



## China to revamp central government and various regulators - what does it all mean?

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## Introduction

Over the past weekend, the Chinese legislature decided on a major restructuring of governmental agencies.

The restructuring plan was announced by the State Council on 13 March 2018, and approved by the National People's Congress on 17 March.

Although the reform was anticipated and has been a public discussion topic since the Central Committee of the Communist Party of China passed a resolution on reforming state institutions on 28 February 2018, the extent and significance of the planned reform measures went beyond the expectation of many commentators.

Based on statements by some of China's high-ranking officials, the purpose of the reform is to re-allocate functions among governmental authorities more rationally, cut red-tape, consolidate law enforcement units, and switch the focus from administrative approval to interim and post-approval supervision. The ultimate goal is to make government more efficient, and remove the mechanical and other obstacles which prevent government from functioning better and the market from playing a decisive role in resource allocation. However, to what extent such aims can be achieved in practice remains to be seen.

What is certain is that, after the reform, the ministerial level institutions of the State Council will be reduced by eight and the vice-ministerial level institutions will be reduced by seven. Correspondingly, the law enforcement powers of the relevant regulators will be more integrated and concentrated in the hands of a smaller number of agencies.

## Establishing a super market regulator

A new "super market regulator", called the State Administration for Market Supervision (国家市场监督管理总局, "**SAMS**"), will assume the functions of the existing State Administration for Industry and Commerce ("**SAIC**"), the

Administration of Quality Supervision, Inspection and Quarantine ("**AQSIQ**") and the China Food and Drug Administration ("**CFDA**"). The new agency will also supervise the restructured State Intellectual Property Office ("**SIPO**").

Importantly for the antitrust world, the three existing antitrust enforcement units within the National Development and Reform Commission ("**NDRC**"), SAIC and the Ministry of Commerce ("**MOFCOM**") will all be transferred to SAMS, which is anticipated to merge them into a single antitrust bureau.

Before the reform, the main regulatory functions of SAIC, AQSIQ and CFDA respectively covered:

- i. business registration, domestic commodity circulation supervision, trademark administration, and non-price related antitrust law enforcement;
- ii. organizational code management, industry manufacturing licensing, and product quality inspection; and
- iii. registration, production, and the administration of the distribution and import and export of foods, pharmaceuticals, medical devices, and so forth.

Following the reform, SAIC, AQSIQ and CFDA will no longer exist, while SAMS will become a market regulator overseeing the entire lifecycle of a full spectrum of products, with enforcement powers covering all types of unlawful behaviour, ranging from business registration to market competition.

### (a) Antitrust merger

At present, the powers to enforce the Anti-Monopoly Law ("**AML**") are divided between (i) the NDRC Price Supervision and Anti-Monopoly Bureau, whose jurisdiction covers enforcement actions against restrictive agreements, abuse of dominance and anti-competitive

government practices that are related to pricing, (ii) the SAIC Anti-Monopoly and Anti-Unfair Competition Enforcement Bureau, whose scope of enforcement relates to the same types of activities as NDRC's, except where they are not related to pricing, and (iii) the MOFCOM Anti-Monopoly Bureau, which is in charge of merger control.

The antitrust enforcement triumvirate was the result of a compromise between competing fractions vying for enforcement powers at the time the AML was enacted in 2007. This institutional set-up has remained in place for almost 10 years, but has led to some inconsistency and uncertainty both for the authorities and market players. Both NDRC and SAIC issued substantive rules implementing the AML in their respective regulated areas, but the rules are not entirely consistent and there are some areas of overlap. Both authorities also released procedural rules which are similar, but not identical. Perhaps most importantly, the culture and enforcement styles of the authorities have been markedly different. This has led to uncertainty for market players as to what the applicable rules are and how they should ensure compliance.

The plan to merge the three antitrust units into SAMS should reduce this uncertainty to a large extent. In the future, the SAMS antitrust bureau is expected to issue a single set of implementing rules and guidelines and follow the same procedures in its enforcement actions. In this sense, the merger of antitrust units should be a positive development for businesses.

The government restructuring will have additional repercussions on the antitrust world. In the short term, the restructuring is likely to have an impact on existing cases before the authorities. In general, we expect the officials in the existing antitrust authorities to set aside substantial blocks

of time for transitioning to the new authority, which has the potential of slowing down the pace of on-going proceedings such as merger investigations. In some instances, however, we may see the opposite effect, an acceleration in procedures relating to on-going cases, if the officials at the existing authorities want to "clean desks" before moving to the new agency.

