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RESPONSES TO CHINA'S MISUSE OF ITS ANTI-MONOPOLY LAW

I. BACKGROUND

The Government of China ("GOC") in 2008 began implementing its Anti-Monopoly Law ("AML"). In the years since, the GOC has used the AML in a manner that has generally furthered GOC industrial policies and favored domestic interests. Foreign companies have, for example, been barred from acquiring leading Chinese companies for dubious reasons, and in some transactions have been burdened with conditions unrelated to the competitive effect of the acquisition at issue.[1] In one particularly egregious episode, GOC regulators invited executives from multinational companies to a seminar only to demand that the executives confess to violating the AML and threatening arbitrary fines for companies that hire lawyers to defend against such charges.[2]

In its most recent National Trade Estimate report, the Office of the United States Trade Representative ("USTR") noted with concern the GOC's increased use of the AML against foreign companies. Moreover, U.S. Trade Representative Ambassador Michael Froman recently responded to a question from a Member of Congress by saying:

> USTR is working intensively, in cooperation with other U.S. government agencies and key trading partners, via both bilateral and multilateral engagement, to combat China's use of the anti-monopoly law as a tool for pursuing industrial policies. We are pressing China hard, building on China's leaders' stated commitments to a level playing field and the rule of law. We are

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[1] *See, e.g.*, "InBev ruling sparks fears for M&A in China," *Financial Times* (November 30, 2008), available at http://www.ft.com/intl/cms/s/0/d7addf8e-beff-11dd-ae63-0000779fd18c.html#axzz37BY4gfsy; "China antitrust push draws ire of US companies and regulators," Financial Times (August 22, 2013), available at http://www.ft.com/intl/cms/s/0/82599dbe-08bc-11e3-ad07-00144feabdc0.html#axzz37BY4gfsy.

[2] *See, e.g.*, "Tough-talking China pricing regulator sought confessions from foreign firms," *Reuters* (August 21, 2013), available at http://www.reuters.com/article/2013/08/21/us-china-antitrust-idUSBRE97K05020130821.

> committed to continued intensive engagement on this important
> concern.

Such concern about the misuse of the AML is becoming so widespread that the GOC felt compelled to address the issue, publishing an article in the State-owned *China Daily* denying that the AML is used to discriminate against foreign interests.[3]

The United States should not allow the GOC to continue to misuse the AML to the detriment of U.S. interests. Congress should do its part by revising U.S. laws in order to provide better and more effective tools to discourage the use of the AML to further Chinese industrial policies or promote national champions at the expense of U.S. interests. Suggestions for how Congress could revise existing U.S. laws to better address this growing problem appear below.

II. POTENTIAL REVISIONS TO U.S. LAW

A. Section 301

1. Background

Historically, the United States government has investigated foreign government practices that harmed U.S. trade interests under Section 301 of the Trade Act of 1974, as amended ("Section 301"). Through various iterations over time, this law has provided for a number of potential responses to unfair trading practices, including increasing import tariffs on products from the offending country. Section 301 provides that USTR can investigate foreign government policies or practices and take certain actions if those practices or policies (a) deny the rights of U.S. persons under international agreements or (b) unreasonably, unjustifiably, or discriminatorily burden or restrict U.S. commerce. After opening an investigation, the law requires USTR to consult with the foreign government at issue about the problem, and also

[3] "Antitrust 'not target' foreign companies," *China Daily* (August 27, 2013), available at http://usa.chinadaily.com.cn/business/2013-08/27/content_16922370.htm.

allows USTR to pursue a remedy through dispute settlement at the World Trade Organization in Geneva. If such consultations do not resolve the issue, however, Section 301 provides USTR with discretion to:

- Suspend concessions under trade agreements;
- Impose duties or other import restrictions (which may constitute a suspension of concessions under one or more trade agreements);
- Impose fees or restrictions on services;
- Enter into agreements with the country at issue to eliminate the offending practice or to provide compensatory benefits for the United States; or
- Restrict service sector authorizations.

