



For centuries, China¹ stood as a leading civilisation, outpacing the rest of the world in arts and sciences, but in the 19th and early 20th centuries, the country was beset by civil unrest, major famines, military defeats, and foreign occupation.

After World War II, the Communists, under Mao Zedong’s leadership, established an autocratic socialist system that, while ensuring China’s sovereignty, imposed strict controls over everyday life and cost the lives of tens of millions of people. After 1978, his successor, Deng Xiaoping, and other leaders focused on market-oriented economic development and by 2000 the output had quadrupled. For much of the population, living standards have improved dramatically and the room for personal choice has expanded, yet political controls remain tight.

Economy

In late 1978, China started moving from a sluggish, inefficient, Soviet-style centrally planned economy to a more market-oriented system. Though the market system still has to operate within a political framework of strict Communist control, the economic participation of non-state organisations and individual citizens has been steadily increasing.

The authorities switched to a system of household and village responsibility in agriculture in place of the old collectivisation, increased the authority of local officials and plant managers in industry, permitted a wide variety of small-scale enterprises (SSEs) in services and light manufacturing, and opened the economy to increased foreign trade and investment.

The result has been a quadrupling of GDP since 1978. Measured on a purchasing power parity (PPP) basis, China in 2004 stood as the second-largest economy in the world after the US, although in per capita terms the country is

PROFILE	
Population:	1.3 billion***
GDP (Current US\$):	1.4 trillion***
Per Capita Income: (Current US\$)	1,100 (Atlas method)*** 4,990 (at PPP)
Surface Area:	9.6 mn sq km***
Life Expectancy:	70.8 years***
Literacy (%):	91 (of ages 15 and above)
HDI Rank:	94
Sources: - World Development Indicators Database, World Bank, 2005 - Human Development Report Statistics, UNDP, 2004 (**) For the year 2002 (***) For the year 2003	

still lagging far behind as compared to many other economies. Agriculture and industry have posted major gains, especially in the coastal areas near Hong Kong and opposite Taiwan and in Shanghai, where foreign investment has helped spur output of both domestic and export goods.

China, however, has experienced the worst results of socialism (bureaucracy and lassitude) and of capitalism (growing income disparities and rising unemployment), as a result of its hybrid political economy. The country, thus, has periodically backtracked, retightening central controls at intervals. In particular, the Government of China has struggled to:

- sustain adequate jobs growth for tens of millions of workers laid off from SoEs, migrants, and new entrants to the work force;
- reduce corruption and other economic crimes; and
- keep afloat the large SoEs, many of which had been shielded from competition by subsidies and had been losing the ability to pay full wages and pensions.

* Original paper submitted in May 2005. Revised in August 2005 & January 2006

‡ Comments received from Mao Xiaofei, Research Centre for International Law, Chinese Academy of Social Sciences

1 CIA World Fact Book

Accession to the WTO helped strengthen China's ability to maintain strong growth rates, but at the same time, put additional pressure on the hybrid system of strong political controls and growing market influences.

Competition Evolution and Environment

In 1978, China adopted an open-door reform policy; since then it has been implementing the policy in a progressive manner, which has resulted in a long transitional period in the economic regime. This transition process has been speeded up during and after China's accession to the WTO.

The Chinese economy is now in its final stage of transforming into a full-fledged market economy. The development of competition law in China has also had to reflect this complex and profound process; it has played and will continue to play an important and indispensable role in this evolution.

Many of the structural reforms introduced in China's economy have improved the operating environment for all enterprises, both state-owned and private. These encourage not only SoEs to perform better, but also provide a framework in which newly-privatised firms are also likely to do well. The major structural reforms, which have been undertaken in China, included the following:

- Entry barriers to market have fallen;
- Extensive trade liberalisation has allowed competition from imports;
- Extensive price liberalisation has taken place;
- Foreign investment has been promoted;
- Hard budget constraints are increasingly common;
- A large number of wealthy domestic private buyers are now in the market for state assets;
- The Government is relatively coherent both in terms of policy formulation and implementation;
- A basic framework needed to facilitate secondary sales has been developed;
- There are firm-level incentives for privatisation;
- Private entrepreneurs have gained sufficient influence to skew sales methods to their advantage; and
- Continued resistance to market-based asset valuation methods for state assets.

