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Analysis on SPC Interpretation on Certain Issues Concerning the Application of Law in Trying Cases Involving Labor Disputes (IV) (Authors: Eric LIU, Ning LI)

The *Labor Contract Law*, the *Law on Labor-dispute Mediation and Arbitration*, the *Regulations on Implementation of the Labor Contract Law*, and other such laws and regulations have enhanced the protection on the employees' rights and interests, thus increasing awareness of labor rights. The number of labor dispute cases that the People's Court receives has also increased, but there are still a wide variety of problems that have yet to be solved within the judicial practice. For the purpose of guiding the judicial practice and solving various problems, the Supreme People's Court promulgated the *Interpretation of the Supreme People's Court on Certain Issues Concerning the Application of Law in Trying Cases Involving Labor Disputes (IV)* (hereinafter referred to as "**Interpretation IV**") on January 18, 2013. The Interpretation IV came into effect on February 1, 2013.

The 15 articles of Interpretation IV attempt to address issues such as the connection between court proceedings and arbitration proceedings, mediation, economic compensation, non-competition, oral amendments to the labor contract, and foreign employees.

The following is a summary and analysis of the main features of Interpretation IV.

I Connection Between Court Proceedings and Arbitration Proceedings

According to Article 47[1] of the *Law on Labor-dispute Mediation and Arbitration*, for some minor labor disputes, the arbitration award shall be final and take legal effect from the date the award is made. However, such final arbitration award is only binding to the employer. Where an employee is dissatisfied with the arbitration award, he/she may file a lawsuit with a people's court pursuant to Article 48[2] thereof.

Interpretation IV specifies employers' rights on filing a lawsuit with a people's court in the following items:

[1] **Article 47** For the following labor disputes, the arbitral award shall be final and take legal effect from the date such award is made, unless otherwise provided for in this Law:

(1) disputes involving the recovery of labor remuneration, medical expenses for job-related injury, economic compensation or damages, and the amount involved does not exceed that of the standard local monthly wage rates multiplying 12 months; and

(2) disputes arising over working hours, periods of rest and vacation, and social insurance, etc., in the course of applying the occupational standards of the State.

[2] **Article 48** Where an employee is dissatisfied with the arbitral award as prescribed in Article 47 of this Law, he/she may file a lawsuit with a people's court within 15 days from the date the employee receives the award.

(1) where an employer is dissatisfied with the final arbitration award, it may apply for revocation of such award with an intermediate people's court. Where an employer is dissatisfied with the non-final arbitration award, it may file a lawsuit with a basic people's court;

(2) whether the arbitration award is final or not shall be determined in accordance with its type as indicated therein. Where the type of arbitration awards is not indicated, it shall be determined by a basic people's court.

II Calculation of Employment Period when Employee is Relocated to New Employer due to Reasons not Attributable to Employee

Article 4 of Interpretation IV provides that where an employee is relocated to a new employer due to reasons not attributable to the employee (such as the division or merger of the employer, job transfers by the employer, the affiliates of the employer entering into labor contracts with the employees in rotations), when the employment contract with the new employer is terminated, the new employer shall pay the employee economic compensation or damages(if it is so obligated) by calculating both employment periods with the new employer and the former employer.

Article 4 also restrains the employer from evading payment of economic compensation. However, the employee might encounter difficulties in evidence collection. According to the general principles of law, the employee must prove the following facts:

(1) the reason why the employee terminated the labor relationship with his/her former employer and established a new labor relationship with the new employer is not attributable to the employee;

(2) the former employer was obligated, but failed, to pay economic compensation or damages;

(3) the new employer is obligated to pay economic compensation or damages;

(4) the employment periods with the former employer and the new employer; and

(5) the basic amount for the calculation of economic compensation or damages.

Due to the difficulty in employees being able to prove the facts set forth in above item (1), the allocation of burden of proof between the parties by the court will directly influence the resolution of the dispute.

In addition to the above-mentioned items, Interpretation IV is silent on the following questions:

(1) Whether or not the employee has the right to claim against his former employer for economic compensation or damages after he has claimed for economic compensation or

damages against this new employer pursuant to Article 4 of this Interpretation IV? From a legal perspective, the answer is no. Then the issue should be whether the new employer has the right to claim for a recovery against the former employer after the new employer has paid the economic compensation or damage? If yes, what standard shall be applied to calculate the amount to be recovered, since the overpaid amount by the new employer might be higher or lower than the amount ought to be paid by the former employer?

