M&A under China's Anti-Monopoly Law: Update

Yee Wah Chin
Ingram, Yuzek, Gainen, Carroll & Bertolotti, LLP
Victoria University of Wellington Law School
ywchin@alum.mit.edu

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In the 18 months since the writer's review of emerging patterns in merger control under China's Anti-Monopoly Law,[1] its Ministry of Commerce has reviewed another 230+ notified transactions and issued 5 decisions. These 5 decisions, plus the unconditional clearance of other transactions, reveal MOFCOM's rapidly increasing sophistication in analyzing the competition implications of transactions, as well as its continued delicate balancing of competition factors with other considerations. The decisions may also reflect the natural conservatism when acting in what is for China still fairly uncharted territory. They confirm that China is a major competition law hurdle for cross-border transactions, sometimes surpassing the United States and the European Union. This article reviews developments in merger control under the AML since August 2010, and discusses what they reveal and their implications for cross-border transactions.

Regulations

MOFCOM has continued to develop the enforcement infrastructure for merger control by issuing regulations.[2] It issued interim provisions regarding the assessment of the competitive impact of concentrations,[3] and interim provisions

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[1] Yee Wah Chin, "Mergers & Acquisitions Under China's Anti-Monopoly Law: Emerging Patterns," Business Law Today (ABA Section of Business Law, September 2010).

[2] MOFCOM, together with the National Development and Reform Commission and the State Administration for Industry and Commerce, also continued to develop relationships with other competition enforcement authorities. On July 27, 2011, the 3 anti-monopoly enforcement authorities entered into a Memorandum of Understanding with the Department of Justice and the Federal Trade Commission to cooperate on antitrust matters. http://ftc.gov/os/2011/07/110726mou-english.pdf. In November 2011 MOFCOM and the 2 U.S. enforcement agencies issued guidance on their cooperation in merger reviews under the MOU. http://www.justice.gov/atr/public/international/docs/277772.pdf.

[3] MOFCOM Notice No. 55 (2011) http://www.mofcom.gov.cn/aarticle/b/c/201109/20110907723440.html (in Chinese) (visited February 16, 2012).

regarding the handling of notifiable transactions that were not notified,[4] and announced that regulations will be introduced in 2012 regarding merger remedies, and review of the competitive impact of unnotifiable transactions. MOFCOM is also revising the notification form and studying how to streamline the review of its rapidly growing docket, especially for transactions that clearly have little competitive impact.[5] In addition, MOFCOM released a regulation regarding national security review of mergers and acquisitions of domestic enterprises by foreign investors,[6] implementing AML Article 31 providing for separate review of transactions with potential national security implications and the State Council Notice on the establishment of a national security review system for acquisitions of domestic enterprises by foreign investors[7].

Statistics

In 2011 through mid December,[8] MOFCOM received 194 notifications, an increase of 43% from 2010, accepted 179 notifications, an increase of 52%, and completed reviews of 160 transactions, an increase of 40%. It unconditionally approved 151 transactions and imposed conditions on 4. Notifications for 5 transactions were withdrawn after acceptance. MOFCOM's docket has more than doubled in size since 2009.

Table 1 sets forth the review time lines for the 12 transactions in which decisions have been issued since the AML became effective, along with those of several high profile transactions that were approved unconditionally.

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[4] MOFCOM Notice No. 6 (2011) http://www.mofcom.gov.cn/aarticle/b/c/201201/20120107914884.html?2850521225=840603354 (in Chinese) (visited February 17, 2012).

[5] Press conference transcript, December 27, 2011 http://www.mofcom.gov.cn/aarticle/ae/slfw/201112/20111207901483.html (in Chinese) (visited February 16, 2012).

[6] MOFCOM Notice No. 53 (2011) http://www.mofcom.gov.cn/aarticle/b/c/201108/20110807713530.html (in Chinese) (visited February 19, 2012).

[7] State Council Notice No. 6 (2011) http://www.gov.cn/zwgk/2011-02/12/content_1802467.htm (in Chinese) (visited February 16, 2012).

