

Anti-monopoly Law

Some key points in the first abuse case on China online retail platform players

On April 10, 2021, the State Administration for Market Regulation (“SAMR”) imposed administrative penalties on a leading Internet company for abusing its dominance in the China online retail market by engaging in “either or” (exclusive dealing) conduct. It was ordered to stop its illegal conduct and was fined CNY 18.228 bn (USD 2.7816 bn), amounting to 4% of its 2019 turnover in China. This amount surpassed the 2015 *Qualcomm Case* (a CNY 6.088 bn fine imposed) to become the highest fine ever imposed in the Chinese anti-monopoly enforcement.

From official announcement about investigation in December 2020 to the final punishment decision, the investigation of this case lasted for five months. It is the first administrative enforcement case for the abuse of market dominance since the release of the *Anti-Monopoly Guidelines for the Platform Economy Industry* (“**Platform Guidelines**”) in February 2021. It has significant instructional value for the application of the *Platform Guidelines*, as well as compliance practice for other Internet platform undertakings. This article will sort out the key points of this case from four different aspects: relevant market definition, market dominance evaluation, “either or” (exclusive dealing) conduct, and the penalty amount. It will also offer suggestions on

compliance for Internet platform undertakings.

I. Relevant Market Definition

According to the penalty decision, the relevant market in this case is defined as “*China’s market for online retail platform services*”. The analysis on relevant market definition is in line with those principles under the *Platform Guidelines*. It considers the characteristics of the platform economy and the details of this case, and thus provides substantial guidance for future multilateral platform undertakings in terms of how to define the relevant market.

1. Online retail platform services and offline retail services do not belong to the same relevant product market.

SAMR followed the approach of supply and demand substitutability analysis and concluded that an online retail platform service is distinct from an offline retail service, constituting a separate relevant product market. Both sides of the platform, i.e., in-platform operators at one side and consumers at the other side were considered in analyzing demand substitutability. From the perspective of (in-platform) operators' demand, offline retail services and online platform services differ significantly in the following four aspects: coverage area and service time, compositions of

operating costs, ability to support operators in matching potential consumers, and efficiency of providing market demand feedback for operators; from the perspective of consumers' demand, these two markets differ in terms of the commodity range available to consumers, shopping convenience for consumers, and the efficiency to compare and match commodities for consumers; from the perspective of supply substitutability, these two markets differ in profit models, and it is more difficult to transform offline retail services into online platform services. Therefore, in terms of demand and supply substitutability analysis, there is no close substitution relationship between these two services, and thus they do not belong to the same relevant product market. It is worthwhile to note that differing online markets from offline markets is not an uncommon practice, as there are a number of SAMR's precedents that distinguish online markets with physical markets regarding merger control reviews¹.

2. There is no need to segment the online retail platform service market according to models of B2C and C2C

According to the penalty decision, the investigated undertaking proposed that the

relevant product market in this case should be B2C (i.e., corporate sellers to individual buyers) online retail platform service markets, on the grounds that it deviates from the C2C (i.e., individual sellers to individual buyers) online retail platform services on both business positioning and business models, so they are not reasonable substitutes for each other. SAMR believed that *"the services provided by online retail platforms to in-platform operators under both types of product sales methods are online operation premises, deal making, and information release, etc., and both can satisfy consumers' online shopping needs."* Therefore, there is no essential difference between the platform services provided by these two types, and the difficulty and cost of switching is relatively low. In this regard, we understand it may be related to the combined use of B2C and C2C modes in the business practices of the major online platforms in China. In the case of such combined use, the platform presents the unity of resources and platforms in the aspects of both information searching and subsequent result jumping, resulting in the unnecessary of such segmentation, at least in this case. However, we cannot rule out the possibility that SAMR may consider such market segments in other cases.²

3. There is no need to segment the online retail

¹ For example, in the case of *Acquisition of equity of LG CNS Co., Ltd., by Crystal Korea Co., Ltd.* the online advertising market was defined as a relevant product market, while in the case of *Establishment of a joint venture by and between JCDcaux Advertising (Shanghai) Co., Ltd. and Guangzhou Metro Group Co., Ltd.*, the China (outdoor) advertising market was defined as a relevant market.