(2) Whether or not the former employer is responsible for the unpaid economic compensation or damage in the event that the employee voluntarily resigns from the new employer or the new employer duly terminates the labor relationship due to the employee's fault.

No answer to the above questions can be found in the Interpretation IV, and we expect either the legislative organs or the Supreme People's Court to promulgate new laws or judicial interpretation on the above questions.

Considering the degree of uncertainty in Interpretation IV with respect to the calculation of employment periods, we suggest that employers pay economic compensations and damages to employees in accordance with the current laws in order to avoid potential disputes that might arise in the event of company and employee resettlement. In regards to the ambiguity of the law, we recommend that employers fully communicate with their workers and conclude with written agreements in order to help guide any future disputes that may arise.

III Non-competition Compensation

Before the promulgation of Interpretation IV, the amount of non-competition compensation was mainly determined by mutual agreement between the employee and the employer, since there was no national statutory standard. Article 4 of Interpretation IV adopts a fixed standard for non-competition compensation: namely 30% of the employee's monthly salary for the 12 months prior to the revocation or termination of the labor contract or equal to the local minimum salary standard, whichever one is higher.

IV Termination of Non-competition Clauses

Article 8 of Interpretation IV provides that the employee shall have the right to claim for the termination of non-competition clauses in the event that the employer fails to pay non-competition compensation for three months due to the employer's reasons. Article 9 provides that the employer may terminate non-competition clauses at any time, provided that the employee has the right to claim for three months' additional non-competition compensation.

We understand that the employee is entitled to non-competition compensation for the period during which the employee has fulfilled his non-competition obligation, where the employee claims for termination of the non-competition clauses pursuant to Article 8 of Interpretation IV. We also gather that the termination right under Article 8 and Article 9 of Interpretation IV does not conflict with the contractual termination right. Therefore, in the event that both parties have reached an alternative agreement on the termination of non-competition clauses, such agreement should prevail.

V Effectiveness of Oral Amendments to Labor Contracts

Article 11 of Interpretation IV confirms that the oral amendment to the labor contract is effective provided that the parties have carried out the oral amendment for more than one month.

We think that Article 11 of Interpretation IV is incomplete for the following reasons:

(1) Section 1 of Article 35 of the *Labor Contract Law* explicitly prescribes that "An employer and an employee may amend the provisions of the labor contract if they reach consensus on the matter through consultation. Any additional amendments in a labor contract shall be made in writing." It can be easily found that Article 11 of Interpretation IV conflicts with the *Labor Contract Law*.

(2) Changes in the labor contract may include a wide range of content. There may be amendments to the essential clauses set forth under Article 17 of the Labor Contract Law, such as labor remuneration, scope of work, workplace, labor contract term. There may be amendments any non-essential clauses as well. Since Interpretation IV has not yet placed restrictions on the application of oral amendments, we can infer that such oral amendments may apply to both essential clauses and non-essential clauses.

(3) To allow for certain provisions of oral amendments in the labor contract may prejudice the employee's rights and interests. For example, the employer reaches an oral agreement with the employee to extend the term of the labor contract before the expiration of the term. In that case, Article 11 of Interpretation IV may preclude the employee from either claiming for dual payment of salary for the period during which there is no written labor contract pursuant to Article 82[3] of the *Labor Contract Law*, or claiming for the establishment of non-fixed term labor contract pursuant Article 14[4] of the *Labor Contract Law*.

[3] **Article 82** Where an employer fails to conclude a written labor contract with an employee for more than a month but less than a year from the date it starts employing he/she, it shall pay the employee two times his salary for each month.

Where an employer fails to conclude a non-fixed term labor contract with an employee in violation of the provisions of this Law, it shall pay the employee two times his salary for each month, starting from the date on which a non-fixed term labor contract should be concluded.

[4] **Article 14** A non-fixed term labor contract is one where the employer and the employee have agreed not to stipulate a definite ending date.

An employer and an employee may conclude a non-fixed term labor contract upon reaching consensus through consultation. If a employee proposes or agrees to renew the labor contract or to conclude a labor contract in any of the following circumstances, a non-fixed term labor contract shall be concluded, unless the employee requests the conclusion of a fixed-term labor contract:

(1) The employee has been working for the employer for a consecutive period of 10 or more years;

(2) The employee has been working for the employer for a consecutive period of 10 or more years but less than 10 years away from the statutory retirement age when the employer introduces the labor contract system or when

(4) Allowing oral amendments in the labor contract may lead to new disputes arising. For example, parties may face difficulties in proving the new term of the labor contract in case the parties reach an agreement to extend the term of the labor contract, and the parties' performance of the amended labor contract cannot prove the new term, then the people's court may also have difficulties in fact-finding.