[8] Press conference transcript, December 27, 2011 http://www.mofcom.gov.cn/aarticle/ae/slfw/201112/20111207901483.html (in Chinese) (visited February 16, 2012).

Table 1 Notification review timelines

	Submitted	Accepted	2d Phase	3d Phase	Decision
InBev/Anheuser-Busch	9/10/08	10/27/08	--	--	11/18/08
Coca-Cola/Huiyuan	9/18/08	11/20/08	12/20/08	--	3/18/09
Mitsubishi Rayon/Lucite	12/22/08	1/20/09	2/20/09	--	4/24/09
GM/Delphi	8/18/09	8/31/09	--	--	9/28/09
Pfizer/Wyeth	6/9/09	6/15/09	7/15/09	--	9/29/09
Panasonic/Sanyo	1/21/09	5/4/09	6/3/09	9/3/09	10/30/09
HP/3Com	12/4/09	12/28/09	1/27/10	--	4/7/10*
Novartis/Alcon	4/20/10	4/20/10	5/17/10	--	8/13/10
Uralkali/Silvinit	3/14/11	3/14/11	4/12/11	--	6/2/11
NXP/Dover	12/30/10	~2/18/11	~3/21/11	--	6/14/11*
Alpha V/Savio	7/14/11	9/5/11	9/30/11	--	10/31/11
Yum!/Little Sheep	6/15/11	6/27/11	7/27/11	10/25/11	11/7/11*
GE-Shenhua JV	4/13/11	5/16/11	6/15/11	9/13/11	11/10/11
Nestlé/Hsu Fu Chi	7/14/11	9/21/11	10/21/11	--	12/6/11*
Seagate/Samsung	5/19/11	6/13/11	7/13/11	10/11/11	12/12/11
Tiande-Henkel JV	8/8/11	9/26/11	10/25/11	1/19/12	2/9/12

* No decision was published as it was an unconditional approval.

Two factors may be noted from these statistics. First, MOFCOM has thus far imposed conditions on or prohibited about 3% of notified transactions.[9] In comparison, the European Commission imposed remedies in or prohibited about 5% of notified transactions.[10] In the U.S., the Department of Justice and the Federal Trade Commission together challenged around 3.5% of notified transactions.[11] While the percentage of notified transactions that have been subject to conditions or prohibitions under the AML is lower than in the EU or

[9] Ministry of Commerce press release, http://www.gov.cn/jrzg/2012-01/10/content_2041384.htm (in Chinese) (visited February 15, 2012).

[10] http://ec.europa.eu/competition/mergers/statistics.pdf (visited February 15, 2012).

[11] Federal Trade Commission and Department of Justice Hart-Scott-Rodino Annual Report Fiscal Year 2010, pp. 1-2 http://ftc.gov/os/2011/02/1101hsrreport.pdf (visited February 15, 2012).

U.S., that may be more the result of the relatively low thresholds for notification than a "lenient" approach to merger control.[12] In fact, MOFCOM may be distinguished by having imposed conditions on transactions that other major competition law jurisdictions cleared unconditionally.

Second, MOFCOM continues to achieve greater flexibility in the time line for review than is apparent from the AML. In 4 of the 5 transactions since 2010 for which decisions were issued, there was a delay in the acceptance of the notification, triggering the start of the Phase 1 30-day review period, of between 25 and 53 days. Thus, MOFCOM might be said to have doubled the length of Phase 1 in those cases. Moreover, in several high profile transactions where the review timeline is known, there were also delays between submission and acceptance of notifications.[13] While the additional information sought during these "pre-acceptance" periods may have facilitated MOFCOM's review, it would seem that the information requirements for notifications would benefit from clarification when such supplemental information submissions are routine before a notification is accepted. Clarification would provide guidance to parties and their counsel so that the notifications will be complete when first submitted.

