China's Blocking Statute Counteracting Unjustified Extraterritorial Application of Foreign Laws

As the first departmental legislation of the Ministry of Commerce (MOC) in 2021, Rules on Counteracting Unjustified Extraterritorial Application of Foreign Legislation and Other Measures (Blocking Rules) were published with immediate effect beginning Jan. 9, 2021. Given the trade, technology, and even diplomacy...
tensions between the United States and China, a series of legislations were promulgated starting in the second half of 2020. Apart from the Blocking Rules, the MOC also issued the Provisions on the List of Unreliable Entities on Sept. 19, 2020, and the National People’s Congress issued the Export Control Law on Oct. 17, 2020. These new laws set out a preliminary framework for China’s trade compliance regime. However, given the brevity of the 16-article Blocking Rules, clarification is needed in subsequent implementation.

1. Background and Target of the Legislation

The Blocking Rules apply where “extra-territorial application of foreign legislation and other measures, in violation of international law and the basic principles of international relations, unjustifiably prohibits or restricts the citizens, legal persons or other organizations of China (Chinese Entities) from engaging in normal economic, trade and related activities with a third state (or region) or its citizens, legal persons or other organizations.” According to a distinguished professor of Renmin University of China, Han Liyu, who was invited by the MOC to attend an official announcement on the new law, the Blocking Rules aim to block the application of “secondary sanctions.” It is unclear whether the Blocking Rules are applicable to primary sanctions, where such laws prohibit or restrict a third-country party from trading with Chinese Entities. For example, a certain Chinese technology company is included on the Entity List of the United States and is therefore restricted from obtaining chip products manufactured by U.S.-originated equipment without a license or where a license restriction does not apply. Lawyers and scholars are debating this issue, and the MOC’s subsequent practice may be the only solution to the disagreement. Either way, the Provisions on the List of Unreliable Entities could be a possible alternative for Chinese entities encountering suspension of transactions by a counterparty in a third state.

2. The Reporting Obligation of Chinese Entities and MOC Countermeasures

Chinese Entities must report to the MOC within 30 days foreign laws and measures prohibiting or restricting their business with third-party states or entities. It is implied that Chinese subsidiaries of foreign companies are also subject to this reporting obligation.

The Chinese government will establish a working mechanism (Working Mechanism) composed of various central government departments led by the MOC. The Working Mechanism may, in its own discretion, issue prohibition orders (Prohibition Orders) against recognition, enforcement, or compliance with such foreign laws and measures. A Chinese Entity may apply to the MOC for exemption from compliance with a Prohibition Order.

3. Penalties and Remedies

Chinese Entities’ failure to comply with the reporting obligations or failure to comply with the Prohibition Orders may lead to administrative penalties such as warnings, orders of rectification, and fines.

If a party's compliance with foreign laws and orders infringes upon Chinese Entities’
legitimate rights and interests, Chinese Entities may initiate litigation against such party (either a Chinese or a foreign entity) in a Chinese court for compensation. Similarly, if a party benefits from a foreign judgement or order rendered under the foreign laws and measures that cause damages to Chinese Entities, such Chinese Entities may initiate litigation in a Chinese court for compensation.

4. Repercussions for Multinational Companies

Multinational companies with presence in both China and the United States may have been placed in a dilemma of conflicting compliance requirements. If the MOC declares a Prohibition Order against certain U.S. sanctions, the Chinese subsidiary of a U.S. company will need to apply for an exemption to comply with U.S. sanctions without violating the Prohibition Order.

However, that leaves two questions unanswered: On what ground can the Chinese subsidiary apply for such exemption? It is possible that the MOC will not grant an exemption simply because the applicant may be penalized or sanctioned by the U.S. government for its violation of U.S. sanctions. Also, will the foreign parent company be protected by this exemption? Under the Blocking Rules, only Chinese Entities may apply for an exemption.

Furthermore, if a multinational company is sued in Chinese court for violating the Blocking Rules, will the Chinese court frown upon its corporate veil given that the company owns nothing in China for the enforcement of the judgment? Will the Chinese court order recovery from the company's Chinese operations?