Our above analysis has shown that despite how Interpretation IV recognizes the effectiveness of oral amendments in labor contracts, there is still the possibility of new disputes arising. Therefore, we recommend that the employers and the employees amend labor contracts in written form.

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the State-owned enterprise has to conclude a new labor contract with him as a result of restructuring; or

(3) The employee intends to renew the labor contract after he has consecutively concluded a fixed-term labor contract with the employer twice and he has not been found in any of the circumstances specified in Article 39 or Subparagraph (1) or (2) in Article 40 of this Law.

If an employer fails to conclude a written labor contract with an employee within one year as of the date when it employs the employee, it shall be deemed to have concluded a non-fixed term labor contract with the latter.

Legal Updates

1. New SAFE Circular Refines Foreign Exchange Procedures of Overseas Listing of a PRC Stock Company (Authors: Huan WANG, Jialin ZHONG)

The China Securities Regulatory Commission ("**CSRC**") promulgated the *Regulatory Guidance on Application Documents of and Review Procedures for Overseas Offering and Listing of Joint-Stock Companies* on December 20, 2012 to relax the criteria of overseas offering and listing for domestic enterprises. On January 28, 2013, the State Administration of Foreign Exchange ("**SAFE**") released the *Circular of the State Administration of Foreign Exchange on Issues Concerning Foreign Exchange Administration of Overseas Listings* (Hui Fa [2013] No.5, "**Circular 5**"), which took effect on the same date. The *Circular of the State Administration of Foreign Exchange and the China Securities Regulatory Commission on Issues Concerning Further Improving Foreign Exchange Administration of Overseas Listings* (Hui Fa [2002] No. 77, "**Circular 77**"), the *Circular of the State Administration of Foreign Exchange on Relevant Issues Regarding Improving Foreign Exchange Administration of Overseas Listings* (Hui Fa [2003] No. 108, "**Circular 108**"), the *Circular of the State Administration of Foreign Exchange on Issues Concerning Foreign Exchange Administration of Overseas Listings* (Hui Fa [2005] No.6, "**Circular 6**"), and other relevant circulars[5] previously established by SAFE were all abolished at the same time.

Circular 5 further regulates and simplifies foreign exchange registration as well as the relevant foreign exchange settlement and sales procedures involved in the overseas listing of a domestic joint-stock company ("**Domestic Company**"), the repurchase of its overseas shares by the Domestic Company itself, and the increase or decrease in overseas shareholding by domestic shareholders of the Domestic Company. In addition, Circular 5 relaxes foreign exchange regulations on overseas listed Domestic Companies to a certain extent, and makes it more convenient for Domestic Companies, especially small and medium-sized enterprises, in dealing with foreign exchange procedures involved in overseas listing. The main features of Circular 5 are as follows:

Foreign Exchange Registration Done after the First Overseas Offering

Pursuant to Circular 77, a company with foreign capital shares listed abroad ("**Foreign Capital**

[5] The *Circular of the Capital Account Management Department of the State Administration of Foreign Exchange on Issues Related to Doing a Good Job in Foreign Exchange Administration of Overseas Listings* (Hui Zi Han [2002] No.29) and the *Circular of the State Administration of Foreign Exchange on Relevant Issues related to Remitting to the National Social Security Funds the Foreign Exchange Income Gained from Overseas Reductions of Stated-owned Shares* (Hui Fa [2004] No. 64).

Shares Company"[6]) shall apply for the foreign exchange registration for overseas listed shares at a relevant SAFE office within 30 days after acquiring CSRC approval on overseas offering and listing. Circular 5 postpones the time for doing such registration. Under the new provisions, the Domestic Company shall, within 15 working days after the first overseas offering, file an application of overseas listing registration with the SAFE office located in its incorporation place. The registration shall consist of the following documents:

1) Written application, with *Overseas Listing Registration Form* enclosed;
2) Certificate issued by CSRC approving the overseas listing of the Domestic Company;
3) Announcement of the conclusion of the overseas offering; and
4) Supplemental documents, if the above-listed documents contradict each other or fail to prove the authenticity of the overseas listing.