² We notice there are cases in merger filing precedents where the market was further segmented according to different models, such as the cross-border e-commerce B2C market (*Establishment a new joint venture by and among CP Group Overseas Co., Ltd., Shanghai Information Investment Co., Ltd., ITOCHU Corporation, China Mobile Communications Co., Ltd. and CITIC Holdings Co., Ltd. and the acquisition of equity of Shanghai Cross-border International Trade Co.,*

Ltd. by the joint venture), B2C e-commerce shopping platform (*Acquisition the equity of Tiantian Express Co., Ltd by Jiangsu Suning Logistics Co., Ltd.*), B2B hotel accommodation intermediate supply service market (*Acquisition of the equity of the parent company of tourism holding company by Xinwen Capital Management Fifth General Partnership and Canadian Pension Plan Investment Commission*), cross-border e-commerce B2C export market (*Acquisition of the equity of Shenzhen Yibai Network Technology Co., Ltd. by Hunan Huakai Cultural and Creative Co., Ltd.*), B2C online retail market (*Acquisition of the equity of Chongqing Shangshe (Group) Co., Ltd. by Wumart Technology Group Co., Ltd. and BBK Investment Group Co., Ltd.*).

platform service markets according to different categories of commodities

SAMR further stated that there is no need to segment the online retail platform service markets according to the different categories of commodities, such as clothing, electronics, digital, household appliances, food and cosmetics, as *“for in-platform operators and consumers, the content of online retail platform services provided for different types of commodities do not substantially differ”*. In this regard, we understand that it may be related to the broad nature of the major platform undertakings - especially the investigated undertaking - resulting in the lack of practical value of such segmentation at least in this case. In other cases, particularly involving specific types of commodities other than daily necessities (i.e. cars, real estate, etc.), we understand that SAMR may still examine the online retail platforms of these special categories of commodities separately.³

4. Other highlights of the relevant market definition

There are other highlights embedded in the market definition part of this case. For example, SAMR fully considered the development of the emerging online retail models such as live streaming, short videos, and graphics, etc.; factors such as the actual regions where most users choose products, consumption habits, regulatory restrictions, and the degree of competition constraints were comprehensively evaluated and taken into account in the process of defining the relevant geographical market, which is in accordance with the provisions of the

Platform Guidelines.

II. Market Dominance Evaluation

The evaluation of market dominance in this case fully reflected the principles of the *Platform Guidelines*. Unique characteristics of the platform economy were considered such as flow control and computing and data services. Some major points regarding the market dominance evaluation part are as follows:

1. Diversified and continuous evaluation on market share

The *Platform Guidelines* state that *“in order to decide the market share of platform economy operators, agencies can consider the proportion of the transaction value, number of transactions, sales, the number of active users, clicks, the duration of usage, or other indicators in the relevant market, as well as the duration of the market share”*. In this case, the service revenue of the investigated undertaking's online retail platform was the main indicator when evaluating its market share, and the time span was 2015-2019. SAMR also considered the transaction value of platform commodities (this refers to the transaction amount of commodities on the online retail platform, which *“comprehensively reflects the operation status of all undertakings and the condition of consumption of consumers on such platform”*, as SAMR stated), and the time span was also 2015-2019. Given the rationality and intuitiveness of the above two factors when evaluating the market power of online retail platforms, we understand there is no need to further evaluate other factors such as the number of active users and clicks, which are possibly

³ In the case of *Acquisition of the equity of Beijing Baowo Automobile Co., Ltd., by UCAR Co., Ltd.*, passenger car and

new car e-commerce retail distribution market was defined as a separate relevant market.

more related to the market power of video or live streaming platforms.

2. Economic Analysis of Market Competition

In terms of evaluating competition in the relevant market, SAMR employed the traditional HHI index (Herfindahl-Hirschmann index) as well as the CR4 index (Concentration Ratio index), both of which show that the China online retail platform services market is highly concentrated with a limited number of competitors.