As reforms progressed, there has been a gradual radicalisation of policy, moving in the 1990s to a creeping recognition of the role of private capital and the utility of privatisation.

Competition Legislations

The rules relating to competition were first introduced by the State Council in a regulation entitled, 'An Interim Regulation on Promotion and Protection of Socialist Competition' (PPSC), which was promulgated in October 1980, two years after China began its economic reform. This was a breakthrough in the economic reforms process, in terms of competition policy and law. In addition, the

PPSC paved the way for further breakthroughs in Chinese competition law development in the following areas:

- A business monopoly in any industrial sector except for those under the state licensing system is strictly prohibited;
- No government agency is allowed to restrict inter or intra-industrial/regional commerce, or to curtail inter-provincial trade;
- All competition should be performed in accordance with the law and/or policy of the state; and
- Counterfeiting and commercial bribery should be condemned.

However, these rules were not effectively enforced, not only because they failed to deal with the problem of ownership (particularly state ownership), which was actually the core problem of competition in China, but also because the administrative arms at all levels held firmly that SoEs should be protected from the enforcement pressure of pro-competition policy and laws.

The PPSC was promulgated by the State Council and primarily targeted government agencies at different levels. Taking into account the administratively-biased framework of legislation in China, it was not until the enactment of the Law on Administrative Litigation in early 1989 that the PPSC became enforceable.

Bearing this in mind, the PPSC is undoubtedly a good starting point for a pro-competition legal system, in at least two ways: its anti-monopoly rules for specific sectors of industry, and its condemnation of administrative segmentation of the domestic markets.

In the following years, these two core policies of the PPSC for the promotion of competition were further developed and enhanced by statutory legislation in regard to pricing and competition, including the Regulation on Pricing (RP), adopted by the State Council in 1987 [which was substituted by the Law of Pricing, promulgated by the National People's Congress in 1997 (LP)], and particularly the Law on Anti-unfair Competition (LAUC) adopted at the 3rd Session of the 8th National People's Congress in 1993.

With respect to demonopolisation, there are many industrial sectors that have been demonopolised over the past decades. The most remarkable demonopolisation moves occurred in the telecommunication sector (1994-2002) and the airline industry (1987-2002). In each sector, a large SoE was split into several companies in local markets, through government coordination.

However, this pro-competition restructuring was not as successful as expected. The new firms that emerged after the restructuring remained owned and controlled by the state, so competition between them, if any, was not that of

an open market. These areas call for further reform and better regulation.

To prevent abuse of administrative power in regulating inter or intra-regional commerce, the LAUC stipulates that no governmental agency or any of its departments shall abuse its administrative authority to demand others to buy what it designates, or to prohibit lawful business activities. This stipulation is rooted in the PPSC, and is further developed by the State Council in 2001 in its Regulation on Prohibition of Regional Trade Barriers (RPRTB), which prohibits a variety of administrative rules, from taxation to technical standards, from being manipulated as regional/sectoral trade protectionist measures.

The PPSC's pro-competition policy was also developed and enhanced in many other areas. From a substantive law perspective, some new legislation in 2004 is noteworthy, i.e. the regulations on pricing behaviour, abuse of market power by regulated/monopolistic/oligopolistic enterprises, and commercial bidding.

In 2003-2004, the Chinese economy underwent some remarkable developments, both in the domestic and foreign trade sectors, which gave rise to the need for further legislation of a new comprehensive competition law.

In May 1994, an Anti-monopoly Law drafting group, which consisted of members of the legal departments of the State Economy and Trade Commission (SETC) and the State Administration of Industry and Commission (SAIC), was established to discuss the possibility of an Anti-monopoly Law. During the legislative process, the drafting group listened to opinions and suggestions from Chinese experts on a proposed new Anti-monopoly Law.

In substantive legislation, a remarkable step forward is the draft law of Anti-monopoly (the DLAM) that has been finalised in the beginning of 2004 by the Ministry of Foreign Trade and Economic Cooperation (MOFCOM) and put forward to the State Council for approval, before it is submitted to the National People's Congress for formal legislative review in the second half of 2005.

