

## **Tetra Pak Receives SAIC's Severest Antitrust Penalty**

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### **Introduction**

On November 9 2016, after a nearly five-year investigation, the State Administration for Industry and Commerce (SAIC) finally concluded the Tetra Pak case. The SAIC's landmark decision:

- imposed a Rmb667,724,176.88 (approximately \$97 million) penalty on Tetra Pak – equivalent to 7% of the Swiss packaging giant's 2011 China sales – for its abuse of a dominant position in China; and
- ordered Tetra Pak to cease its illegal conduct.

This is the largest antitrust fine ever imposed by the SAIC and the second largest penalty imposed in China's eight-year antitrust law enforcement history (the Rmb6.088 billion (\$975 million) penalty imposed on Qualcomm in 2015 by the National Development and Reform Commission of China remains the largest). Six affiliated companies of Tetra Pak were involved in the case:

- its headquarters registered in Switzerland;
- its holding company in Hong Kong; and
- four manufacturing entities in China.

The case demonstrates that Chinese anti-monopoly agencies have extensive power when regulating anti-monopoly activities that occur in China, and that all entities – including offshore companies – will be subject to their scrutiny if they fail to comply with China's anti-monopoly laws.

The milestone decision signals the SAIC's determination to enforce antitrust law and its aggressive approach regarding complicated competition issues. The 47-page decision is the lengthiest administrative decision ever released by a Chinese antitrust agency. The decision is well drafted and provides detailed analysis regarding:

- market definition;
- the identification of a dominant position; and
- abusive behaviour.

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In particular, the decision is the first ruling to involve loyalty discounts, a behaviour not clearly defined in the Anti-Monopoly Law. Further, the decision's lengthy and in-depth economic analysis and reasoning provide useful guidance on practical competition issues, such as tying, exclusive dealing and justifiable reasons.

### **Analytical method and key findings**

Although the decision is innovative and aggressive, the SAIC followed its usual analytical method and identified Tetra Pak's illegal conduct by:

- defining the relevant market;
- analysing Tetra Pak's dominant market position;
- identifying Tetra Pak's abusive behaviour; and
- assessing the anti-competitive effect of the abusive behaviour and whether there were justifiable reasons for it.

After comparing Tetra Pak's products with similar products from both a demand-side and supply-side substitution perspective, the SAIC identified the relevant product markets as the market for:

- aseptic paper packaging equipment for liquid food;
- technology services regarding aseptic paper packaging equipment for liquid food; and
- materials used for aseptic paper packaging for liquid food.

As regards the geographical market, the SAIC concluded that all three markets were nationwide, based mainly on the common practices, customs tax, transportation costs and localisation sourcing policy of the downstream customers in China.

In terms of the identification of a dominant market position, the SAIC assessed the factors prescribed in Article 18 of the Anti-Monopoly Law – for example:

- Tetra Pak's market share in the relevant market and the market's competitiveness;
- Tetra Pak's ability to control the market;
- the extent to which other undertakings had depended on Tetra Pak; and
- the difficulty that other undertakings had encountered in entering the relevant market.

According to the penalty decision, the SAIC identified that Tetra Pak had held a dominant position in the three markets above between 2009 and 2013. The SAIC concluded that Tetra Pak had abused this dominant market position by:

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- conducting tying practices when selling and renting out equipment and providing technology services;
  - restricting upstream suppliers from selling raw material paper to its competitors; and
  - running a loyalty discount programme to exclude or restrict competition.

The SAIC rejected Tetra Pak's argument that it had had justifiable reasons for the above behaviour and stated that the conduct had eliminated and restricted competition in the relevant markets.

### **Tying practice**

The SAIC found that Tetra Pak had tied packaging materials when supplying its aseptic paper packaging equipment by requesting that its customers use:

- Tetra Pak packaging materials or packaging materials "recognized by Tetra Pak" during the trial (ie, performance) period; and
- Tetra Pak packaging materials or packaging materials of "equivalent quality" during the warranty period.

Further, Tetra Pak had engaged in similar tying conduct when renting packaging equipment and providing technology services.

Under Article 17(5) of the Anti-Monopoly Law, a business operator in a dominant position is prohibited from conducting tying practices without a justifiable reason. Although Tetra Pak presented arguments to support its tying practice, the SAIC rejected all of these arguments. For example, Tetra Pak claimed that the tying of its packaging materials had been necessary to ensure the verification of the equipment's performance. However, the SAIC stated that other brands of packaging materials that met the relevant industry standard were a proper substitute for Tetra Pak's materials and would have no impact on the performance of Tetra Pak's packaging equipment. Tetra Pak also argued that it had tied its packaging materials in order to protect consumer health and address food safety concerns. However, the SAIC stated that Tetra Pak's tying practice was irrelevant with regard to safety concerns and consumer protection, and that there was no evidence that other suppliers' packaging materials involved higher food safety risks than Tetra Pak's.