The HHI index has been commonly used to reflect the competition situation in the history of Chinese Anti-Monopoly Law (“**AML**”) enforcement. SAMR, however, additionally employed the CR_n index (the total market share of the top operators in the industry, for example, the CR4 index here refers to the combined market share of the top four operators in the China online retail platform market) in addition to the HHI index in this case. Although the PRC Ministry of Commerce listed the CR_n index as early as 2011 as an official index to assess market competition in the “*Interim Regulations on Evaluating the Impact of Concentration of Operators*”, its application in AML enforcement practice in recent years is far less frequent than that of the HHI index.⁴ We understand that this may be due to the inability of the CR_n index to reflect the total number of undertakings operating and competing in the market. The application of the CR_n index in this case reflects not only SAMR’s prudence and attention to the economic analysis of this case, but also reflects the fact that the platform economy market is characterized by a network

externalities effect, where the first-entry advantage of an enterprise is of great significance, leading to the limited number of competitors in the industry.

3. Other highlights of market dominance evaluation

Other factors attracting attention in the antitrust enforcement against internet big techs have also been given comprehensive consideration by SAMR in this case, including without limitation to areas such as data, algorithms, cloud services, artificial intelligence and supporting facilities (logistics, payment), etc. The above-mentioned factors are reflected in the financial and technical advantages in the relevant markets and significant advantages in related markets owned by the investigated undertakings, as well as the market entry barriers of the relevant markets. It is also worthwhile to note that the logistics, payment, cloud computing and other markets were identified as related markets in this case, rather than adjacent or vertical markets. It remains controversial whether the related markets here are vertical or adjacent markets in the context of a platform economy, and whether main platform undertakings who “ecologically develop” their business in multiple related markets will be recognized as abusive by leverage effect.

III. “Either or” conduct (exclusive dealing)

According to the penalty decision, SAMR regarded the “either or” conduct of the investigated undertaking constituted exclusive dealing prohibited by AML. To be more specific, the said conduct of the investigated undertaking

⁴ In 2019, Shanghai Administration for Market Regulation adopted the CR3 index in the case of *Eastman Company Abusing its Dominance*; As for merger control, the PRC Ministry of Commerce’s approval of *Establishment of a*

new joint venture by and among Corun, Toyota China, PEVE, The Announcement of New Zhongyuan and Toyota Tsusho employed the CR4 index to evaluate the competition situation of the global automotive nickel-hydrogen battery market.

included:

- (1) prohibiting in-platform operators starting businesses on other rival platforms;
- (2) prohibiting in-platform operators from participating in promotional activities on other rival platforms; and
- (3) adopting various reward and punitive measures to ensure the implementation of the "either-or" requirements.

Some highlights will be exemplified as follows.

1. Well-implemented verbal restrictions equal to "either or" conduct

According to Article 15 of the *Platform Guidelines*, exclusive dealing "*may be implemented through written agreements, telephone or verbal negotiations with the trading counterparty*", which is fully reflected in the conduct assessment of this case. SAMR found that the investigated undertaking implemented the above-mentioned restrictions not only through direct agreements, but through verbal requirements during negotiation as well, and most of them had been implemented relatively well as proven by evidence. SAMR concluded that such conduct was equal to exclusive dealing and set a higher anti-monopoly compliance standard for internet platform undertakings.

2. Platform-characterized conduct is regarded as new forms of "either or"

According to Article 15 of the *Platform Guidelines*, platform undertakings that impose restrictions through blocking stores, lowering the ranking in search results and traffic restrictions can be identified as exclusive dealing. In this case,

SAMR's assessment included the investigated undertaking disqualifying the in-platform operators concerned from participating in promotional activities, lowering their ranking in search results, and depriving other significant rights and interests of them, fully reflecting the above-mentioned provision of the *Platform Guidelines*.