For the first time in Chinese legislation, the DLAM explicitly prohibits agreements for concerted refusal to deal, setting restrictions upon buying or developing new technology and/or equipment, and imposing market segmentation, in addition to those stipulated in existing rules or regulations. Equally importantly, the DLAM also provides for exemptions to prohibited agreements on the grounds of enhancing quality and/or efficiency, cost-savings, technology development, etc.

To prevent abuse of market dominant position, the DLAM introduces the concept of 'market dominant position' for the first time in Chinese competition law history, and spelt out in detail various criteria for determining a dominant

position. Rules against abuse of administrative power have also been elaborated in several aspects, in comparison with the Law on Anti-Unfair Competition (LAUC) 1993.

Merger control is another major provision in the draft Antimonopoly Law, since it would be the first time the national legislature has ruled on this area, although MOFCOM addressed the issue in 2003 in Provisional Rules on Mergers & Acquisitions of Domestic Enterprises by Foreign Investors (MADEFI). Admittedly, MADEFI is a set of ministerial rules based on the foreign investment laws rather than any specific competition principles, hence its binding force on merger control may be relatively weak.

Furthermore, MADEFI provides MOFCOM with very limited means to investigate merger deals and to sanction them, if appropriate. This makes the enforcement of MADEFI less effective than other stipulations on foreign investment. The well-known clauses of MADEFI seem to be little more than a standard set of clauses on the scrutiny and approval of foreign investment. These shortcomings precipitate the need for more rigorous and effectively enforceable rules for merger control.

The scope of applicable industries also features in the DLAM. Industries that may be exempted from monopoly scrutiny are limited in number. Traditionally exempted industries or some 'naturally monopolistic industries, such as power generation, telecommunications, railroad transportation and airlines, will not necessarily be exempted, as it may be that deregulation and opening-up to foreign investment will result in much more competition in these sectors. This, in turn, would make the abuse of a dominant position less attractive if not unworkable. At the same time, any abuse of market power would still be subject to the scrutiny of the future competition authority for the sake of economic efficiency and development.

Also from the angle of economic efficiency and public interest, a merger that might generate a monopolistic position could be considered valid and exempted or approved if it would improve competition in a market, or if it would be beneficial to the economy as a whole, or if it would be in the public interest.

With regard to merger approval, the DLAM proposes in detail various stipulations for documentation, for time periods for scrutiny, for notice to be given to the applicant and for the extension of a deadline to make a decision, among others. In addition, the DLAM specifies investigative procedure with greater clarity than the LAUC.

The drafting of the DLAM took more than 10 years. After the former State Economy and Trade Commission (SETC) took control of the drafting process in 1994, little progress was made. However, as a result of administrative restructuring in 2003, the part of SETC with market

regulation functions was merged with the former MOFTEC and, ultimately, this long, drawn-out drafting process does not seem to have been retarded by the technical difficulty and bureaucracy of the drafting process.

In 2004, one relevant development in the procedural aspect of competition law is the establishment of the Anti-monopoly Office in MOFCOM. This further strengthens MOFCOM's position as a regulatory agency for enforcing competition law.

Anticompetitive Business Practices

In 2004, SAIC undertook a nationwide investigation into regional trade barriers. The main targets of the investigation were agricultural inputs, such as chemical fertilisers and pesticides, and alcoholic drinks, tobacco products, beer, and so on. Some anticompetitive practices were identified and removed after the investigation. For example, one municipal authority ruled that no pork produced in an urban area could be sold to a rural area, or vice versa.

Another municipal authority required all schools in the city to use water supplied by a designated supplier. Many local authorities were found to use the well-known distribution/retail measure of placing a higher tipping charge on foreign beer, or beer produced in other cities.

All these measures were abolished by the SAIC and/or its branch agency.

In summary, the development of competition law in China in 2004, following all the developments of the past two decades, has constituted a new start in China's competition policy and law. This includes a more consistent statutory law of competition – including anti-unfair competition law on one hand, and anti-monopoly law on the other – to tackle the market failures that may arise after the substantial restructuring of ownership and industrial organisation, and the deregulation of the major industries.

Sectoral Regulation

Electricity Regulation

China's State Electricity Regulatory Commission (SERC) is a law enforcement agency directly under the State Council of China. It is responsible for supervising and regulating market competition in the electricity industry.

