

Competition & Trade Update In China

December 2011

The New Chinese Regulation on Safe Management of Hazardous Chemicals Enters Into Force

On 1 December 2011, the revised Regulation on the Safe Management of Hazardous Chemicals (the “New Regulation”) became effective. The New Regulation¹ (popularly referred to as “State Council Decree 591”) replaces the original Regulation on the Safe Management of Hazardous Chemicals which was in force since 15 March 2002.

The New Regulation imposes a number of obligations on companies (including multinational companies with Chinese presence) who produce, use, purchase and sell, or import hazardous chemicals in China. Some of the obligations are newly introduced or amended by the New Regulation. The most important amendments under the New Regulation can be summarized as follows:

- The New Regulation explicitly authorizes the State Administration of Work Safety of China (“SAWS”) as the main competent authority in charge of the overall safety administration at a national level. Other authorities involved in the administration of hazardous chemicals will support and coordinate with SAWS.
- The New Regulation intends to establish a consolidated “catalogue of hazardous chemicals” to replace the existing three catalogues, i.e., (a) dangerous goods list, (b) highly toxic chemicals, and (c) other hazardous chemicals which are not included in the dangerous goods list. SAWS has the main responsibility of determining, publishing and

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properly adjusting the list of hazardous chemicals. So far the first list of the consolidated catalogue has been published, which includes 60 chemicals “with prior concerns”.

- The New Regulation gives legal effect to two mandatory national standards, which introduce rules that comply with the UN Globally Harmonized System (GHS) for chemicals classification and labeling. Standard GB 13690-2009 is for general rules for classification and hazard communication of chemicals, and Standard GB 15258-2009 is for precautionary labeling. Although the two national standards have already been effective from early this year, it is commonly considered that the 1 December date on which the New Regulation enters into force gives the official legal force to the two standards.
- The existing registration system for hazardous chemicals will be changed. Under the New Regulation, companies producing or importing hazardous chemicals shall register their hazardous chemicals with SAWS and include the following information:
 - ▶ Classification and label;
 - ▶ Physical and chemical properties;
 - ▶ Primary purpose;
 - ▶ Hazardous properties;
 - ▶ Storage, use, and transport safety requirements; and
 - ▶ Emergency response measures

SAWS is drafting an implementing regulation of management on the Registration of hazardous chemicals. The final version is expected to be published in early 2012 and will take immediate effect.

- According to the New Regulation, a special permit will be required by companies using hazardous chemicals in their production in an amount above a certain quantity. The detailed provisions on the quantitative criteria for hazardous chemicals being used for its own production are being drafted by SAWS. Such provisions are expected to be published in early 2012 and will become effective immediately.
- According to the New Regulation, there is no special permit required to incorporate a company engaged in production or storage of

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hazardous chemicals. However, a special “safety permit” is required by companies for the new establishment, renovation or enlargement of a construction project for production or storage of hazardous chemicals.

- The New Regulation introduces new conditions to be met by companies starting a hazardous chemicals trade business (purchase and sale). Companies that trade in hazardous chemicals after 1 December 2011 must have full time safety management staff, emergency plans for hazardous chemical accidents, and necessary equipment for emergency rescue.

The New Regulation shows the increasing level of attention that China is giving to legislations on chemicals, and in particular the prominence of penalties and enforcement. It should be noted that the New Regulation introduces significantly higher fines in many situations. After 1 December, a producer, user, trader or an importer who severely breaches the above obligations may face a fine up to RMB 100,000, or even a suspension of operation. If your company engages in the hazardous chemicals business and either has operations in China or imports from / exports to China, you must be aware of what is necessary to comply with the New Regulation.

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Anti-monopoly Investigation on China Telecom and China Unicom

On 9 November 2011, China’s National Development and Reform Commission (“NDRC”) announced its anti-monopoly investigation (“Investigation”) on China Telecom and China Unicom (the “Telecom’s Companies”) for alleged abuse of dominance in respect of the broadband access market. This is the first anti-monopoly Investigation on China’s state-owned enterprises.

Under China’s Anti-Monopoly Law (“AML”), NDRC is in charge of ‘price-related monopoly agreements and price-related abuse of dominance’. NDRC has recently renamed its Price Supervision Department as the Price Supervision and Anti-Monopoly Bureau and enhanced its workforce by employing 20 new staff.

Background Information

■ Investigation on China Telecom and China Unicom

Based on the NDRC's announcement, the Telecom's Companies are in a dominant position in the broadband access market and they abused the dominance by committing price discrimination under China's AML.

■ News and public information on the Investigation

From news and publicly available information, we understand that:

- ▶ The Telecom's Companies are two nationwide telecommunication giants running and operating frame facility networks.
- ▶ They provide "wholesale access" service to other internet service providers ("ISPs", or "Competitors") and "retail access" service to end-users who include businesses, families, and internet content providers ("ICPs") ("Non-competitors").
- ▶ The Telecom's Companies charge Competitors different Access Fees. They also charge different Access Fees to Competitors and Non-competitors. In other words, they charge their Non-competitors more favorable Access Fees².
- ▶ On 2 December 2011, the Telecom's Companies submitted their respective commitments to the NDRC in accordance with the provision of Article 45 under the AML.

