China issues new Anti-Monopoly Guidelines targeting the Online Platform Sector

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Introduction

On 7 February 2021, the PRC State Council published the Anti-Monopoly Guidelines for the Platform Economy Sector (the “Guidelines”). While a number of changes have been made to the previous consultation draft, the structure and key principles largely remain the same. In particular, the Guidelines may restrict the freedom with which larger firms impose exclusivity obligations, offer subsidies, use algorithms, or analyse big data.

The Guidelines also have the potential to affect acquisitions by dominant firms of smaller players by subjecting those transactions to merger review under the PRC Anti-Monopoly Law (“AML”) even where the current turnover thresholds have not been met. Set out below is an overview of the key provisions and recommendations for firms considering the implications of the Guidelines and how best to comply.

Highlights of the Guidelines

Changes to the Draft Guidelines

A number of key changes have been made to the draft version of the Guidelines released for public consultation in November last year. These changes include, among others:

- Removing the provision that in certain circumstances it is possible to leave the relevant market undefined and conclude that the relevant platform economy player is in breach of the AML; instead, the Guidelines specify that investigation of monopoly agreements and abuse of dominance cases and review of merger filings usually require definition of the relevant market;
- Clarifying that concerted practice does not include parallel behaviour based on a player’s independent decision;
- Removing the provision specifying that exclusive agreement may constitute a vertical monopoly agreement;
- Removing the provision on determination of whether data may constitute essential facilities; and
- Including further justifications for predatory pricing.
**Targets of the Guidelines**

The Guidelines apply to different market participants in the platform economy sector and distinguish between the following platform economy players: “platform operators”, “business operators trading on the platform” and other business operators participating in the platform economy. “Platform operators” refers to the operators providing marketplace, deal matchmaking, exchange of information and such other Internet platform services; “business operators trading on the platform” refers to those offering commodities or services on the Internet platforms. The Guidelines also specify that platform operators may provide products through their platform in addition to provision of Internet platform services.

While the Guidelines do not directly target tech companies that are not active in the platform economy sector, the key principles established under the Guidelines may also be a reference for other tech companies on their compliance with the AML.

**Relevant market**

To determine who is subject to the Guidelines and the extent of the obligations, defining the relevant market will often be required. The Guidelines clarify that how the relevant market should be defined needs to be analysed on a case-by-case basis taking into account the characteristics of the platform economy. The relevant product market may be defined based on the products sold on one side of the platform; multiple relevant product markets may also be defined based on the different products sold on multiple sides of the platform. Where a platform has a cross-platform network effect that can bring sufficient competition constraints on platform operators, it is possible to define the relevant product market based on the entirety of such a platform.

With regard to cases involving abuse of dominance, the first step is to determine whether the relevant company has a dominant market position. Different from the traditional industries, the Guidelines specify that to determine whether a firm has a dominant position one needs to consider the characteristics specific to the platform economy, including market shares (taking into account the transaction value and volume, sales amount, number of active users, click rate, length of use or other indicators) and competition condition in the relevant market, as well as the ability to control the market, financial strengths and technical capabilities, to what extent other business operators reply upon the player in terms of transactions, how difficult it is for other business operators to enter the market and such other factors. This principle was reflected in the *Qihoo vs Tencent* case of the Supreme People’s Court regarding abuse of dominance, in which the court pointed out that in the Internet sector, market share is only a rough indicator and may be misleading in determining the existence of a market dominant position, and that the role it may play in determining market dominance should depend on the specific situation of the relevant case.
Conspiracy by algorithm

Given that in the platform sector the players may conclude a monopoly agreement in a concealed way by using technical methods, the Guidelines also point out that the competing platform economy players may act in concert by collecting or exchanging sensitive price and quantity information or utilising data and algorithms to fix price and allocate markets. Further, the competing business operators trading on the platform may enter into a hub and spoke agreement by leveraging their vertical relationship with the platform or reach horizontal monopoly agreement by making use of algorithm or platform rules under the organisation of the platform operator. Also, from a vertical perspective, the platform economy players may restrict the resale price with counterparties such as distributors by using algorithms.