5. New Considerations for Contract Negotiation

To mitigate the impact of the Blocking Rules, parties to cross-border deals may consider adjusting certain customary clauses in their contracts. However, considering the unpredictable political environment and legal practice, it is impossible to propose a one-size-fits-all solution. Rather, the following issues are worth reconsidering in negotiation:

1. **Representations and Warranties**

It is common practice for transaction documents to include representations and warranties of compliance with foreign laws and sanctions. With the promulgation of the Blocking Rules, the parties may have been put in a dilemma, as they may either breach foreign laws or sanctions or breach the Blocking Rules (Chinese law). Therefore, the parties should reconsider the representations and warranties clause and probably make necessary carve-outs.

2. **Dispute Resolution in Cross-Border Deals**

Though Chinese Entities may bring lawsuits in Chinese courts for compensation for violation of the Blocking Rules, dispute resolution in a cross-border deal is typically governed by the contract. Parties may agree that foreign law governs the contract, and the venue of dispute resolution should exclusively be a tribunal or a court.
outside China. However, it is unclear if such agreement would prevail over the application of the Blocking Rules and Chinese court’s jurisdiction. Furthermore, if a party does bring a lawsuit in a Chinese court despite the dispute resolution clause in the contract, it is hard to predict how the parallel litigations will develop.

6. Conclusion

The Blocking Rules create considerable uncertainty and obscurity. In the absence of further official explanation or practice, parties to cross-border deals may temporarily mitigate the risks through due diligence and well-drafted contracts.

The State Council Officially Publishes the Full Text of the Administrative Regulations on Pollutant Discharge Permits

State Council Officially Publishes the Full Text of the Administrative Regulations on Pollutant Discharge Permits

In late December 2020, the State Council officially adopted the Administrative Regulations on Pollutant Discharge Permits (Administrative Regulations) and published the full text on Jan. 24, 2021. The Administrative Regulations took effect on March 1, 2021.

First, pollutant discharging entities with different amounts of pollutant production, emissions, and environmental impact are subject to varying levels of regulation (represented by different types of permits). The Administrative Regulations authorize the Ministry of Ecology and Environment (MEE) to formulate a detailed list of pollutant discharging entities subject to such varying levels of regulation. The table below may help to illustrate the regulatory framework:

<table>
<thead>
<tr>
<th>Regulatory Requirement</th>
<th>Amount of Pollutant Production</th>
<th>Amount of Emissions</th>
<th>Environmental Impact</th>
</tr>
</thead>
<tbody>
<tr>
<td>Discharge Permit under Critical Regulation</td>
<td>Comparatively Large</td>
<td>Comparatively Large</td>
<td>Comparatively Large</td>
</tr>
<tr>
<td>Discharge Permit under Simplified Regulation</td>
<td>Comparatively Small</td>
<td>Comparatively Small</td>
<td>Comparatively Small</td>
</tr>
<tr>
<td>Regulation by Filling a Registration Form</td>
<td>Very Small</td>
<td>Very Small</td>
<td>Very Small</td>
</tr>
</tbody>
</table>

In fact, this regulatory framework is the same as the one under the current Administrative Measures for Pollutant Discharge Permits (for Trial Implementation) (Administrative Measures) promulgated by the Ministry of Environmental Protection (predecessor of the Ministry of Ecology and Environment) and its supporting document, the List of Classification Management of Fixed Pollution Source Discharge Permits (2019 Edition) (2019 Edition List) promulgated by the MEE. The...
2019 Edition List is a catalog of various pollution sources, such as mining, ink production, electrical appliance production, etc. Companies running plants classified as pollution sources according to the catalog must apply for pollutant discharge permits.

As mentioned above, the MEE will draft a similar catalog of pollutant discharging entities and pollution sources subject to different regulation, but the 2019 Edition List will continue to be in effect until the MEE publishes a new list. That is to say, after the Administrative Regulations come into effect and before the MEE publishes a new list, companies should refer to the 2019 Edition List to determine what level of regulation they are subject to and what types of permits they should apply for.

Compared with the Administrative Measures, the Administrative Regulations impose complicated and strict obligations on pollutant discharging entities. In addition to obtaining pollutant discharge permits, these entities are required to accurately and faithfully record their pollutant discharge. Violations of the Administrative Regulations will lead to punishment more severe than violations of the Administrative Measures. All data on pollutant discharging entities related to the pollutant discharge permits will be published on an online, public system maintained by the MEE. Such information includes the application for and approval of pollutant discharge permits, details of pollutant discharge, results of inspection by the MEE, and penalties imposed by the MEE, subjecting the pollutant discharging entities to extensive supervision.

