreements between suppliers and buyers from Article 101(1) TFEU: (a) if neither party's market share exceeds 30% on the relevant sales and purchasing markets; and (b) the vertical agreement does not contain any hardcore restrictions. Other hardcore restrictions include certain territorial/customer restrictions.

[16] Guidelines on Vertical Restraints (2022/C 248/01) (VGL). The VGL clarifies that the imposition of minimum advertised prices will be treated as an indirect form of RPM (VGL, para. 189). The VGL further clarifies that price monitoring and reporting software, which are increasingly used in e-commerce, are not, in and of themselves, RPM (VGL, para. 191).

[17] Article 4(a) VBER.

[18] Article 101 (3) TFEU. To satisfy Article 101(3) TFEU, an agreement must satisfy four cumulative conditions: (i) it must contribute to improving the production or distribution of goods or contribute to promoting technical or economic progress; (ii) consumers must receive a fair share of the resulting benefits; (iii) the restrictions must be indispensable to the attainment of these objectives; and (iv) the agreement must not afford the parties the possibility of eliminating competition in respect of a substantial part of the products in

question.

[19] The VGL at para. 197 clarifies that under strict conditions the following practices may be justified by Article 101(3) TFEU: (i) facilitating the launch of new products, (ii) conducting short-term (two to six weeks) price campaigns, and (iii) avoiding free-riding between retailers on pre-sale services in the case of complex products.

[20] Amended AML, Art. 18.

[21] Provisions on the Prohibition of Monopoly Agreements (Draft for Comments) 2022 (Draft Monopoly Agreement Provisions), available at https://www.samr.gov.cn/jzxts/tzgg/zqyj/202206/P020220627368048136678.pdf.

[22] For example, the Auto and IP Guidelines provide a safe harbour for horizontal agreements (i.e., 20% combined market shares), while the amended AML's safe harbour terms only apply to vertical agreements.