SAFE will issue an overseas listing registration certificate ("**Overseas Listing Registration Certificate**") to the Domestic Company after reviewing and verifying the above documents. The Domestic Company shall bring the Overseas Listing Registration Certificate to open a special bank account in the bank of its incorporation place. This account shall be used for the capital remittance as well as the transfer of funds related to its initial offering (or additional issuance of shares) and repurchase of shares.

Raised Funds May be Retained Abroad

Circular 77 and Circular 6 state that the Foreign Capital Shares Company shall repatriate the raised funds within 6 months after they are raised with the related listing costs deducted. Without SAFE approval, the raised funds shall not be retained abroad.

According to Circular 5, funds raised in the overseas listing of the Domestic Company may be repatriated to the corresponding domestic special bank account or retained in the overseas special bank account. The usage of such funds shall be consistent with publicly disclosed documents such as prospectuses, shareholders' circulars, and shareholders' resolutions.

Overseas Funds can be used to Repurchase Overseas Shares

Under Circular 77, prior to the repurchase of overseas listed outstanding shares, the Foreign Capital Shares Company shall obtain CSRC approval and complete the foreign exchange registration for the changes of overseas listed shares. The Foreign Capital Shares Company shall also obtain SAFE approval for opening overseas accounts and remitting out the domestic funds.

Circular 5 simplifies the procedure and exempts CSRC and SAFE approval. When repurchasing

[6] This refers to companies registered in China and listed overseas.

its overseas shares, the Domestic Company may use overseas funds in accordance with the relevant provisions or remit out the domestic funds. With the Overseas Listing Registration Certificate specifying the relevant repurchase information, the Domestic Company may transfer funds to its domestic special bank account for repurchase and remit out such funds.

Regulates the Foreign Exchange Procedures regarding the Increase or Decrease in Overseas Shareholding by Domestic Shareholders

Circular 7, Circular 108, and Circular 6 do not mention the increase or decrease in overseas shareholding by domestic shareholders of the Foreign Capital Shares Company, while Circular 5 contains explicit provisions regarding such increase or decrease in shareholding. When a domestic shareholder of the Domestic Company proposes to increase or decrease the overseas shareholding after the Domestic Company is listed overseas, it shall file an overseas shareholding registration application with the SAFE office located in its domicile and provide the following documents:

1) Written application, with *Overseas Shareholding Registration Form* enclosed;
2) Board resolution or shareholders' resolution regarding the increase or decrease in shareholding (if needed);
3) Approvals from the relevant authorities, when approvals of the state asset management authority are required; and
4) Supplemental documents, if the above-listed documents contradict each other or fail to prove the authenticity of overseas listing.

SAFE will issue an overseas shareholding registration certificate ("**Overseas Shareholding Registration Certificate**") to domestic shareholders, which is used for increasing or decreasing shareholding in the Domestic Company.

To increase overseas shareholding in the Domestic Company, a domestic shareholder may use overseas funds in accordance with the relevant provisions or remit out the domestic funds to purchase the overseas shares. With the Overseas Shareholding Registration Certificate, a domestic shareholder may transfer funds to its domestic special bank account to increase shareholding and remit out such funds.

Capital gains under the capital account due to the decrease in shareholding in the Domestic Company, the transfer of the overseas shares of the Domestic Company, or the delisting of the Domestic Company shall be repatriated to the domestic special bank account for decreasing shareholding within 2 years after the acquisition of such gains. With the Overseas Shareholding Registration Certificate, the repatriation of such gains can be conducted in the bank directly without SAFE approval.

Relaxes Overseas Special Bank Account Regulation

Pursuant to the provisions of Circular 77, Circular 108, and Circular 6, to temporary keep the funds raised by the Foreign Capital Shares Company or the capital gained by decreasing shareholding or selling the assets or interests of listed company overseas, an application shall be filed with SAFE for opening an overseas special foreign exchange account. However, there are certain limitations and/or requirements in such an account: 1) the validity of an overseas special foreign exchange account is only 2 years; 2) Chinese banks in the place of listing shall be chosen preferentially to open the overseas bank account; and 3) Chinese banks chosen shall also issue a written commitment[7] to SAFE.

Circular 5 relaxes overseas special bank account regulations by providing the Domestic Company and its domestic shareholders need only make a filing with SAFE for the opening, changing, or closing of the overseas special bank account within 10 working days.

