Courts Grapple with Novel Legal Issues Relating to Chinese Companies Sued in U.S. for Antitrust Violations

FROM THE ANTITRUST PRACTICE GROUP

As the world economy grows increasingly interconnected, plaintiffs' lawyers in the US are searching for ways to sue foreign companies in US courts for anticompetitive behavior. Several recent Sherman Act cases have been brought against consortiums of partially government owned Chinese companies alleging price-fixing activity that impacts US markets. The increasing willingness of plaintiffs' lawyers to bring US antitrust lawsuits against Chinese companies may raise the interest of the Department of Justice and lead to future cartel investigations.

Two recent cases illustrate this developing trend: In re Vitamin C Antitrust Litigation, 584 F. Supp. 2d 546 (E.D.N.Y. 2008) (hereinafter "Vitamin C") and Animal Science Products, Inc. v. China National Metals & Minerals Import & Export Corp. et al., Civ. No. 05-4376 (GEB) (D.N.J. Dec. 30, 2008) (hereinafter "Magnesite"). Rulings of the federal district courts in New Jersey and the Eastern District of New York demonstrate the challenges faced by those bringing these types of claims, but also underscore that Chinese companies may face exposure in US courts. Plaintiffs’ lawyers will take heart that in neither case did the federal court summarily dismiss the complaint.

Vitamin C Case

This case arose from the growing dominance of Chinese companies in the market for vitamin C products. In response, a number of U.S.-based vitamin C manufacturers filed lawsuits against their Chinese competitors alleging Sherman Act violations through the manipulation of vitamin C prices. The complaints alleged that the Chinese defendants formed a cartel in December 2001 aimed at controlling prices and the export volume of vitamin C in the world market. The purported cartel was formed during meetings of the Western Medicine Department of the Association of Importers and Exporters of Medicines and Health Products of China, a form of trade association, and continued to meet under its auspices. By December 2002, the price of vitamin C had jumped from $2.50 to $7.00 per kilogram, with Chinese manufacturers controlling 60 percent of the global market supply.

Supported by a brief filed by the Chinese Ministry of Commerce ("MOFCOM") (the first-ever appearance by the Chinese government in an amicus role in a US antitrust case), the defendants sought dismissal on the basis of act of state, foreign sovereign compulsion, and international comity doctrines. The defendants argued that the activities of the producers were compelled by the Chinese government, which required the producers to coordinate prices in
order to comply with governmental directives and to avoid exposure to US antidumping proceedings alleging Chinese prices were too low. The MOFCOM *amicus* brief stated that the Chinese government supervised the joint conduct of the companies as part of its effort to “play a central role in China’s shift from a command economy to a market economy.”

Despite precedent that supported dismissal of antitrust suits based on the involvement of foreign governments in anti-competitive activities, the federal court in Brooklyn held that the “complex interplay” between public and private action in this particular case precluded dismissal at this stage. The court evaluated whether the Chinese cartel acted like a Western-style private trade association, or more like a public central-planning governmental entity, in order to determine whether antitrust liability may attach to its activities. At the early stage in the case, the court adopted a “wait-and-see” attitude, deferring the issue until the assembly of a more complete record through discovery to assist in its decision.

**Magnesite Case**

The New Jersey federal court took a somewhat different approach in a decision issued in late December. In *Magnesite*, the complaint alleged that thirteen Chinese magnesite producers and exporters formed the “Jiayuan Magnesite Export Group” in April 2000, a cartel that fixed magnesite export prices. A second, similar cartel purportedly was formed around the same time. The two cartels allegedly accounted for more than 70 percent of the export volume of magnesite in China. The complaint asserted that as a result of the actions of these groups, the price of magnesite products increased by more than 45% in 2000, resulting in $50 million in additional revenue for the participating companies by mid-2001. The complaint alleged that the two cartels subsequently merged under the name “Chinese Magnesite Export Association,” eventually growing to dominate the world magnesite market. These efforts were alleged to violate both the Sherman Act, with the court enabled to hear the claims by the Foreign Trade Antitrust Improvements Act (FTAIA).

The Chinese government did not file a supporting brief in *Magnesite*, but the court’s opinion acknowledged the principles of comity and sovereign action that can arise in the context of cases involving Chinese companies. The complaint alleged that two of the Chinese defendant companies were state-owned entities, while the others were labeled vaguely as “Chinese trading companies” or “Chinese corporations.” The court said the complaint left it unclear whether the companies were state-owned entities, privatized entities still subject to state control, companies operating outside any Chinese regulatory constraints, or any combination of the three. The court elected not to delve into these questions in the context of a threshold motion to dismiss, given the lack of clarity in the complaint. For purposes of the motion, the court assumed that the legal and operational status of the Chinese companies did not implicate any of the doctrines relating to the action of a foreign sovereign.

Having sidestepped these complex issues, the court moved on to dismiss the *Magnesite* complaint upon concluding that it lacked subject matter jurisdiction, finding that the complaint as drafted failed to allege that any of the processed magnesite was brought into the US. The court reacted with skepticism to the data pled in the complaint, and undertook its own independent analysis of the magnesite market. The opinion, replete with statistics taken from US Customs data and other official sources, identified a number of apparent factual errors in the complaint. Furthermore, the court found no connection between defendants’ alleged actions and US commerce, dismissing the factual assertions in the complaint as “baseless conjecture.”