It also issues licenses to operators in the industry, monitor their operations and hold them accountable for violations of pricing and competition rules. The SERC was established by the Chinese Government in December 2002. It is the first governmental regulatory agency in the primary industry sector.

Box 8.1: Conflict between Different Agencies

In 1996, Xindu Railway Station in Chengdu, Sichuan province, reached an agreement with Xindu Insurance Company, under which the Xindu Railway Station provided an insurance agent service for the insurance company for all the commodities which arrived by train and should be taken out of the railway station by lorry.

Customers were asked to buy the insurance for the trucking provided by the insurance company as they picked up their goods from the railway station. However, most of the customers were not willing to buy this insurance because the trucking distance was less than 1,000 Meters.

Yet, they paid for this since Xindu Railway Station is the only authorised provider for the railway transport in the region. According to the arrangement, the railway station took 10 percent of the insurance fee as commission for the agent service. From February 1996 to March 1998, Xindu Insurance Company earned 1,234,699 RMB from this insurance service, of which 10 percent or 123,470 RMB was earned by the Railway Station.

The State Administration of Industry and Commerce (SAIC) in the city of Chengdu considered the agreement between Xindu Railway Station and Xindu

Insurance Company as anticompetitive. Furthermore, the railway station misused its exclusive right of railway conveyance on the local market to carry out enforced insurance, which violated Article 6 and Article 23 of the Chinese Anti-Unfair Competition Law (LAUC).

However, Xindu Insurance Company contended that the dispute was not of a competition concern so that it should not be decided by the Chengdu SAIC. It was in their point of view that a matter of sector regulation should be judged by the Supervision and Administration Department for Banking of the Chinese State Council, pursuant to the Chinese Bank Law and the Notice of Strengthening the Supervision and Administration on Banking issued by the State Council in 1994.

Xindu Insurance Company brought fore an administrative action against the decision of the SAIC to the Middle-level Court in Chengdu. The court acknowledged the authority of the SAIC in regulating competition issues, which covers special economic sectors as well. The insurance company then appealed to the High Court of Sichuan Province but failed. The questions as how to solve the conflicts between the competition regulation and sectoral administration and which state agency shall be in a position to deal with cases as such remain unclear.

Telecom Regulation

Until mid-1994, the Ministry of Posts and Telecommunications (MPT) was the sole in-charge of China's telecom industry. Not only was it the regulator, it was also the monopoly operator, providing virtually all telecom services.

The service function was provided at the local level by the MPT's various Posts and Telecommunications Administrations (PTAs), the operators in the country's 31 provinces, autonomous regions and major cities. They made up the MPT's operating arm and, collectively, were known as China Telecom.

In 1998, the Government established a new regulatory body, the Ministry of Information Industry (MII), and made it directly responsible to the State Council. The MII assumed most of the responsibilities of the MPT (excluding postal services), and took over the administrative functions of the former State Radio Regulatory Commission.

Subsequently, in January 1999, the MII's service function under China Telecom was siphoned off and assigned to an independent organisation (also called China Telecom), while the MII became purely a regulator.

The State Administration of Radio, Film and Television (SARFT), which is under the direct supervision of the State Council, is the regulator for the broadcasting sector, including cable TV services.

With the convergence of broadcasting and telecom, especially with telecom and cable TV being available over a single network, regulatory conflicts between the MII and SARFT have been reported. The absence of a Telecommunications Law, a piece of legislation that has been under consideration for some 20 years, does nothing to help the situation.

As a result, the regulatory situation in China is still by no means straightforward. Even though a set of Telecommunications Regulations has been published, they are incomplete and open to various interpretations. The long-awaited Telecommunications Law is in final stages.

Nevertheless, from a regulatory standpoint there is a sense that the country is moving forward. The MII, having been relieved of its operational functions, can focus on industry regulation. China Telecom has been broken up and competition has been introduced in all major segments of the industry. China has entered the WTO and has accepted a number of that body's regulatory commitments.