2. Tax Exemption for Foreign Individuals on Dividends to be Abolished (Author: Fang JI)

On February 3, 2013, the State Council approved the *Several Opinions on the Further Reform of the Income Distribution System* (the "**Opinions**") drafted by the National Development and Reform Commission, the Ministry of Finance and the Ministry of Human Resources and Social Security, and forwarded the Opinions to the provincial level governments and the ministries and commissions of the State Council. Article Fourteen of the Opinions states that the preferential treatment exempting foreign individuals from individual income tax on dividends and bonuses income obtained from foreign invested enterprises ("**FIE**") shall be abolished (the "**Proposed Reform**").

Evolution of the Relevant Tax Regulations

In the past, FIEs and their foreign investors have enjoyed "super national" tax treatments. FIEs were entitled to several preferential tax treatments that were not available to Chinese domestic enterprises. In addition, both foreign enterprise investors and foreign individual investors were permitted to acquire dividends and bonuses from FIEs free from PRC income taxes. Such "super national" tax treatments have been largely abolished since the implementation of the new *Enterprise Income Tax Law* in 2008. One of the major changes brought about by the new *Enterprise Income Tax Law* is that foreign enterprise investors become subject to a 10% withholding enterprise income tax (or such lower rate as provided in the applicable tax treaty) with respect to dividends distributed from profits accumulated on or after January 1, 2008. However,

[7] The written commitment shall consist of the followings: using the foreign exchange account in accordance the account scope of revenues and expenses and duration approved by SAFE; reporting the account opening certificate, account utilization and account cancellation certificate to SAFE within 10 working days after opening and closing the overseas account.

foreign individuals remain exempt from individual income tax on dividends received from FIEs pursuant to the *Circular of the Ministry of Finance and State Administration of Taxation on Several Policy Issues Regarding Individual Income Tax* (Caishuizi [1994] No. 020), which is currently in effect.

Following the integration of the enterprise income tax treatment for FIEs and domestic enterprises, other "super national" tax treatments for FIEs and their foreign investors have been gradually abolished. For instance, the Chinese government has started to levy a real estate tax, city construction tax, and education surcharge on FIEs and foreign enterprises in 2009 and 2010 respectively. As a result, the tax exemption treatment for foreign individuals on dividends appears to be inconsistent with the general trend to eliminate "super national" tax treatments for FIEs and foreign enterprises. Furthermore, dividends distributions, whether or not made to a foreign enterprise investor or a foreign individual investor, are the same in an economic sense. However, if such preferential tax treatment for foreign individual investors is to be maintained, the distributions would attract different tax treatments, i.e., enterprise income tax liability would arise for the foreign enterprise recipient, while individual income tax would be exempt for the foreign individual recipient. Applying different tax treatments for the same economic activity would violate the neutrality principal, which represents a fundamental principal of tax legislations. As such, abolishing the tax exemption treatments for foreign individuals who receive dividends from FIEs is a necessary consequence of the general trend to eliminate "super national" tax treatments, and will promote the establishment of a fair and neutral tax system in China.

Tax Treatments for Foreign Individuals on Dividends following the Proposed Reform

The provision in the Opinions regarding the abolishment of the preferential tax treatment that exempts foreign individuals from individual income tax on dividends and bonuses income obtained from FIEs should serve only as a guiding principle. Based on past experiences, the Ministry of Finance and/or the State Administration of Taxation will soon issue a new circular prescribing the individual income tax treatment for foreign individuals that receive dividends and bonuses income from FIEs. At the current stage, we understand that when tax is to be levied on dividends and bonuses income obtained by foreign individuals, the applicable tax rate should be 20% as pursuant to the *Individual Income Tax Law*. Foreign individuals should also be entitled to preferential tax treatments provided by applicable tax treaties.

Implications of the Proposed Reform

Capital gains derived by foreign individuals from the transfer of equity interest in FIEs are currently taxable at the flat rate of 20%. After the Proposed Reform is implemented, a direct holding structure, whereby foreign individual investors directly hold FIEs in China, would not have any tax advantages. As such, foreign individual investors may consider restructuring the investment into an indirect structure by imposing an intermediate holding company established in a jurisdiction that concluded a tax treaty (with preferential tax provisions) with China. It should however be noted that the PRC tax authorities have recently issued several tax regulations with anti-avoidance provisions targeting overseas structures. These anti-avoidance provisions address issues such as the application of tax treaty treatments and tax treatments for indirect equity transfers of Chinese companies. With these PRC tax laws and regulations, including the anti-avoidance provisions in mind, foreign individual investors should thus consider restructuring their investments in China while taking into account the possible means of obtaining investment returns as well as the future disposal of investments.