The court warned plaintiffs that any amended complaint would need to include sufficiently detailed facts to satisfy the court that it had
subject matter jurisdiction, again indicating skepticism that a new complaint was likely to do so. The court advised that the Chinese defendants should assert challenges based on subject matter jurisdiction and on doctrines that would shield the challenged practices as actions of a foreign sovereign or as compelled by Chinese regulatory requirements.

**Evaluation**

These two decisions represent a mixed bag for both US antitrust plaintiffs and Chinese state-owned companies. In *Vitamin C*, the court was not persuaded that the mere assertion of the unique interplay between the Chinese government and industry segments provided a basis for preventing application of the Sherman Act to Chinese companies in the US. It permitted the case to go forward, leaving the foreign sovereign and government compulsion defenses to later factual development. In *Magnesite*, by contrast, the court appeared receptive to international comity and sovereign act considerations, though it avoided reaching them by finding the complaint’s factual allegations insufficient to state a cognizable claim for the US courts.

Perhaps more important, these cases illustrate a coming trend of US plaintiffs suing Chinese companies for antitrust remedies – including the treble damages remedy that motivates much US antitrust litigation. It is widely known that Chinese market shares have increased dramatically over the past several years, as China’s export industries have geared up. It has been less widely known, at least until recent years, that Chinese industry chambers play a major role in export trade, and that Chinese industry and governmental bodies have responded to the wave of US antidumping remedies by attempting to avoid unduly low pricing. The *Magnesite* complaint, for example, points to internal minutes of an industry meeting that appear to reflect coordination of pricing for products going into the US market.

The antitrust plaintiffs’ bar certainly will take heed of these recent decisions in framing future complaints. The *Vitamin C* case suggests that antitrust complaints will not be rejected in the opening rounds on the basis of MOFCOM or other governmental roles related to US pricing, and will leave that topic to discovery and factual development. That will encourage new antitrust complaints against Chinese producers. The *Magnesite* case will teach the plaintiffs’ bar that surviving the threshold motions is not automatic, and that some elbow grease will need to be applied in framing the complaint so that a clear and direct impact on the US market will appear on the face of the complaint.

In addition, a focus on Chinese companies in civil antitrust litigation may foreshadow a rise in interest of the US Department of Justice in the practices of Chinese companies that together combine to have a significant impact on US market sectors. In many antitrust cases over the past decade, the civil plaintiffs’ bar has both eagerly followed – and directly enticed – investigations by the Department of Justice, knowing that the fruits of Justice Department investigations can create huge leverage for plaintiffs in civil antitrust class actions. Plaintiffs’ lawyers will point to the *Vitamin C* and *Magnesite* cases as examples that warrant broad suspicion by government antitrust enforcers on pricing of Chinese products in US markets.

As privatization of Chinese industry grows, and as Chinese dominance in certain industries increases, their actions will increasingly fall under scrutiny of the US legal system. Chinese pricing conduct has already been subjected to repeated investigation in the context of antidumping actions that allege that Chinese prices are too low and thereby compete unfairly against US producers. Now we are seeing the leading edge of a wave of antitrust cases in which the claim will be that Chinese pricing has been artificially high due to collusion by Chinese producers.
Those cases will test the extent to which Chinese pricing actions have been guided by government authorities eager to avoid expanded antidumping exposure, by industry chambers eager to coordinate expansion of US market shares of member producers, or by export groups aiming for increased profits from old-fashioned price-fixing. They will also test the extent to which the government compulsion and state action defenses will prove useful to exporters operating in the Chinese system.

Chinese companies work hard to gain access to the biggest market in the world. They may be taking on more than they bargained for, as they learn the complexity, expense, and burden of defending US antitrust litigation that often follows US market success.

If you have any questions concerning these developing issues, please do not hesitate to contact any of the following Paul Hastings lawyers:

**Washington, D.C.**
- Kirby Behre
  - 202-551-1719
  - kirbybehre@paulhastings.com
- Michael P. A. Cohen
  - 202-551-1880
  - michaelcohen@paulhastings.com
- Kelly DeMarchis
  - 202-551-1828
  - kellydemarchis@paulhastings.com

**San Francisco**
- Jeremy Evans
  - 202-551-1755
  - jeremyevans@paulhastings.com
- Hamilton Loeb
  - 202-551-1711
  - hamiltonloeb@paulhastings.com
- Kristen Warden
  - 202-551-1869
  - kristenwarden@paulhastings.com

---

StayCurrent is published solely for the interests of friends and clients of Paul, Hastings, Janofsky & Walker LLP and should in no way be relied upon or construed as legal advice. The views expressed in this publication reflect those of the authors and not necessarily the views of Paul Hastings. For specific information on recent developments or particular factual situations, the opinion of legal counsel should be sought. These materials may be considered ATTORNEY ADVERTISING in some jurisdictions. Paul Hastings is a limited liability partnership. Copyright © 2009 Paul, Hastings, Janofsky & Walker LLP.

IRS Circular 230 Disclosure: As required by U.S. Treasury Regulations governing tax practice, you are hereby advised that any written tax advice contained herein or attached was not written or intended to be used (and cannot be used) by any taxpayer for the purpose of avoiding penalties that may be imposed under the U.S. Internal Revenue Code.