Yet a number of problems remain. One is the potential for different interpretations of the regulations and, where disputes arise, the lack of sufficient backup to have them resolved and then to have the judgements enforced. The second is in ensuring that the regulations are adhered to in

a country as large and diverse as China where each provincial jurisdiction tries to operate autonomously. These problems have always existed, and reducing or eliminating them cannot happen overnight.

Consumer Protection

The Law of the People's Republic of China on Protection of the Rights and Interests of the Consumers was adopted by the 4th Session of the Standing Committee of the Eighth National People's Congress on October 31, 1993, and became effective on January 01, 1994.

This Law is formulated in order to protect the lawful rights and interests of the consumers, to maintain the socio-economic order, and to promote sound development of the socialist market economy.

Where the consumers, for their consumption needs, purchase and utilise commodities or accept services, their rights and interests are protected by this Law; and in the absence of appropriate provisions in this Law, are protected by other relevant laws and regulations.

A national consumer association and other consumer organisations have been established according to law to carry out social supervision over commodities and services, and to protect the lawful rights and interests of the consumers.

The China Consumer Association exercises the following duties and functions:

- to provide consumers with information on consumer issues and advice;
- to assist relevant administrative departments in supervising and inspecting consumer goods and services;
- to report to relevant administrative departments, inquire into and put forward suggestions on issues concerning the lawful rights and interests of the consumers;
- to take cognisance of consumer complaints, investigate and mediate such complaints;
- where the complaints involve quality of goods and services, the consumer association may submit to the appraising departments for appraisal, and the appraising departments shall inform them on their findings;
- to support the consumer whose rights and interests are infringed upon in filing suits against any act which infringes the lawful rights and interests of the consumers; and
- to expose and criticise through the mass media such acts which infringe upon the lawful rights and interests of the consumers.

People's governments at all levels support the consumer movement in exercising their duties and functions.

Concluding Observations and Future Scenario

Developing a nationwide competition enforcement regime will be difficult, particularly given the shortage of qualified

personnel with antitrust experience. Reliable market data may also be scarce.

Though some Chinese firms have sophisticated accounting systems, bookkeeping in other firms remains manual and rudimentary. Statistics from China's official and quasi-official sources are infamously inaccurate, and antitrust officials may avoid contradicting the official pronouncements of other ministries or the State Council. China's fragmentation into regional markets, rampant graft and tax evasion, and poor cooperation at local levels may compound these problems.

Many common assumptions about market conduct – the stability of property rights, the commercial value of intellectual property, judicial enforcement of contracts, the predictability and transparency of government action – do not apply uniformly in China. It might be prudent to concentrate initially on cartels and administrative monopolies before phasing in more complicated enforcement efforts. Unfortunately, China's top antitrust priorities – policing abuses by dominant firms and international mergers – both entail intricate economic analysis.

The bite of Chinese antitrust regime may vary with the political circumstances. Other government entities will resist enforcement of competition rules against favoured enterprises. China's antitrust authorities will have to contend with local protectionism and contrary policy goals through China's fluid political process. The long-term impact of China's Anti-monopoly Law will thus depend on the credibility, competence, and stature of its antitrust authorities.

Currently, China has two major categories of anticompetitive practices, one is business anticompetitive conduct and the other is administrative anticompetitive conduct. They result from different reasons and have different significance to the Chinese economy at present and in the future. To deal with the business conducts, the major measure should be to complete the legal framework of competition and to enhance the enforcement system.

But to deal with the administrative conduct, the right way is to deepen and further promote the economic and administrative reform, including continuing to separate the Government's regulatory and ownership functions, and to democratise the ownership and to establish good governance structure in those monopolised sectors.

✦ The China's State council (Cabinet) has approved the Anti-monopoly Law. The next step will be the submission of the approved draft to the Standing Committee of the National People's Congress for formal enactment. Whilst it is likely that further amendments will be suggested by the Committee, it appears that the law will be enacted very soon.

(Source: South China Morning Post, June 8 2006)

Suggested Readings

1. *New developments in competition law in China*, Li Li Zhong Lun Law Firm, Global Competition Review
2. *China telecom industry: Reform, Development and Regulation*; Su Jinsheng
3. Briefing Note, *Will privatisation in China work?*, Stephen Green
4. *Anticompetitive Conducts: China Experience*, Junkuo Zhang, Development Research Centre of the State Council

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