Among them, lowering the ranking in search results is an emerging form of exclusive dealing in the platform economy. Given the indispensability of search results and rankings towards converting search volume into sales volume, platform undertakings lowering the ranking in search results or even delisting the operators' products in the search results will essentially affect the sales of the platform operators' products.

3. Justification for Exclusive Dealing

According to Article 15 of the *Platform Guidelines*, "*to protect the input of specific resources for transactions*" constitutes a justification for exclusive dealing. However, in this case, SAMR found that the investigated undertaking's investment in this case did not serve as a justification, as the funds and flow resources invested by the investigated undertaking during daily operations and promotion were necessary for the operation of the platform itself rather than for the in-platform operators, and that the incentive measures taken by the investigated undertaking could be rewarded in many ways. The implementation of "either or", however, is not the only option available.

From the perspective of competition law principles, exclusive dealing sometimes can have a pro-competitive effect regarding promoting

inter-brand competition, preventing "free-riding", and protecting investments. Other jurisdictions across the world have developed detailed regulations on this type of conduct and its justifications. For example, the EU believes that justification must be established on the basis that the implemented restrictive measures are indispensable for achieving efficiency, i.e., whether there is a way to achieve such efficiency with less impact on competition. In this case, however, we did not find more detailed analysis on the "indispensability" standard, and thus we look forward to more legislation and enforcement guidance in the future to effectively balance the platform undertakings operation, new industrial development and healthy competition.

IV. Fine Amount and Other Administrative Penalty Measures

In addition to behavioral qualitative analysis and anti-competitive effect analysis, we consider that the administrative penalties and rectification procedures in this case would be a very good reference for future cases.

1. The Base of Fine

Article 47 of the AML stipulates that undertakings abusing their market dominance shall be fined between 1% and 10% of the turnover of the previous year. According to the penalty decision, the base of fine in this case is the China turnover amount in 2019 (455.712 billion), and the fine ratio is 4%.

The China retail business revenue of the investigated undertaking in the 2019 fiscal year was CNY 58.441 bn, as stated in its public financial report, which is much lower than the base of fine in this case. Therefore, we understand that the penalty base in this case is not the turnover of the concerned business, but more likely to be a full caliber turnover.⁵ This is consistent with SAMR's current attitude towards base of fine, which also means that the cost of antitrust violations for undertakings will become increasingly higher in the future.

2. An administrative guidance issued simultaneously

We notice that SAMR has also issued an administrative guidance along with the penalty decision, requiring the investigated undertaking to fully regulate its competitive conduct, strictly implement the responsibility of platform undertakings, improve the internal compliance control system, actively protect the legitimate rights and interests of in-platform operators and consumers, formulate rectification measures, as well as submit an annual self-assessment report on compliance to SAMR for the next three years. The specific requirements (including the application of the FRAND principle) of the administrative guidance are similar to the behavioral remedies enforced in the merger control reviews of China. It covers more extensive behavior and more detailed instructions, providing further references for other platform undertakings on self-examination and rectification procedures.

⁵ The turnover of the investigated undertaking in the fiscal year 2019 was CNY 376.844 bn, as stated in its public financial report, which deviates from the base of fine in this case (CNY 455.712 bn) significantly. Therefore, we speculate that the data used here might be the turnover in the natural year 2019 (CNY 476.317 bn), turning into CNY 444.958 bn after deducting

overseas business income. Although there still exists deviation, we speculate that this may be because the data used here also includes the investigated undertaking's global and cross-border retail business revenue generated in China. So, we conclude that the base of fine is still closer to the full-caliber turnover.

V. Summary

This case has far-reaching implications on the antitrust enforcement and compliance construction of Internet platforms, as well as ongoing or subsequent anti-monopoly civil lawsuits. The rules and analysis of the penalty decision in terms of relevant market definition, market dominance evaluation, abusive behavior assessment, and administrative penalties provide

meaningful guidelines on compliance for Internet platform undertakings. Considering the increasingly sophisticated and enhanced enforcement, we suggest that Internet platform undertakings should attach more significance to internal anti-monopoly compliance review and professional training, strengthen compliance awareness and further reduce antitrust operational risks.

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