

China Intensifies Law Enforcement on Unfair Price Competition: the Unilever Case

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Background

On 6 May 2011, China's National Development and Reform Commission ("NDRC") published a statement commenting on the punishment on Unilever (China) Co. Ltd. ("Unilever") for its unfair price competition acts, endorsing publicly the law enforcement action in Shanghai. In the statement, NDRC said that it noted in late March 2011 a wave of consumer panic buying linked to the rumours of price rise of some home care and personal care products. NDRC and the Shanghai Price Administration Bureau ("Price Bureau"), the NDRC's price law enforcement arm in Shanghai, then conducted a price inspection on relevant products in the market. The inspection revealed that Unilever had conducted some pricing activities which are prohibited by law. The NDRC later instructed the Price Bureau to take action promptly to stop and punish for the illegal activities.

In April, the Price Bureau issued an administrative decision punishing Unilever for "disseminating price rise information to public and distorting the market price order". The decision ordered Unilever to rectify its violations and imposed a fine of RMB2 million or US\$307,000. This is the first and most high-profile price-related law enforcement action against a multinational company in China. Recently, NDRC is seen taking frequent and increasingly aggressive actions to control price and crack down the price-related law violations. These actions highlight not only the determination of the PRC government in combating the rising inflation, but also the specific risks connected to price adjustment in China. China's first quarter CPI (consumer price index) in 2011 rises 5% year on year. Its CPI in March 2011 reached to 5.4%, hitting the three-year high. Premier Wen Jiabao commented in March that curbing inflation is a top economic priority of the work of his government this year.

China now has a more sophisticated legal regime regulating pricing activities. The PRC Price Law, which came into effect in 1998, prohibits a range of activities of "unfair price competition", and sets out the basic principles business operators must follow when pricing their commodities and services. In 2007, China promulgated the Anti-Monopoly Law ("AML") to address pricing issues related to anti-monopoly practice. Issues such as price-fixing, price-related abuse of market dominant position, discriminatory pricing, pricing below cost, unfairly pricing, etc. are dealt with in the law. Recently, NDRC rolls out more regulations to implement AML. The development of price-related law and practice in China may raise more concerns to international business operators, as China is increasing its ability of using more complicated approaches in tackling price-related monopoly issues.

Below we summarise the Unilever case and comment on the relevant legal issues.

Factual Background

The action against Unilever was based on a public announcement and a few press interviews by Unilever. The Price Bureau found Unilever issued a notice in March to its downstream sellers informing the latter that Unilever will increase the price of its home care and personal care products starting from 1 April 2011. Several press interviews were conducted during 21-22 March by Unilever's press officer following the notice. During the press interviews, the officer told the media his forecast that some of Unilever's products have already entered in the period of continuous price rise, due to the inflation of raw material prices. He also stated that Unilever would continuously and gradually raise its price to test the market reaction, especially those from the competitors. He hinted that market and the competitors will follow Unilever to raise their prices.

The Enforcement Action

The statement issued by the NDRC revealed more insights of the case. The Price Bureau asserted that the Unilever notified its distributors of the forthcoming price rise information in early March well before the price rise date, and the subsequent interviews carried out by Unilever on the same information had further helped the information disseminated among the public. The NDRC statement commented that early publishing the price rise information had given time to Unilever's competitors in the market to align their price of similar products. The information has in fact been responded to by the competitors in the market with similar actions. The signalling can help achieve a price cartel without significant change of market share among the competitors. Clearly, NDRC is of the view that Unilever had communicated the price rise information to the market through its notice to resellers and media, and left sufficient time for the market to coordinate the price. However, NDRC did not comment whether publishing the price rise information by Unilever was intended to seek such coordinated acts.

