

## China Insight



# Are Agreements containing Resale Price Maintenance and / or Minimum Resale Pricing Clauses Illegal *per se*? - New decision of the PRC Supreme People's Court

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Dear Sir or Madam,

Please find our update on the verdict issued by the PRC Supreme People's Court on an administrative retrial case appealed by Hainan Yutai Scientific Fish Feed Co. Ltd.

Kind regards,  
CMS, China

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On 18 December 2018, the PRC Supreme People's Court (the "**SPC**") issued a verdict (which was made publicly available on 24 June 2019) on an administrative retrial case appealed by Hainan Yutai Scientific Fish Feed Co. Ltd. ("**Yutai**").

The summary of the Yutai case is as follows:

Yutai was fined by the Hainan Price Bureau for breaching Article 14 of the *PRC Anti-Monopoly Law* due to concluded (but not implemented in practice) agreements containing resale price maintenance clauses with its distributors between 2014 and 2015 (the "**Relevant Agreements**").

Yutai lodged an administrative lawsuit against the decision of the Hainan Price Bureau with the Intermediate People's Court of Haikou Municipality. The Intermediate People's Court of Haikou Municipality overruled the decision of the Hainan Price Bureau. The Hainan Price Bureau then appealed to the Higher People's Court of Hainan Province, which revoked the decision of the Intermediate People's Court of Haikou Municipality. Finally Yutai applied to the SPC for the retrial of the case. The SPC analyzed in detail and summarized whether the Relevant Agreements constituted vertical monopoly agreements which are prohibited by Article 14 of the *PRC Anti-Monopoly Law*.

## 1. Legal Provisions

### a) *PRC Anti-Monopoly Law*

Article 14 of the *PRC Anti-Monopoly Law* expressly prohibits undertakings from reaching with their trading counterparties agreements containing (i) resale price maintenance clauses; and (ii) minimum resale pricing clause. Such agreements constitute vertical monopoly agreements and are prohibited by Article 14 of the *PRC Anti-Monopoly Law*.

Article 14 of the *PRC Anti-Monopoly Law* also specifies that the PRC competition authorities shall have the discretion to determine other types of vertical monopoly agreements which should also be prohibited by the

b) *The Guide to the Pricing Behavior of Business Operators Dealing in Drugs and Active Pharmaceutical Ingredients in Short Supply*

According to Article 6 of the *Guide to the Pricing Behavior of Business Operators Dealing in Drugs and Active Pharmaceutical Ingredients in Short Supply* (the "**Guide**"), which was issued by the PRC National Development and Reform Commission (the "**NDRC**") and took effect on 16 November 2017, for price-related monopoly agreements, the business operators of drugs and active pharmaceutical ingredients in short supply may claim exemption according to Article 15 of the *PRC Anti-Monopoly Law* ( i.e. the "**Prohibition + Exemption Principle**").

According to Article 15 of the *PRC Anti-Monopoly Law*, an exemption situation exists when undertakings can demonstrate that the monopoly agreements they entered into are for the purposes of improving technology or research and development, enhancing product quality, reducing costs, improving product efficiency or unifying product specifications or standards, enhancing overall competitiveness of small and medium sized enterprises and aiming at achieving public interests such as environmental protection or energy conservation, etc.

As such, according to the Guide, in the industry of drugs and active pharmaceutical ingredients in short supply, based on the Prohibition + Exemption Principle, if the concerned undertakings can prove that the requirements of Article 15 of the *PRC Anti-Monopoly Law* are met, they can be exempted from constituting monopoly agreements.

However, please note that the above Prohibition + Exemption Principle should only apply to the concerned industry as mentioned in the Guide.

## 2. Decisional Practices

Due to the fact that there are no uniform block exemptions under the PRC competition regime, decisional practices relating to the determination and investigation of vertical monopoly agreements between the PRC competition authorities and the PRC People's Courts have not been consistent during the past ten years since the *PRC Anti-Monopoly Law* took effect on 1 August 2018.

a) PRC Competition Authorities

For determination of vertical monopoly agreements, in general, the NDRC, one of the three previous competition law enforcement authorities in the PRC before March 2018, has adopted a strict approach.

In practice, and in various industries, the NDRC, even though sometimes it has made some (simple) analyses on the agreements in question, basically considered that vertical monopoly agreements were illegal *per se* and, therefore, were prohibited under Article 14 of the *PRC Anti-Monopoly Law*. Accordingly, it penalized quite a few undertakings based on this methodology.