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[12] Notification generally is required under the AML if (1) the total worldwide turnover of all parties in the previous fiscal year exceeds RMB 10 billion (approximately $1.5 billion), and the PRC turnover of at least 2 parties exceeds RMB 400 million (approximately $62 million), or (2) the total PRC turnover of all parties in the previous fiscal year exceeds RMB 2 billion (approximately $314 million) and the PRC turnover of at least 2 of the parties exceeds RMB 400 million. State Council Rule on the Notification Thresholds for Concentration of Undertakings, Decree No. 529 (August 3, 2008). Effective, February 27, 2012, the U.S. thresholds for notifiable transactions are (1) size-of-transaction $68.2 million with size-of-persons $13.6 million and $136.4 million, and (2) size-of transaction $272.8 million. 77 Fed. Reg. 4323 (January 27, 2012). Generally, transactions must be notified to the EC if (1) the aggregate worldwide turnover of all the parties exceeds €5000 million and the aggregate Community-wide turnover of each of at least 2 of the parties exceeds €250 million, unless each of the parties achieves over 2/3 of its aggregate Community wide turnover within one and the same Member State, or (2) the aggregate worldwide turnover of all the parties exceeds €2500 million, in each of at least 3 Member States the combined aggregate turnover of all the parties exceeds €100 million, in each of at least 3 of those Member States the aggregate turnover of each of at least 2 of the parties exceeds €25 million, and the aggregate Community-wide turnover of each of at least 2 of the parties exceed €100 million, unless each of the parties achieves more than 2/3 of its aggregate Community-wide turnover within one and the same Member State. Council Regulation (EC) No. 139/2004.

[13] In addition to the transactions listed in Table 1, there were at least 2 other publicized transactions which appear likely to have had delays in the acceptance of notifications. The Diageo acquisition of control of Sichuan Chendu Quanxing Group was announced in March 2010, and cleared by MOFCOM in June 2011. The Caterpillar acquisition of Bucyrus was announced in November 2010 and cleared by MOFCOM in July 2011. It was cleared in May 2011 in the U.S. after a second request and the EU.

Beyond the published data, it appears from anecdotal information that the majority of AML notified transactions go beyond the 30-day Phase 1 review into Phase 2. In fact, the percentage of transactions going into Phase 2 has been growing.[14] In contrast, in the U.S., historically, fewer than 4.5% of transactions notified under the Hart-Scott-Rodino Antitrust Improvements Act are subject to a "second request", extending the initial 30-day waiting period until after the parties have complied with the additional request for information.[15] Moreover, in the U.S., requests for early termination of the waiting period are made in 84% of notifications, and most of the requests are granted.[16]

These aspects of the merger review process may reflect MOFCOM's limited resources for merger review, and the newness of the law. With a rapidly growing volume of notifications and a small staff responsible for enforcement of a law which still represents much uncharted territory, it is perhaps to be expected that more time is needed to review notifications than the 30-day allotted in Phase 1. MOFCOM may have achieved flexibility and thoroughness of review by obtaining additional information and time before beginning Phase 1, and entering Phase 2, in the majority of cases. It is clear that MOFCOM is sensitive to the need to streamline its process, and the facts that its review process is often longer than that in other jurisdictions and it more often enters into extended investigations.[17]

The Dog that Didn't Bark

Diageo's acquisition of control of Sichuan Chendu Quanxing Group is noteworthy because it may reflect MOFCOM's subtle accommodation of non-competition factors in its merger reviews. The transaction was approved unconditionally even though it resulted in Diageo controlling the high-end Shui Jing Fang brand of baijiu, white spirit. The deal was announced in March 2010, and cleared over a year later, in June 2011. In the interim, there was much speculation over whether MOFCOM would clear the transaction in light of its 2009 prohibition of Coca-Cola's acquisition of Huiyuan, a major Chinese brand.

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[14] Press conference transcript, December 27, 2011 http://www.mofcom.gov.cn/aarticle/ae/slfw/201112/20111207901483.html (in Chinese) (visited February 16, 2012).

[15] Federal Trade Commission and Department of Justice Hart-Scott-Rodino Annual Report Fiscal Year 2010, App. A http://ftc.gov/os/2011/02/1101hsrreport.pdf.

[16] Federal Trade Commission and Department of Justice Hart-Scott-Rodino Annual Report Fiscal Year 2010, App. A http://ftc.gov/os/2011/02/1101hsrreport.pdf.