2. Proposed Changes

Section 301 could be strengthened in a number of ways to more directly address China's abuse of its AML and to offer a wider array of potential remedies. New potential remedies could, for example, curtail the use of U.S. government discretion in favor of Chinese entities in areas such as export licenses for controlled technologies and the availability of financing from U.S. government banks. Such potential amendments to Section 301 are reflected in underlined text below:

(a) Mandatory action

(1) If the United States Trade Representative determines … that—
(A) the rights of the United States under any trade agreement are being denied; or
(B) an act, policy, or practice of a foreign country—
(i) violates, or is inconsistent with, the provisions of, or otherwise denies benefits to the United States under, any trade agreement;~~, or~~
(ii) is unjustifiable and burdens or restricts United States commerce; <u>or</u>
<u>(iii) is intended to unfairly advantage an industry or entity located in that country at the expense of a U.S. industry or entity;</u>
the Trade Representative shall take action authorized in subsection (c) of this section … .

…

(c) Scope of authority

(1) For purposes of carrying out the provisions of subsection (a) or (b) of this section, the Trade Representative is authorized to—

(A) suspend, withdraw, or prevent the application of, benefits of trade agreement concessions to carry out a trade agreement with the foreign country referred to in such subsection;

(B) impose duties or other import restrictions on the goods of, and, notwithstanding any other provision of law, fees or restrictions on the services of, such foreign country for such time as the Trade Representative determines appropriate;

(C) direct the appropriate agencies to deny export licenses to residents or nationals of such foreign country notwithstanding any other provision of law, or suspend any regulatory programs such as validated end-user programs for residents or nationals of such country notwithstanding any other provision of law;

(D) direct the Export-Import Bank of the United States to deny financing to residents or nationals of such foreign country;

(~~C~~E) in a case in which the act, policy, or practice also fails to meet the eligibility criteria for receiving duty-free treatment under [certain preference agreements and programs], withdraw, limit, or suspend such treatment under such provisions, notwithstanding the provisions of subsection (a)(3) of this section; or

(~~D~~F) enter into binding agreements with such foreign country that commit such foreign country to—

(i) eliminate, or phase out, the act, policy, or practice that is the subject of the action to be taken under subsection (a) or (b) of this section,

(ii) eliminate any burden or restriction on United States commerce resulting from such act, policy, or practice, or

(iii) provide the United States with compensatory trade benefits that—

(I) are satisfactory to the Trade Representative, and

(II) meet the requirements of paragraph (4).

…

Amendments to other provisions in Section 301 and in other statutes may be necessary in order to effectuate the proposed revisions above.

B. The Antidumping Law

1. Background

The United States considers a handful of countries including China as "non-market economies" for antidumping purposes, which results in the use of alternative methodologies to determine whether companies located in these countries are dumping and the antidumping duties imposed. [4] Attaining "market economy" treatment in antidumping investigations is one of China's paramount trade objectives.[5] Toward this end, China has actively campaigned for recognition as a market economy in countries around the world and is promoting an interpretation of its WTO Accession Protocol that purportedly would require it to be treated as a market economy in 2016.[6]

In the United States, the Tariff Act of 1930 as amended (the "Tariff Act") defines non-market economies for antidumping purposes as:

> any foreign country that the administering authority determines does not operate on market principles of cost or pricing structures, so that sales of merchandise in such country do not reflect the fair value of the merchandise.[7]

The statute further provides for a six-part test for when a country requests to graduate to market economy treatment.[8] These factors are:

- The extent to which the currency of the foreign country is convertible into the currency of other countries;
- The extent to which wage rates in the foreign country are determined by free bargaining

[4] *See, e.g.,* Weijia Rao, "China's Market Economy Status under WTO Antidumping Law after 2016," 5 Tsinghua China Law Review 2013.

[5] *See generally* "China's market economy status key to world economy," *China Daily* (December 12, 2012).

[6] *See* "U.S. unlikely to grant China market economy status soon," *China Daily* (May 12, 2010).