In the medium term, we would expect the SAMS antitrust bureau to get off to a slow start. It would be understandable for the SAMS officials to focus part of their attention on drafting internal rules and protocols and issuing fresh AML implementing rules and guidelines for businesses. These rules may cover both substantive and procedural aspects, replacing or consolidating the existing NDRC, SAIC and MOFCOM rules. It is also possible that the new antitrust bureau will continue the efforts of drafting new guidelines on a variety of aspects of AML implementation – the leniency program; the commitment procedure; the exemption procedure; the principles for imposing fines (at the moment put on hold); sector-specific rules for the automotive industry; the relationship between antitrust and intellectual property; rules on standard essential patents; and rules on vertical restraints more generally – which are currently on-going (mainly at the instigation of NDRC).

It is probably too early to have a clear idea about the direction of future competition policies and enforcement priorities for the new antitrust bureau. This will depend not only on the structure of the bureau, but also on which and how many officials will join the bureau and its appointed leadership. On a high-level note, however, we anticipate some degree of continuity in policy and enforcement action. For example, the healthcare sector has been a

focus of antitrust enforcement for all three existing antitrust authorities. The top levels of the Chinese government and consumers view this sector as important to China's future development, so we would expect antitrust enforcement to continue after the government restructuring.

In short, while the longer-term implications of the government reshuffle for the antitrust community are not yet all known, it is clear that the merger of the three existing antitrust enforcers is a game-changer, just as the AML approaches its 10th anniversary.

#### **(b) Food and Drug Administration**

The China Food Safety Commission will remain in existence, but its specific tasks will be taken on by SAMS. Due to the specialist nature of drug administration, a dedicated body, to be named the National Drug Supervision Administration (国家药品监督管理局, "NDSA") will be established under SAMS.

China's food administration regime has undergone extensive reforms over the last few years. The State Council established

CFDA in 2013 largely in response to food safety scandals and widespread public outrage. After its establishment, CFDA took over the food production administration function from the then AQSIQ as well as the food circulation administration function from the then SAIC, thus making it the primary regulator supervising the entire life cycle of food products. But this time around, given that NDSA will be created to take sole charge of drug supervision, it appears that the food administration function will again be removed and re-allocated to a separate bureau under SAMS.

Despite its name, administration and supervision of medical devices will most likely fall within NDSA's responsibilities. With this new government restructuring, the local counterparts of NDSA will be set up at provincial level. It is therefore anticipated that NDSA will mainly be responsible for marketing authorizations and the manufacturing aspects of pharmaceuticals and medical devices, while the distribution process will be supervised by lower-level departments within SAMS.



**(c) Import of products**

While AQSIQ will be merged into SAMS and will disappear, AQSIQ's exit-entry inspection and quarantine administrative functions will be transferred to the General Administration of Customs ("GAC"). This should mean that the import and export process for goods should, to some extent, be streamlined in the future, as GAC becomes a 'one stop shop.'

At present, enterprises engaging in the import and export of goods need to separately register with China Inspection and Quarantine (a branch of AQSIQ) and GAC and make both customs declarations and quarantine declarations during the import and export process. Following the restructuring, a merger of the registration and declaration processes may also be on the cards.

**(d) Intellectual property merger**

The existing SIPO will be restructured, with its responsibilities enlarged to cover the SAIC's original trademark administration function and the AQSIQ's original administration of geographic indications of origin function.

SIPO was formerly known as the China Patent Office, and its main functions include patent application review and patent enforcement. After the reform, SAMS will assume the mantle of the key regulator in administrative protection of patents, trademarks and geographic indicators of origin.

In this way, the revamped intellectual property protection regulator will undergo a change similar to that in the antitrust space: the powers of three different enforcement agencies will be merged into the revamped SIPO.

**Merging the banking and insurance watchdogs**

The China Banking Regulatory Commission ("CBRC") will merge with the China Insurance Regulatory Commission ("CIRC") into the China Banking and Insurance Regulatory Commission (中国银行保险监督管理委员会, "CBIRC"), while the legislative and rule-making functions of the CBRC and CIRC will be transferred to the People's Bank of China ("PBOC").

This move has been interpreted as a measure to address the trend of financial institutions engaging in cross-over business. In line with the rapid evolution of China's financial services industry, the banking industry and the insurance industry are leaching into each other, e.g. certain life insurance products are starting to bear characters of bank savings products, and commercial banks have recently become the main distribution channel for insurance products. Establishing a unified watchdog may be helpful in terms of consolidating scarce



regulatory resources, better utilising the skills of experienced professionals, and control systemic risks which cannot be effectively identified by siloed supervision.

Regarding the transferring of the legislative and rule-making powers to PBOC, it is reportedly to separate the functions of nurturing and supervising the market. The functions of promoting the development of the financial services market will be assumed by PBOC, which will coordinate the drafting and promulgation of legislation across different financial sectors so as to avoid potential inconsistencies in approach and 'turf wars.' In turn, CBIRC will be able to focus on its regulatory and supervisory roles unhindered by conflicting policy directives and directions.