“MFN treatment”

With regard to the “MFN treatment” (where the platform operator requires business operators trading on its platform to offer it prices and other trading conditions not less favourable than those offered to other third party platforms) the Guidelines do not premise the determination of whether such arrangement is in breach of the AML on the finding that such player must have a dominant position; instead the Guidelines specify that such arrangement may also be deemed a vertical monopoly agreement under the AML. Effects analysis may be required to determine whether such arrangement constitutes a vertical monopoly agreement. Although to date the enforcement authority has not penalised any players for reaching vertical monopoly agreements that are not related to price, MFN clauses may become an area that the authority is likely to focus on in terms of non-price related vertical monopoly agreements.

“Either-or choice” and “Subsidy war”

For “either-or choice” restrictions (where the platform operator intends to prohibit business operators trading on its platform from trading on other platforms at the same time) that are commonly seen in the platform economy sector, the Guidelines specifically point out such restrictions may constitute an abuse of dominance. Other exclusive dealing arrangements may also constitute an abuse of dominance, e.g. by punitive measures including blocking business operators’ online stores, not showing them on search results, setting up barriers in technology and traffic allocation or by incentive measures such as offering subsidies, favourable treatments, traffic resources support and others.

Similarly, for platforms providing massive subsidies to customers to exclude competitors, such conduct may also be considered an abuse of dominance if the platform uses predatory pricing to exclude competitors and may increase prices to gain improper profits and harm fair competition and consumer interests after its competitors are excluded from the relevant market.
Discrimination against customers by using big data

Discrimination against customers by using big data has long been a concern for consumers. The Guidelines provide that in determining whether a platform economy player has abused its dominant position by offering differentiated treatment to counterparties with the same conditions, one may consider whether such player has offered differentiated transaction prices based on the customer’s ability to pay, shopping preference and habits through using big data and algorithm.

Merger filing requirements

The Guidelines also respond to some common issues encountered by tech companies in practice in relation to merger filings, such as how to calculate a platform operator’s turnover. In particular, the Guidelines provide that the enforcement authority may investigate a transaction on its own initiative even if the transaction does not meet the relevant filing thresholds (such as start-ups/new platforms whose turnover is relatively low as they adopt a free or low-price model) but there are facts and evidence showing that the transaction has or may have an adverse effect on competition.

The Guidelines also confirm that transactions involving a contractually control structure are subject to merger review, which further addresses the question of whether a concentration involving variable interest entity (or “VIE”) structures requires a merger filing. A VIE structure is an arrangement often used by tech companies listed overseas, which enables an enterprise listed overseas to indirectly control the domestic entity operating the actual business in China in sectors that are subject to restrictions on foreign investment. The Guidelines have the potential to lead to greater scrutiny of companies using VIE structures and may speed up the recent trend of offshore-listed tech companies returning to China.
The Guidelines illustrate the current focus of the PRC authorities on enhancing antitrust enforcement in the digital sector, following fines recently being imposed on tech companies for failure to comply with merger filing and other competition law obligations and the launch of various enforcement campaigns (including in Shanghai). Given the likelihood of further enforcement action in light of the Guidelines, we suggest companies take immediate action to prepare, including by assessing the risks arising from their current business practices. In particular, participants in the digital sector should undertake the following:

• For platform operators and business operators trading on the platform, conduct a “health check” based on the principles and requirements under the Guidelines and other anti-monopoly laws and regulations. Other tech companies outside the platform economy sector should also take into account the requirements under the Guidelines;

• Given the additional regulatory scrutiny, firms in the Internet and digital sector should review their existing commercial agreements to ensure they do not contain any price fixing or market allocation arrangements with competitors or upstream/downstream companies by utilising algorithm and technical means;

• Assess cautiously the effect on competition and risks of violation in light of the Guidelines and other laws and regulations relevant for the Internet and digital sector for the recent hot issues such as “either-or choice”, “MFN treatment” and “discrimination against customers by using big data”;

• For the leading players in the market, carry out an overall assessment to identify if they may be regarded as having a dominant market position taking into account the characteristics of the platform economy. If it is very likely that a company may be considered as having a dominant position, the company should examine its arrangements carefully to avoid engaging in conduct considered as abusing its dominant position; and

• Keep in mind that transactions involving VIE structures are also subject to merger review; for a transaction that does not meet the filing thresholds, companies need to assess whether the transaction may have an adverse impact on competition which may result in an investigation by the authority on its own initiative.
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