[7] Section 771(18)(A) of the Tariff Act.

[8] Section 771(18)(B) of the Tariff Act.

between labor and management;

- The extent to which joint ventures or other investments by firms of other foreign countries are permitted in the foreign country;
- The extent of government ownership or control of the means of production;
- The extent of government control over the allocation of resources and over the price and output decisions of enterprises; and
- Such other factors as the administering authority considers appropriate.

2. Proposed Changes

Denying market economy treatment for Chinese respondents in antidumping cases as a result of government misuse of legal and administrative proceedings would provide a powerful incentive for the GOC to cease such behavior. The Tariff Act could be amended so that a new factor for consideration when a country applies to graduate is whether it uses legal or administrative processes, such as investigations under the AML, to further its industrial policies, promote its national champions, or punish foreign entities that seek to enforce their rights, including intellectual property rights. Such an amendment could take the following form:

(18) Nonmarket economy country.

(A) In general. The term "nonmarket economy country" means any foreign country that the administering authority determines does not operate on market principles of cost or pricing structures, so that sales of merchandise in such country do not reflect the fair value of the merchandise.

(B) Factors to be considered. In making determinations under subparagraph (A) the administering authority shall take into account

(i) the extent to which the currency of the foreign country is convertible into the currency of other countries;

(ii) the extent to which wage rates in the foreign country are determined by free bargaining between labor and management,

(iii) the extent to which joint ventures or other investments by firms of other foreign countries are permitted in the foreign country,

(iv) the extent of government ownership or control of the means of production,

(v) the extent of government control over the allocation of resources and over the price and output decisions of enterprises, ~~and~~

(vi) the extent to which the government uses policies, administrative or legal proceedings, or investigations to promote particular domestic companies or industries or shield them from competition, and
(vii) such other factors as the administering authority considers appropriate.

C. Section 337

1. Background

Section 337 of the Tariff Act addresses the importation of goods that may infringe intellectual property rights or benefit from “unfair methods of competition and unfair acts.” Investigations are conducted by the U.S. International Trade Commission and most often involve claims regarding intellectual property rights, including allegations of patent infringement and trademark infringement by imported goods. Other forms of unfair competition involving infringement of registered copyrights, mask works or boat hull designs, misappropriation of trade secrets or trade dress, passing off, and false advertising, may also be asserted. The primary remedy available under Section 337 is an exclusion order that directs Customs to stop infringing imports from entering the United States. Such exclusion orders have proven very effective in helping protect U.S. entities from imported goods that infringe their intellectual property rights or benefit from other unfair acts.

2. Proposed Changes

Although as currently written Section 337 focuses on the unfair actions of private actors such as companies, as opposed to governments, it may be possible to amend Section 337 to cast the abuse of legal or administrative proceedings by governments as unfair acts as follows:

(a) Unlawful activities; covered industries; definitions
(1) … the following are unlawful, and when found by the Commission to exist shall be dealt with, in addition to any other provision of law, as provided in this section:
(A) Unfair methods of competition and unfair acts in the importation of articles … into the United States, or in the sale of such articles by the owner, importer, or consignee, including the discriminatory use of legal,

administrative, or regulatory proceedings against U.S. entities by foreign governments, the threat or effect of which is—

(i) to destroy or substantially injure an industry in the United States;

(ii) to prevent the establishment of such an industry; or

(iii) to restrain or monopolize trade and commerce in the United States.

…

(d) Exclusion of articles from entry

(2) The authority of the Commission to order an exclusion from entry of articles shall be limited to persons determined by the Commission to be violating this section unless the Commission determines that—

(A) a general exclusion from entry of articles is necessary to prevent circumvention of an exclusion order limited to products of named persons; ~~or~~

(B) there is a pattern of violation of this section and it is difficult to identify the source of infringing products~~.~~; or

(C) the violations stem from government activity, and such violations unfairly advantage an enterprise or group of enterprises, or a significant portion of the industry producing the articles concerned operating within the jurisdiction of the relevant government.