### Tax authority consolidation

In addition to the central government reforms, the local tax bureaus and state tax bureaus at the provincial level and below will also merge. The new tax bureaus will operate under the dual guidance and direction of the State Administration of Taxation ("SAT") and the local provincial-level government.

China has been promoting cooperation and collaboration between the central state tax authority and local tax authorities since 2015, and this consolidation in effect forces the hand of local government. It is predicted that after the consolidation, with the dual track administration system being replaced, businesses will reap the benefits of the consolidation of their tax affairs, and the administrative measures adopted by tax authorities will be more unified. Furthermore, enforcement against tax irregularities may also be strengthened due to the consolidation of law enforcement units within the SAT.



## Other major changes

Other major steps in the consolidation of ministries and other main government bodies will include:

- reforming the existing National Health and Family Planning Commission into the National Health and Hygiene Commission (国家卫生健康委员会), which will also take over functions of coordinating and advocating reform of the medical and healthcare administrative regimes;
- restructuring the existing Ministry of Land and Resource ("MLR"), State Ocean Administration ("SOA") and National Administration of Surveying, Mapping and Geo-information into the Ministry of Natural Resources (自然资源部), which will also take over natural resource planning and administrative functions from other relevant ministries and administrations, e.g. NDRC, Ministry of Water Resources and so forth;
- dissolving the Ministry of Environmental Protection, transferring its functions, the climate change addressing and emission reduction functions within NDRC, the underground water protection function of the MLR, the ocean protection function of the SOA, among others, to a newly-established Ministry of Ecological Environment (生态环境部); and
- establishing the Ministry of Emergency Management (应急管理部) to assume the functions of the existing State Administration of Work Safety and take over the emergency management functions of the General Office of the State Council, the fire control management functions of the Ministry of Public Security, the disaster relief functions of the Ministry of Civil Affairs, the drought and flood relief functions of the Ministry of Water Resource, earthquake emergence response functions of China Earthquake Administration and so forth,

thereby consolidating all such functions into a single unit, presumably to provide a better, more coordinated and less siloed response to natural and other disasters.

In addition, China is to (i) establish the Ministry of Agriculture and Rural Areas (农业农村部) to replace the Ministry of Agriculture, establish the Ministry of Culture and Tourism (文化和旅游部) to replace the Ministry of Culture and the National Tourism Administration, establish the State Administration of Broadcasting and Television (国家广播电视总局) to replace the State Administration of Press, Publication, Radio, Film and Television, establish the State Administration of Grain and Material Reserves (国家粮食与物资储备局) to replace the State Grain Administration, and establish the State Administration of Forest and Grasslands (国家林业和草原局) to replace the State Forestry Administration; (ii) and establish various new bodies, such as the Ministry of Veteran Affairs (退役军人事务部), the State Administration of Healthcare Security (国家医疗保障局) and the State Immigration Administration (国家移民局); and (iii) restructure the Ministry of Science and Technology and the Ministry of Justice.

## Conclusion

This is the most significant government restructuring and reallocation of regulatory functions since 2013. It cannot, of course, be completely divorced from the major political changes going on in China in the background, but it does, overall, seem to us to be a move in the right direction, removing many notorious overlaps and/or reducing the potential for agencies tripping over each other or fighting 'turf wars' amongst themselves. It also represents a substantial modernisation of the administrative system in China, with nods in the direction of military veterans, healthcare safety and ecology, as well as recognising the convergence and cross-over of financial services products.

Perhaps the other interesting observation about the restructuring is what was left out: namely the all-powerful telecoms and Internet regulator, the Ministry of Industry and Information Technology, which has historically not been particularly encouraging of foreign investment, which appears to have escaped the restructuring unscathed. This suggests that China will continue to maintain an iron grip on these perceived sensitive and critical sectors, where China has upped the ante recently with the creation of the China Cyberspace Administration, following a frenetic pace of issuing cybersecurity-related and data-privacy-related legislation in recent years.

As with any merger, old loyalties die hard, so query how easy it will be for a former CBRC civil servant to view even-handedly the prospect of the distribution of say insurance products through non-banking institutions in China. That said even if leopards cannot change their spots (at least not overnight), it is clear that past practices and old tribal loyalties will need to be broken down if the reform is to truly achieve its aims. Conflicts are likely to continue to be an issue, especially in areas like tax where SAT appears to be to some extent reining in the powers of local tax bureaus.

In short, China is undertaking an exercise to make sure it is 'fit for the future.' With this major government reshuffle, the government agencies you need to engage with for your business in China many undergo significant changes, and their law enforcement practices may also alter as a result of the changes in personnel or policy. As one of the most well-established and largest foreign law firms in China, our extensive experience on the ground in China and our relationships with government can help you assess the real impact of the reform, and help you address such changes in a way that minimizes any negative impact on your business.

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