3. NDRC Punished Enterprises Outside Mainland China for Price-related Anti-competitive activities for the First Time (Authors: Joyce LI, Tracy ZHOU, Haoze LI)

On January 4, 2013, the National Development and Reform Commission of the People's Republic of China (the "**NDRC**") announced a crackdown against six leading international LCD panel manufacturers (collectively the "**Group**"), namely Samsung, LG, Chimei, AU Optronics ("**AUO**"), Chunghwa Picture Tubes ("**CPT**") and HannStar, for price-fixing cartel among them from 2001 to 2006[8]. The total penalty imposed against the Group is RMB 353 million. This case is the first enforcement action by China against price-related monopoly activities of firms outside mainland China, and the RMB 353 million penalty is also the largest penalty that China has ever imposed for price-related violations.

Background

Since December 2006, the NDRC has received a number of complaints regarding conspiracy among the Group members to manipulate prices for LCD panels and conduct price-fixing cartel in mainland China. The NDRC investigated the case accordingly.

The NDRC found that from 2001 to 2006, the Group had 53 "LCD" meetings in Taiwan and South Korea mainly to exchange information on LCD panel market and negotiate prices for LCD panels. The Group members artificially manipulated prices for LCD panels they sold in mainland China based on prices agreed on and information exchanged during the LCD meetings. The total illegal gains obtained by the Group from sale of LCD panels involved were found to be RMB 208 million.

On January 4, 2013, the NDRC announced its sanctions against the Group, including return by the Group to Chinese television enterprises overcharged prices for LCD panels in an amount of RMB 172 million, confiscation of all other illegal gains in an amount of RMB 36.75 million and payment of fines in an amount of RMB 144 million. The penalty (including return and/or confiscation of illegal

[8] For the decision of NDRC (in Chinese), please refer to: http://www.sdpc.gov.cn/xwfb/t20130104_521958.htm.

gains as well as fines) on each of Samsung, LG, Chimei, AUO, CPT and HannStar was RMB 101 million, RMB 118 million, RMB 94.41 million, RMB 21.89 million, RMB 16.20 million and RMB 0.24 million respectively. Since AUO was the first to report to the NDRC the price-fixing cartel among the Group, AUO was exempted from fines and the punishment on it was only return and confiscation of all illegal gains it obtained. Samsung was fined twice of its illegal gains, while the other four firms were each fined 50% of its illegal gains. In addition, the NDRC also ordered the Group to implement certain rectification measures, including fair treatment of all customers in respect of procurement of high-end or new technology products and commitment to extend the free repair warranty period for LCD panels used on televisions that Chinese televisions enterprises sell within the mainland China from 18 months to 36 months9.

The price-fixing cartel among the Group has also been investigated and punished in the United States (US), the European Union (EU) and South Korea. The Group was fined USD 1.215 billion in the US, EUR 648 million in the EU and KRW 194 billion in South Korea, all being much higher than the NDRC's penalty. Samsung receive full immunity from fines in all the three areas because it blew the whistle on the cartel.

Comments

There are a few points that are worth noting in this case:

(a) China strengthens enforcement against foreign companies' anti-competitive activities.

The Anti-monopoly Law of the People's Republic of China (the "AML"), which took effect on August 1, 2008, applies not only to anti-competitive activities occurred within mainland China, but also to those conducted outside mainland China but having an impact to eliminate or restrict competition within mainland China. The AML prohibited three types of monopolistic activities, which are monopoly agreements among business operators, abuse of dominant market positions, and concentrations among business operators that may eliminate or restrict competition. The NDRC and its competent local counterparts are in charge of enforcement against price-related monopoly agreements and abuse of dominant market positions, the State Administration of Industry and Commerce (the "SAIC") and its competent local counterparts are in charge of enforcement against all other monopoly agreements and abuse of dominant market positions, and the Ministry of Commerce (the "MOFCOM") is in charge of review and approval of concentrations.