Additional amendments may be necessary to the text of the statute so that the unfair acts of a government can be attributed to companies and the goods they produce.

D. Foreign Direct Investment

1. Background

As China has developed economically, the GOC's focus has been shifting gradually toward outward investment, as reflected in the "going out" provisions contained in China's 12th Five Year Plan. The GOC intends, *inter alia*, to use the country's capital reserves to purchase both high technology and the resources it needs to develop its domestic industries.

The U.S. government has the ability to block or unwind foreign acquisitions of U.S. entities that the governments considers would threaten national security. The Committee on Foreign Investment in the United States ("CFIUS") is an inter-agency committee authorized to review such transactions in order to determine the effect of such transactions on national security. CFIUS operates pursuant to section 721 of the Defense Production Act of 1950, as amended by the Foreign Investment and National Security Act of 2007 and as implemented by Executive Order 11858, as amended.

2. Proposed Changes

The relevant provisions of the Defense Production Act of 1950 could be revised to include the abusive use of legal or administrative processes abroad as a national security concern that could lead the U.S. government to block the acquisition of U.S. assets by Chinese interests. In particular, the relevant section of the law could be revised so that the U.S. government considers the issue when reviewing covered transactions as shown in the underlined text that follows:

> Section 721 Authority to review certain mergers, acquisitions, and takeovers
> (…)
> (f) Factors to be considered.—For purposes of this section, the President or the President's designee may, taking into account the requirements of national security, consider —
> (1) domestic production needed for projected national defense requirements,
> (2) the capability and capacity of domestic industries to meet national defense requirements, including the availability of human resources, products, technology, materials, and other supplies and services,
> (3) the control of domestic industries and commercial activity by foreign citizens as it affects the capability and capacity of the United States to meet the requirements of national security,
> (4) the potential effects of the proposed or pending transaction on sales of military goods,
> equipment, or technology to any country—
> (. . .)
> (5) the potential effects of the proposed or pending transaction on United States international technological leadership in areas affecting United States national security;
> (6) the potential national security-related effects on United States critical infrastructure, including major energy assets;
> (7) the potential national security-related effects on United States critical technologies;
> (8) whether the covered transaction is a foreign government-controlled transaction, as determined under subsection (b)(1)(B);
> (9) as appropriate, and particularly with respect to transactions requiring an investigation under subsection (b)(1)(B), a review of the current assessment of—

(A) the adherence of the subject country to nonproliferation control regimes, including treaties and multilateral supply guidelines, which shall draw on, but not be limited to, the annual report on Adherence to and Compliance with Arms Control, Nonproliferation and Disarmament Agreements and Commitments' required by section 403 of the Arms Control and Disarmament Act;

(B) the relationship of such country with the United States, specifically on its record on cooperating in counter-terrorism efforts, which shall draw on, but not be limited to, the report of the President to Congress under section 7120 of the Intelligence Reform and Terrorism Prevention Act of 2004; ~~and~~

(C) the potential for transshipment or diversion of technologies with military applications, including an analysis of national export control laws and regulations; <u>and</u>

(D) <u>the extent to which the country treats United States interests or investments in a fair and objective manner under its domestic laws and regulations, and whether any such unfair or unobjective treatment threatens the development of industry, technology, commercial activity or national defense requirements in the United States;</u>

(10) the long-term projection of United States requirements for sources of energy and other critical resources and material; and

(11) such other factors as the President or the Committee may determine to be appropriate, generally or in connection with a specific review or investigation.

III. CONCLUSIONS

Unless challenged, the GOC is unlikely to stop using the AML as an industrial policy tool to build up Chinese industry at the expense of foreign companies and interests. This paper presents four options for how Congress could help give the United States government and companies the tools that they need to combat this threat. Members of Congress should consider these and additional changes to U.S. law to provide effective and WTO-consistent disincentives for the GOC to continue wielding the AML in a subjective manner that harms non-Chinese businesses.