In conclusion, the SAIC determined that Tetra Pak's tying practice did not agree with common business practices and lacked justifiable reasons. By adopting such tying practice, Tetra Pak had:

- limited its customers' choice of packaging materials;
- affected the sales of other competitors; and

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- restricted overall competition in the materials market.

### **Exclusive dealing**

According to the SAIC, Tetra Pak had requested its supplier of kraft base paper (the raw material paper used for its packaging materials), Foshan Huaxin Packaging Co Ltd, and its subsidiary, Zhuhai Hongta Renheng Paper Co, Ltd (collectively, 'Hongta'), to supply raw paper exclusively to Tetra Pak and its affiliates. Under the exclusive supply arrangement, Hongta could not sell kraft base paper to other third parties or use any Tetra Pak technologies for purposes other than producing products for Tetra Pak. The SAIC found that the scope of 'Tetra Pak technologies' was too broad and contained many technologies in the public domain. Further, Hongta owns the patents for producing kraft base paper, and the SAIC concluded that Tetra Pak's restriction on Hongta's use of its own patents had prevented Hongta from supplying kraft base paper to third parties.

Article 17(4) of the Anti-Monopoly Law provides that a business operator in a dominant position is prohibited from requesting its trade partners to deal exclusively with itself or its designated business operator without any justifiable reason. According to the SAIC, Hongta owns patented technology to produce kraft base paper and Tetra Pak did not transfer or licence kraft base paper production technology. Further, Hongta's supply of kraft base paper to other customers would not jeopardise its cooperation with Tetra Pak. Tetra Pak had had no legitimate right to restrict Hongta from using public knowledge in its production, and, as such, the SAIC determined that:

- Tetra Pak's restrictive arrangement had lacked justifiable reasons; and
- Tetra Pak had breached the Anti-Monopoly Law, abused its dominant position and eliminated competition in the materials market.

### **Loyalty discounts**

In its decision, the SAIC made a breakthrough in its determination of illegal conduct in relation to loyalty discounts. According to the penalty decision, loyalty discounts violate Article 17(7) of the Anti-Monopoly Law, which was invoked for the first time as a miscellaneous provision. Unlike the preceding provisions of Article 17 of the law, which target specific types of abusive conduct, Provision 7 is a catch-all provision that prohibits other forms of abuse of dominance determined by the antitrust authorities under the State Council.

The SAIC took an unusual approach to the controversial issue of loyalty discounts. In

particular, it used concepts that were new to the Chinese antitrust enforcement regime (eg, retrospective and customised discounts) to identify Tetra Pak's anti-competitive conduct. The SAIC found that Tetra Pak had adopted retrospective and customised discounts to induce its customers to buy as many of its products as possible and foreclose competition in the materials market. 'Retrospective discounts' refer to a scenario in which the customer purchases a set quantity of a product within a certain period and can subsequently enjoy a discount on another unit of the product. They apply to all products purchased within the allotted period. 'Customised discounts' refer to when a seller provides different discounts depending on the size and purchasing power of the customer and target a different class or category of customer.

Further, the SAIC used detailed economic analysis to show that the nature of loyalty discounts would have induced downstream buyers to purchase substantial portions or all of their requirements from Tetra Pak, restricting competition to a great extent. In particular, the SAIC analysed the loyalty-inducing effect of this practice in its decision. As a dominant player in the materials market, Tetra Pak had been able to leverage its dominance by lowering the price of a portion of its products for customers that may have otherwise switched to different suppliers, inducing customers to continue purchasing from it.

### **Comment**

This case provides a strong indication of the SAIC's growing competency in complicated investigations and analysis. Further, its innovative approach to assessing unspecified monopolistic behaviour is a milestone in antitrust law enforcement and its decision will serve as a valuable precedent. Further, the penalty decision provides a detailed example of analysis in an abuse of market dominance case. The decision provides clear guidance on how justifiable reasons will be evaluated when determining an abuse of dominance in practice. Companies holding a dominant position should carefully review their business practices in China to ensure full compliance with the country's increasingly challenging antitrust enforcement regime. Conduct (eg, the provision of loyalty discounts in this case) that is not expressly prohibited under the Anti-Monopoly Law or lawful in other jurisdictions could still be scrutinised by Chinese antitrust agencies.