NDRC continues resale price maintenance crack-down

Kluwer Competition Law Blog
December 20, 2016

Adrian Emch (Hogan Lovells, China)

Please refer tot his post as: Adrian Emch, 'NDRC continues resale price maintenance crack-down', Kluwer Competition Law Blog, December 20 2016, http://competitionlawblog.kluwercompetitionlaw.com/2016/12/20/ndrc-continues-resale-price-maintenance-crack-down/

On 5 December 2016, the National Development and Reform Commission ("**NDRC**") – one of the three Chinese antitrust authorities – issued its decision fining the local unit of Medtronic, a U.S.-listed medical device maker, for resale price maintenance ("**RPM**").

Case summary

Medtronic was found to maintain a distribution system for cardiovascular, rehabilitation therapy and diabetes medical devices in China, consisting of various tiers of distributors. NDRC held that Medtronic had engaged in RPM practices since 2014, including:

• **Setting resale prices.** For an unspecified type of product, Medtronic was found to set the resale prices for distributors at various tiers of the distribution system. For another unspecified type of product, Medtronic was only found to set the price at which tier 1 distributors could resell the products to tier 2 distributors.

• **Fixing profit margins.** Medtronic was found to fix the profit margins of "platform" distributors reselling its products to tier 2 distributors. Different from tier 1 distributors, the platform distributors were not allowed to resell the products to end customers.

• **Imposing minimum bidding prices.** Medtronic was found to have imposed "guiding" bidding prices in the distribution agreements, and distributors were required to seek Medtronic's approval for any deviation from those prices.

• **Setting minimum resale prices to hospitals.** Medtronic was found to impose minimum prices for the resale of products to hospitals.

Which benchmark for RPM?

There have been a number of RPM cases decided by NDRC, its local offices and the Chinese courts in recent years. However, there seems to be a divergence between the authority and the courts in applying Article 14 of the Anti-Monopoly Law ("**AML**"), which regulates RPM conduct.

On one side, the courts seem to have developed an effects-based approach to RPM through a string of cases – ranging from **Rainbow v. Johnson & Johnson** in 2013 through to the **Gree** case decided by the Guangzhou Intellectual Property Court in August 2016. In other words, beyond the finding of the resale price obligation as such, plaintiffs needed to prove that the obligation actually restricted competition in the marketplace. In several instances, the courts found that there was not sufficient proof of such restriction and dismissed the actions.

In contrast, NDRC's position on RPM has been much more restrictive, resembling a "per se" approach. In some of the past cases, NDRC seemed to consider the finding of RPM conduct to be sufficient to establish a violation of Article 14 of the AML, without the need to look at actual effects in the market. The **Haier** case, from August 2016, is a recent example of this NDRC position. In some other past cases, NDRC did mention some sort of effects of the RPM conduct found, but its analysis remained very high-level.

Now the *Medtronic* decision is somewhat more elaborate on the anti-competitive effects of the RPM conduct, when compared to NDRC's past cases. The decision has a sub-heading referring to negative effects on competition and consumer harm, and mentions Medtronic's leading market position and high barriers to entry into the relevant markets.

One interpretation of this somewhat more detailed discussion of NDRC's underlying reasoning would be that the authority's position is converging with that of the courts – in particular, RPM would only be problematic where the company in question has a significant degree of market power and there is not sufficient competition in the marketplace. However, at this point in time, it is far from certain whether this interpretation represents the true intention of NDRC.

Expanding the scope of the law?

As noted, NDRC's decision in the *Medtronic* case found the territorial and customer restrictions and the exclusive purchasing requirement to have increased the anti-competitive effects of the RPM conduct. As a result, Medtronic committed to terminating the territorial and customer restrictions (presumably for all products), and the exclusive purchasing requirement for those products where it has market power. This is a very notable development.

As the law currently stands, it would seem that territorial and customer restrictions and exclusive purchasing requirements are problematic only if the company in question has a dominant position. For non-dominant companies, Article 14 of the AML only explicitly prohibits RPM. That said, the provision also contains a catch-all clause allowing NDRC and the State Administration for Industry and Commerce ("**SAIC**") – another antitrust authority – to find other, not specified vertical agreements to be unlawful.

To the best of our knowledge, there are no public cases where NDRC and SAIC have used the catch-all clause to tackle territorial/customer restrictions and exclusive purchasing requirements imposed by non-dominant companies.

Now, the *Medtronic* decision may signal a shift in the law. Even though NDRC did not find these additional restrictions to be illegal themselves, it found them to aggravate the competition problem and accepted Medtronic's commitments in that regard. Taking into account that NDRC published draft guidelines for the automotive industry which also target certain types of territorial restrictions and exclusive purchasing requirements, a new trend to expand the scope of the AML's application may arguably become visible.

Conclusions

Most of all, the *Medtronic* decision is a strong reminder for companies that they should not engage in RPM conduct – at least until the benchmarks on what distinguishes anti-competitive from pro-competitive resale practices have been clarified.

Beyond this simple lesson, the decision may become more important if it were to

indicate a shift in the law – leading to an alignment between NDRC and the courts as to the necessity of an effects analysis for RPM, and/or expanding the obligations on non-dominant companies not to impose territorial/customer restrictions and exclusive purchasing requirements.