In the Yutai case, the Hainan Price Bureau investigated and imposed fines on Yutai because it considered that the Relevant Agreements constituted vertical monopoly agreements as prohibited by Article 14 of the *PRC Anti-Monopoly Law*.

b) The People's Courts

(1) The *Rainbow v Johnson & Johnson* Case: Rule of Reason Analysis

On the contrary, the People's Courts normally conduct rule of reason analyses when it comes to vertical monopoly agreements. They do not consider that these agreements are necessarily illegal *per se*. The People's Courts in the past considered that such agreements which have the effect of eliminating or restricting competition are prohibited by Article 14 of the *PRC Anti-Monopoly Law*. Therefore, the People's Courts considered that the "effect" is one of the important factors in determining whether the Relevant Agreements are prohibited by Article 14 of the *PRC Anti-Monopoly Law*.

Taking the *Rainbow v Johnson & Johnson* case as example, the People's Courts held that vertical monopoly agreements are not illegal *per se*. Therefore, the appraisal of an agreement in its legal and economic context should be conducted, including whether the competition on the relevant market is sufficient, whether the undertaking has a powerful market position, what the motivation of the undertaking is in exercising resale price maintenance and/or minimum resale pricing, as well as what the effect of resale price maintenance and/or minimum resale pricing will be.

## (2) The Yutai Case: Illegal *per se*?

However, the approach in determining vertical monopoly agreements by the People's Court seems to have changed in the Yutai case.

From its decision on the Yutai case, the SPC confirmed the approach adopted by the Hainan Price Bureau. The SPC in particular held in the Yutai case that:

- (a) Since the Relevant Agreements constituted vertical monopoly agreements which are prohibited according to Article 14 of the *PRC Anti-Monopoly Law*, it was not necessary for the PRC competition authorities (i.e. the Hainan Price Bureau) to bear the burden of proof to prove that the Relevant Agreements have the effect of eliminating or restricting competition.
- (b) Yutai failed to prove that the Relevant Agreements met the requirements under Article 15 of the *PRC Anti-Monopoly Law*. Therefore, the SPC held that the Relevant Agreements were not exempted under the *PRC Anti-Monopoly Law*.
- (c) The SPC considered that there are obvious differences between an administrative case and a civil case when it comes to the determination of vertical monopoly agreements:
  - (i) For an antitrust civil case, it is necessary to prove that there is monopolistic conduct which has caused "actual losses". Therefore, take the *Rainbow v Johnson & Johnson* case, which was a civil case, as example, the SPC stated that it was not inappropriate for the People's Courts to investigate whether the vertical agreements had an effect of eliminating or restricting competition and, thus, caused actual losses.
  - (ii) For an administrative litigation case such as the Yutai case, however, the PRC competition authorities (i.e. the Hainan Price Bureau) are not obliged to follow the "actual losses" prerequisite. Therefore, the SPC held that the Hainan Price Bureau was correct in investigating and fining Yutai due to the concluded (but not implemented) Relevant Agreements.

### 3. Conclusion

The SPC held in the Yutai case that vertical monopoly agreements shall be prohibited according to Article 14 of the *PRC Anti-Monopoly Law* unless the concerned undertakings can prove that the Relevant Agreements are exempted according to Article 15 of the *PRC Anti-Monopoly Law*. As such, in the Yutai case the SPC has *de facto* confirmed the approach adopted by the NDRC in respect of vertical monopoly agreements.

In the decision of the Yutai case, the SPC also pointed out that because of the governmental restructuring in 2018, the new competition law enforcement authority – the State Administration for Market Regulation (the "SAMR") – has taken the uniform responsibility for competition law enforcement throughout the PRC. Thus, the SAMR should timely issue guidance on competition law enforcement on vertical monopoly agreements, further clarify enforcement standards and clearly instruct business operators how to abide by the PRC competition law, etc.<sup>1</sup>

The decision of the SPC on the Yutai case is very important in practice and it may have a material influence on the determination of the legality of vertical monopoly agreements.

Therefore, to avoid any possible non-compliance risks under PRC competition law, for safety reasons, it is suggested that undertakings doing business in the PRC should not reach and/or implement such agreements which may qualify as vertical monopoly agreements, as well as other types of agreements which are expressly prohibited by the *PRC Anti-Monopoly Law*.

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<sup>1</sup> On 26 June 2019, the SAMR published the *Interim Provisions on the Prohibition of Monopoly Agreements* (the "Provisions"), which will take effect on 1 September 2019. The Provisions have also adopted the same methodology as the SPC in the *Yutai* case on vertical monopoly agreements.

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In case you have questions or for further information, please contact the author of this newsletter:



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