Monopolistic activities occurred outside China may eliminate or restrict competition in Chinese markets. The MOFCOM has been actively involved in concentrations among foreign

9 It is reported that in addition to the price collusion, the Group also delayed supply of new products to Chinese television enterprises and provided Chinese television enterprises a much shorter warranty period for LCD panels than the 36-month warranty period provided by the Chinese television enterprises to customers.

enterprises ever since before the adoption of the AML[10]. The NDRC's latest punishment has sent a signal that Chinese anti-monopoly regulators are further strengthening supervision on and enforcement against anti-trust related violations by foreign or international companies.

(b) Price-related anti-competitive activities may be subject to huge fines.

Under the AML, competitors are forbidden from reaching monopoly agreements[11]. It is reported that since the adoption of the AML, the NDRC has investigated 49 price-related monopoly cases, among which penalties have been imposed in 20 cases. In addition, the local counterparts of the NDRC have also investigated and punished a number of price-related monopoly cases. Before the latest crackdown by the NDRC, the penalties imposed were generally not high. However, the LCD panel price-fixing cartel case indicates that price-related anti-competitive activities, whether occurred within or outside China, may be subject to huge fines in China in future.

The Group's conspiracy to manipulate prices falls within the definition of monopoly agreements that are prohibited under the AML. However, since the Group's monopoly activities occurred before the AML took effect, the NDRC decided the penalties based on the Price Law of the People's Republic of China (the "Price Law"), which took effect on May 1, 1985, instead of the AML. Both the Price Law and the AML provide for confiscation of illegal gains as penalties for business operators engaged in price-related monopoly activities. However, in respect of fines that may be imposed in addition to confiscation of illegal gains, the Price Law allows fines up to five times of illegal gains, while the AML provides for fines equal to 1% to 10% of turnovers in the last year. Since illegal gains are much lower than annual turnovers at most cases, fines imposed under the AML will normally be much higher than fines under the Price Law. According to the NDRC, if the AML were applied in this case, the fines imposed on the Group would have been much higher.

(c) A firm's cooperation with the regulator during the investigation may significantly affect the fines imposed on it.

In a price-related monopoly agreement case, the fines imposed on each participating firm will not only vary according to the amount of its illegal gains or turnovers, and its roles in the monopoly agreements, but also be significantly affected by its cooperation with the regulator during the investigation.

Investigation on monopoly agreements is complicated and collection of evidences is difficult. China, the US, the EU and South Korea all have investigated the LCD panel price-fixing cartel for more than four years. Information provided by internal participants of price-fixing cartels is

[10] The anti-monopoly review of concentrations was provided in the Interim Regulation on Acquisitions of Domestic Companies by Foreign Investors which took effect in 2003.
[11] Monopoly agreements refer to agreements, decisions or other concerted actions eliminating or restricting competition.

always the key evidence. Therefore, most regulators have adopted a leniency program, under which firms that voluntarily cooperate with regulators and provide information of monopoly agreements to regulators may receive full or partial immunity from punishment. Samsung's exemption from fines in the US, the EU and South Korea is resulting from its voluntary provision of information to regulators under the leniency program.

China has also adopted leniency program. The AML provides that for any firm who voluntarily reports information on reaching the monopoly agreement and provides important evidence, the regulators may impose a mitigated punishment or exempt it from punishment in consideration of concrete circumstances. The regulation promulgated by the NDRC further provides that the NDRC may exempt from punishment the first firm that voluntarily reports information on reaching the price-related monopoly agreement and provide significant evidence, reduce penalties by no less than 50% for the second one that reports and provides evidence, and reduce penalties by no more than 50% for the other enterprises that reports and provides evidence. The SAIC has promulgated similar rules for monopoly agreements not related to prices. However, it is worth noting that the SAIC does not apply the leniency program to organizers of monopoly agreements, while the NDRC regulations do not prohibit organizer from benefiting from filing for leniency.

In this LCD panel price-fixing cartel case, AUO's illegal gains were RMB21.89 million, ranging the fourth among all six firms, but it was exempted from fines because it was the first to report the price conspiracy during NDRC's investigation. Besides, the NDRC stated that the fines imposed on all other five firms were also reduced due to their confession. The latest punishment by NDRC and some other decisions on price-related monopoly cases published before indicate that Chinese regulators have used leniency program in practice, and successful filing for leniency by a firm may significantly reduce its penalties.