**Anti-Monopoly**

**AMC Issues Anti-Monopoly Guide for the Platform Economy Sector**

On Feb. 7, 2021, the Anti-Monopoly Commission of the State Council (AMC) issued the *Anti-Monopoly Guide (Guide)*, which took effect on the same date. The Guide includes a total of 24 articles in six chapters, e.g., General Provisions, Monopoly Agreements, Abuse of Dominant Market Position, Concentration of Undertakings, Abuse of Administrative Power to Eliminate or Restrict Competition, Supplementary Provisions.

The *Guide* provides relevant definitions for “platform,” “platform operators,” and “platform-based operators” and sets the tone for conducting case-by-case evaluations on defining relevant commodity markets and regional markets in the platform economy sector because different types of monopoly cases have different actual demands for the definition of relevant markets. Further, the *Guide* adopts the definition of multiple relevant commodity markets based on multilateral commodities involved in a platform (interpreted as an introduction of the “two-sided markets” theory by the law review articles published by a Wechat post official account, “Wuhan University Competition Law”). The *Guide* also explains that the forms of collaborative practices involving substantive coordination and consensus by means of data, algorithms, or platform rules (notwithstanding that there is no explicit agreement reached or decision made by the operators) are deemed monopoly agreements in the platform economy, except for those parallel practices carried out
by the relevant operators on the basis of independent declaration of intention.

The *Guide* appears to apply the approach, similar to the *Rule of Reason* (the legal doctrine used to interpret the U.S. Sherman Antitrust Act), of the case-by-case analysis, as the platform economy involves complicated business types and changeable competition dynamics. Article 4 of the *Guide* stipulates that defining the relevant market is generally required for the investigation of cases suspected of constituting a monopoly agreement and abuse of a dominant market position, and for the review of the concentration of undertakings in the platform economy sector. The basic method for defining the market (both the relevant commodity market and the regional market) is to adopt the substitution analysis – demand substitution and supply substitution analysis for different cases. Article 7 of the *Guide* stipulates that the following factors, among others, may be considered when analyzing whether a vertical monopoly agreement is made:

- market power of the platform operator
- status of competition in the relevant market
- degree of hinderance to other operators’ access to the relevant market
- impact on the interests of customers and innovation.

As described below, the either-or practice is one factor in determining the presence of a restriction on transactions. Article 15 of the *Guide* provides that whether an operator requires its platform-based operators to “choose one from two” competitive platforms or limits its transaction counterparts to entering into transaction only with it may be considered when determining the constitution of transaction restrictions. The *Guide* further explains that two scenarios may be considered when analyzing the constitution of limitations on a transaction: (i) punitive measures such as shielding the store, degrading the right to be searched out [on the platform], restricting the network traffic [of the store], imposing technology restriction [on the store], and deducting deposit [of the store], generally may be deemed restrictions on transactions (this appears to apply the approach similar to the *Per Se Rule*, i.e., certain categories of agreements are presumed to violate antitrust laws, regardless of other factors such as business purpose or competitive benefits); (ii) the incentive measures such as providing subsidies, discounts, preferential offers, and traffic resource support (which may have a certain positive effect on the interests of platform-based operators and consumers and the overall welfare of society) may still constitute a restriction on transactions if such measures have an obvious impact of eliminating or restricting market competition, as proved by evidence (this appears to apply the approach similar to the *Rule of Reason*). In addition, the *Guide* provides options for platform operators to defend and justify their measures as necessary to protect: intellectual property rights, trade secrets or data security; the interests of transaction counterparts and consumers; specific resource inputs for transactions; or a reasonable operation mode.

In April 2021, the State Administration for Market Regulation (SAMR), China’s national antitrust enforcement agency, issued a penalty decision against a technology company that implemented the “choose one from two” practice by prohibiting platform-based operators from opening online stores or participating in
promotional activities on competitor platforms and taking other punitive or incentive measures to restrict the platform-based operators to only transact with the company.

In Chapter IV - Concentration of Undertakings, the Guide expressly includes the variable interest entities (VIE) into the scope of anti-monopoly review. On Dec. 14, 2020, SAMR issued three penalty decisions in three cases where the concentrations of undertakings were not declared in accordance with law. The entities involved were fined the maximum 500,000 Chinese yuan. Such cases share the common ground that the acquiring parties are internet platforms, and no effect of eliminating or restricting competition is found after the analysis of authority.