With respect to the effect of the above acts, NDRC contended that they had resulted in increased expectation on the future price rise of the products among customers. NDRC quoted the fact of consumer panic purchase in some cities as a consequence of the dissemination of the information. Cited in the NDRC's comment, the investigators found that the sale of home and personal care products in Shanghai had surged 21.2 times and some detergent products of Unilever's brands increased 65 times to 100 times in some supermarkets in Shanghai and Xi'an, comparing to the sale of the products in the weeks before and after the one Unilever disclosed its price rise information. However, NDRC did not comment on whether there are other market factors considered in linking the quoted surge of sales to the disclosure of the information, and what are the rationales underlying the linkage.

Interestingly, NDRC specifically mentioned in its statements the market leading position of Unilever as a factor relevant to the action taken against it. Unilever's market shares relating to shampoos, soaps and detergents in China are found respectively at 12%, 12.5% and 15.2%. NDRC argued that the fairly large market shares have afforded the company with comparatively large influencing power over the price in the market. Some major domestic competitors had, in fact, after Unilever's price rise announcement, declared the price rise of

their own products, although all withdrew at last for some reasons. NDRC concluded that the conduct of Unilever would have caused rapid and significant rise of the price of home and personal care products in the entire market, if it were not stopped and punished immediately.

The Price Bureau accused Unilever of breaching Article 14 of the Price Law, which prohibits business operators from engaging in the activities of “fabricating or disseminating price rise information for increasing the prices to excessively high.” The law is worded differently from the accusation quoted in the NDRC’s statement, which is “disseminating price rise information to public and distorting the market price order”. The Price Bureau apparently reached its decision on the basis of three key findings, i.e. (i) Unilever disclosed its price rise information to public at a time unnecessarily early, and further disseminated such information among public through media; (ii) the information disseminated had caused high expectation from the public on future hike of the price, evidenced by public panic buying and the extraordinarily high sale increase in some regions; (iii) the dissemination of the information was conducted by a company with large market shares, which made the company of adequate influence over the price in the market. This had enhanced the effect of the price rise information on the market. To hold up the findings, several facts such as media interviews, the surge of sales, following actions from some competitors, market shares of Unilever in some products are considered. The facts such as high public expectation on future hike of price, the leading market position of Unilever, the following actions from other market players are not expressly stated as essential facts to qualify a violation of Article 14 of the Price Law. Apparently, the Price Bureau used them to support that disseminating the information is to or would raise the market price to an excessively high level, if it were not stopped. In another word, it would have severely distorted the market price order. More detailed reasoning behind the establishment of these findings and the decision is unknown.

According to the NDRC statement, the fine was imposed in accordance with the Provisions on Administrative Punishment for Price-related Illegal Activities (the “Provisions”). The Provisions stipulate that the violator of Article 14 of the Price Law shall be ordered to rectify its act and fined no more than five times of the illegal gains or up to RMB3 million, if the case is relatively serious. Under the Provisions, if there are any illegal gains, it shall be confiscated. In the worse case, the violator may be ordered to cease business to rectify its act and its business licence may be cancelled. The Price Bureau is, however, silent on whether there is any illegal gains generated from the violation, but holds the view that the violation is in a “serious” case. Nonetheless, NDRC stated that it has noted that Unilever has already temporarily halted its decision on price rise and issued an apology to its customers publicly to mitigate the adverse effect it has caused to them. The Price Bureau finally applied the fine of RMB2 million as a result of taking the above into account.

Price Monopoly Agreement under AML

AML took effect on 1 August 2008. The law prohibits and punishes competitors and their downstream resellers for reaching any agreement for the purpose of eliminating price competition. Price fixing through monopoly agreement is listed as a prohibited act in the law,

but the law itself provides little detail for implementation. AML has given NDRC additional powers to investigate and punish price law violation in China. However, seen from the past, NDRC seems reluctant to use the AML, but remains keen to rely on the Price Law and other regulations in punishing a price law violation. This may be because more AML enforcement guidelines are still under work or the NDRC's law enforcement departments have more experience in enforcing the Price Law.