4. SARFT's New Rules: Taiwanese Films No Longer Subject to Imported Film Quota Restrictions (Authors: Tracy ZHOU, Arong)

On January 17, 2013, the State Administration of Radio, Film, and Television of the People's Republic of China ("**China**" or "**PRC**") ("**SARFT**") promulgated *the Measures on Strengthening Cooperation and Management of Cross-Strait Films《国家广电总局电影管理局关于加强海峡两岸电影合作管理的现行办法》* (the "**Measures**") to implement the commitments regarding Taiwanese access to the Mainland China film industry in the Economic Cooperation Framework Agreement ("**ECFA**"), which has been in effect since September 12, 2010.

The Measures include rules on the import of Taiwanese films, co-produced films by Mainland China and Taiwan, as well as Taiwanese investments in movie theaters. With regard to the import and co-production of films, Taiwanese investors will enjoy similar preferential treatment compared to

Hong Kong and Macau. However, regarding investments in movie theaters, Taiwanese investors shall comply with the policy applied to normal foreign investors. The details of the Measures are as follows:

Definition of Taiwanese Films

Taiwanese films refer to those films made by production entities that are set up or established in accordance with the relevant laws of Taiwan, and own more than 50% of the copyrights of the films concerned. Taiwan residents should comprise more than 50% of the total principal personnel in the films concerned.

Import of Taiwanese Films

Imported foreign films (including films produced in Hong Kong, Macau, and Taiwan) that may be exhibited in China are subject to a quota restriction, and only a limited number of foreign films are allowed to be imported and distributed per year. In addition, foreign films can only be imported by designated film importers (namely China Film Group Film Import & Export Corporation), and be distributed by designated film distributors (namely China Film Group Film Distribution & Exhibition Corporation and Huaxia Film Distribution Co., Ltd.) in China.

After the release of the Measures, Taiwanese films will be imported, approved, and distributed as foreign films, but on a quota-free basis.

Co-produced Films by Mainland China and Taiwan

Under PRC law, any organizations or individuals from abroad may not independently make films within China. Only cooperation between a foreign entity and a PRC entity in film production (including Joint Production, Co-production through synergy, and Co-production through commission) is allowed. Moreover, the employment of any foreign principal creative personnel[12] shall be approved by SARFT, and the foreign leads shall not exceed two thirds of the total number of leads. The development and post-production of the negatives and samples of a Sino-foreign jointly produced film shall be completed in China. If such development and post-production are to be completed outside China due to special technical requirements, an application shall be filed with SARFT for approval.

Pursuant to the Measures, for co-produced films by Mainland China and Taiwan, when referring to the regulations related to Sino-foreign cooperation in film production, the following rules shall apply:

(a) In regards to Joint Production films, the plots and leading characters must be related to

[12] Creative personnel refer to individuals performing the roles of director, screenwriter, cinematographer, and leads.

Mainland China or Taiwan;

(b) In regards to Joint Production films, the employment of foreign principal creative personnel shall be approved by SARFT. Except for requiring at least one third of the leads to come from Mainland China, there is no restriction on the percentage of foreign principal creative personnel;

(c) Subject to the approval of SARFT, the development and post-production of the negatives and samples of co-produced films may be completed in Taiwan, without being limited to only special technical requirements;

(d) Films co-produced by Mainland China and Taiwan are treated as domestic films for the purpose of distribution in Mainland China pursuant to the applicable PRC laws.

Taiwanese Investments in Movie Theaters

Under PRC law, foreign investments in movie exhibitions are restricted, and foreign investors may not hold more than 49% of the equity interests in any PRC movie theater company. In a Sino-foreign joint venture movie theater company established in one of the trial cities, Beijing, Shanghai, Guangzhou, Chengdu, Xi'an, Wuhan, and Nanjing, the foreign investor shall not hold more than 75% of the equity interests. Notwithstanding the foregoing, "Hong Kong and Macau service providers" may construct or renovate movie theaters for film exhibition by taking the form of joint ventures or wholly owned enterprises.

According to the Measures, Taiwanese investors that invest in movie theaters shall comply with the restrictions applied to normal foreign investors, which require the shareholding percentage of Taiwanese investors in the joint venture to not exceed 75% in trial cities and not exceed 49% in other cities.

Important Announcement

This Newsletter has been prepared for clients and professional associates of Han Kun Law Offices. Whilst every effort has been made to ensure accuracy, no responsibility can be accepted for errors and omissions, however caused. The information contained in this publication should not be relied on as legal advice and should not be regarded as a substitute for detailed advice in individual cases.

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