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Legal assessment

Based on a news item, an NDRC official comments that because the NDRC considers the Telecom's Companies to be in a market dominant position, the difference in Access Fees between Competitors and Non-competitors means the Telecom's Companies committed "price discrimination" under the AML. The following legal assessment is made on the assumption that the Telecom's Companies are in a dominant position.

■ Price discrimination under China's AML

² Resulting in the NDRC's Investigation based on public information and news.

▶ Legal provision

Article 17(6) under the AML provides that an undertaking in a dominant position must not abuse its dominance by “applying discriminating treatment on prices or other transaction terms to relative trading parties with equal standing without any justifiable reason.”

▶ About Article 17 (6) of China’s AML

For “price discrimination” to be caught by Article 17 (6), we understand that at least two conditions must be met: (i) the other party/parties to the transactions must have equal standing; and (ii) there is no justification for the dominant undertakings for their conduct.

But as the AML and its implementing rules do not set out express provisions on these conditions, their implementation is at the discretion of China’s authorities.

Therefore, in this NDRC Investigation, we literally need to consider if i) the Telecom’s Companies Competitors have equal standing, irrespective of their size, scale, and profitability, etc; and ii) the Telecom’s Companies’ Competitors have equal standing to their Non-competitors.

We should next consider if the Telecom’s Companies have a justifiable reason for the different prices in terms of the Access Fee applied to them.

Further, theoretically, we should also consider if there has been, or was very likely to be, an anti-competitive effect on the market. In other words, has the Telecom’s Companies’ conduct changed the structure of competition on the relevant market.

■ Price squeeze

However, some Chinese anti-monopoly experts insist that if the Telecom’s Companies’ conduct constitutes abuse of dominance, it is the price squeeze (margin squeeze) rather than price discrimination, which was claimed by the NDRC official.

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Experts who insist on the “price squeeze” theory think that the Telecom’s Companies’ conduct was similar to that of Deutsche Telekom AG (“DT”) in the Deutsche Telekom case.

▶ The Deutsche Telekom case

Similar to DT, the NDRC considers the Telecom’s Companies are in a dominant position and enjoy a degree of price-making right in terms of Access Fees³. And the Telecom’s Companies provide “wholesale access” services to their Competitors and “retail access” services to their Non-competitors. In addition, the Telecom’s Companies charge higher prices for wholesale access than for retail access.

The object or effect (or both) of the different pricing policies between the Competitors and Non-competitors must be that the profit of the Telecom’s Companies’ Competitors will fall so far that they are squeezed out of the market. In this way, the Telecom’s Companies’ market power in the downstream market will be strengthened.

▶ Definition of price squeeze

Under China’s anti-monopoly regime, there is no definition for “price squeeze”.

In the Deutsche Telekom case, the Commission stated that “ ... [A] margin squeeze exists if the charges to be paid to DT for wholesale access, taking monthly charges and one-off charges together, are so expensive that competitors are forced to charge their end-users prices higher than the prices DT charges its own end-users for similar services. If wholesale charges are higher than retail charges, the DT’s competitors, even if they are at least as efficient as DT, can never make a profit, because on top of the wholesale charges they pay to DT they also have other costs such as marketing, billing, debt collection, etc...”.

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³ However, the SOEs should act in accordance with the price cap system in terms of the Access Fee made by the Ministry of Industry and Information Technology.

Possible penalties

■ Penalties under the AML

Article 47 of the China's AML stipulates that if the abuse of dominance is established, China's authorities will order the companies concerned to cease and desist the anti-monopoly conduct, confiscate illegal gains, and impose fines from 1% to 10% of the total sales volume in the previous year.

■ Possible penalties on the Telecom's Companies

As there is no definition of price squeeze under China's anti-monopoly regime, we doubt that the NDRC will deal with the Investigation case using "price squeeze" terminology, even if it uses the same or similar methodology.

But if the Telecom's Companies are fined for "price discrimination" or under the "catch-all" clause of Article 17 (7) of the AML⁴, given their huge turnover⁵, even 1% will be "appreciable"⁶.

Conclusions

As it is the first Investigation of state-owned enterprises under the AML, since the NDRC announced its intention to investigate the Telecom's Companies in November 2011, the spotlight has shone brightly on its findings, its procedures and approach, and the possible penalties it can impose.

Where doubts from China and overseas exist about whether or not China's AML applies to state-owned enterprises, the NDRC's public announcement signalled a positive response.

But, in addition to the NDRC's attitude in handling the alleged abuse of dominance by the Telecom's Companies, it might be more important for

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⁴ Article 17 (7) of the AML: The undertaking in a dominant position, ..., shall not conduct any activities which are considered by the anti-monopoly enforcement authority as abuse its dominance.

⁵ Based on public news, the turnover in previous year for China Telecom and China Unicom was approximately RMB 50 billion and RMB 30 billion, respectively.

⁶ Especially this should be the case under the circumstance that the SOEs submitted their respective commitments on 2 December 2011 in accordance with Article 45 of the AML. Based on Article 45, the authorities may suspend the Investigation if they are satisfied with the content of the commitments as well as the implementation situations thereof.

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We will closely follow the progress of this Investigation.

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