NDRC is intensifying its steps in preparing for implementing the AML. It has in December last year promulgated respectively the Anti Price Monopoly Provisions ("APMP") and the Provisions on Procedures relating to Administrative Enforcement of Anti Price Monopoly Laws ("Procedure Provisions"), both of which came into effect in February 2011. These regulations, from the implementation angle, further interpret some key concepts in the AML relating to price monopoly activities and clarified certain procedural issues related to law enforcement action.

In the Unilever case, the enforcement agency again did not refer to the price monopoly rules in the AML. However, companies must be aware that Article 13 of the AML can be used to punish price collusion among competitors too, and the fine can be higher than the Price Law. Article 13 of the AML prohibits a business operator from engaging in price-related monopoly agreement with competitors to fix or to change the price of their products or services. The prohibition on the price-related monopoly agreement was further interpreted by NDRC in the APMP. The APMP clarified that a price-related monopoly agreement under the AML may not necessarily be a clear agreement reached among the relevant parties, but may appear as a kind of "coordinated act" among the competitors or a "decision". In the APMP, NDRC explicitly named two most prominent circumstances among others for judging the conduct of such a "coordinated act". These circumstances are (i) the pricing activities of the competitors are of the character of price alignment, and (ii) the competitors have engaged in a kind of "communication" to coordinate their price, regardless the form of such communication. The APMP lacks of further guidance as to what will constitute the price alignment, the communication, and how to weigh these factors in the complex market context.

The price-related monopoly agreement, as interpreted in the APMP, appears relevant to the Unilever case. Arguably, the findings in the Unilever case may also prove that a coordinated act has been conducted among the competitors as a result of the dissemination of the price rise information. In the Unilever case, it was found that some competitors in the market appear to have responded to the message by raising their product prices. In the light of APMP, this can be used as a key fact to accuse Unilever and other competitors of forming a price monopoly agreement that is prohibited under Article 13 of AML. Unlike Article 14 of the Price Law, all the parties participated in such a price monopoly agreement can be punished for the violation. The punishment under AML for participating in a price monopoly agreement includes an order to stop the violation, confiscation of the illegal gains, and a fine of 1%- 10% of the turnover of the previous year of the violator. Order to cease business or cancellation of business licence is not listed as a penalty in the AML.

Conclusions

As many economists have forecasted, China likely will see a period of time accompanied with high inflation rate. The Chinese government is determined to tackle the inflation by using all the resources at its hands. NDRC, the agency charged with the responsibilities of maintaining price order in China, plays a main role in fighting the price rise. The recent frequent law enforcement actions and price-related legislation indicate that the agency is prepared to take more proactive approaches to stabilize the market prices, especially the prices relating to the consumer products and services. It, however, makes companies in China increasingly concerned about the risks associated with their price adjustment plan.

Whilst NDRC preparing itself for implementing the AML, the agency is seen frequently engaged in price law enforcement actions relying on the powers it has under the Price Law and other associated regulations. Companies must be aware that NDRC is not only equipped with the needed powers, but also determined to stop and punish the violation of China's price laws. Although NDRC has not yet used the AML to punish a price-related violation, the AML is in effect and can be used at any time. Companies that plan to adjust product price must understand and follow all the rules regulating pricing activities in China.

The Unilever case clearly serves as a warning message to the companies who plan to raise price recently, particularly for the market leaders who can exert greater influence over the market. The message may not be interpreted as a ban of future price rise, but companies shall be alerted in regard to how to handle price rise in China. Firstly, release of price rise information shall now be treated as sensitive information both internally and externally. Companies may set up internal rules for managing such information and alert their staffs who can access to such information to handle it with greater caution. Secondly, the release of such information to public may not be at a time unnecessarily early or in a manner easily being considered as a price communication to competitors or business associations, in order to avoid be accused of seeking coordinated price acts. Companies or its management must avoid themselves discussing the information related to any specific price rise, expectations or even a rise of production cost in public. Lastly, companies must keep a close eye on the development of price-related legislation and practice to ensure continuing compliance.

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