[17] Press conference transcript, December 27, 2011 http://www.mofcom.gov.cn/aarticle/ae/slfw/201112/20111207901483.html (in Chinese) (visited February 16, 2012).

In March 2011, Sichuan Swellfun, which was controlled by Sichuan Chendu Quanxing and also owned the more famous Quanxing baijiu brand, sold it. The AML notification for Diageo's acquisition may have been submitted after the Quanxing divestiture, and enabled the acquisition to be approved unconditionally.[18] Diageo was permitted to acquire control of arguably the lesser of two brands controlled by Sichuan Chendu Quanxing.

MOFCOM may have achieved its goals in Diageo/Sichuan Chendu Quanxing without reference to the Provisions on M&A of a Domestic Enterprise by Foreign Investors, which provide for special scrutiny of transfers of control of domestic businesses that own famous or venerable Chinese brands. This is consistent with MOFCOM's prohibition of Coca-Cola's Huiyuan acquisition and conditions on InBev's acquisition of Anheuser-Busch. Both deals involved major Chinese brands which attracted much attention and public concern, yet MOFCOM's decisions in both cases protected the Chinese brands from foreign control and made no reference to the Foreign M&A Provisions. MOFCOM's treatment of Diageo's acquisition might also be consistent with the apparent pocket vetoes earlier of Sina.com's proposed acquisition of an interest in Focus Media and General Motor's proposed sale of its Hummer division by Sichuan Tengzhong Heavy Industrial Machinery, where MOFCOM apparently effectively prohibited the deals by never accepting any proffered notification. In all these cases, non-competition law policies, such as industrial policy and nationalism, may have been served *sub silentio*.[19] A similar dynamic may have been involved in Diageo.

The later unconditional clearances of Yum!'s acquisition of Little Sheep and Nestlé's acquisition of Hsu Fu Chi may offer some further encouragement that acquisitions of even major Chinese brands may be permitted, but the fact that the Little Sheep transaction went into Phase 3 before being cleared unconditionally and the apparent process for Diageo's acquisition of the Shui Jing Fang brand suggest that there likely continues to be sensitivity about acquisitions by foreign entities of Chinese brands.

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[18] "Beijing did not force the company to divest itself of that brand, but 'it was reasonably clear it had to be done', according to Edward Radcliffe, a partner at Vermilion, the lead adviser on the transaction." Diageo deal shows China thirst for investment, Financial Times, June 28, 2011 http://www.ft.com/intl/cms/s/0/31a00704-a1b8-11e0-b9f9-00144feabdc0.html (visited February 15, 2012).

[19] Yee Wah Chin, "Mergers & Acquisitions Under China's Anti-Monopoly Law: Emerging Patterns," Business Law Today (ABA Section of Business Law, September 2010).

On the Record

MOFCOM's handling of anti-monopoly matters reflected in its published decisions has become increasingly sophisticated. Its Uralkali/Silvinit decision appears to be consistent with earlier patterns, while its Alpha V/Savio decision is both more detailed and sophisticated than its earlier announced decisions. The decision in the GE-Shenhua joint venture is noteworthy as involving a state-owned enterprise, a joint venture, and a technology market. The economic analysis in MOFCOM's Seagate/Samsung decision is significantly more detailed than in earlier decisions. The result in the Tiande-Henkel joint venture possibly reflects a conservative approach to the potential competitive impact of a vertical integration. Overall, the decisions also reflect a continuing focus on the impact of transactions on Chinese businesses.

Uralkali/Silvinit[20]

Uralkali, a major potash, or potassium chloride, producer based in Russia, proposed to acquire Uralkali, another Russian potash producer. Potash is a key fertilizer ingredient and China is one of the largest potash consuming nations, with growing demand that is about 50% satisfied by imports.

MOFCOM found that the relevant product market is potassium chloride, a major form of potassium fertilizer as well as a key ingredient in other types of fertilizer, and considered the global and domestic market for potassium chloride, including imports into China. The production of potassium chloride depends on the availability of potassium. The majority of known potassium reserves are located in 3 countries, with production and sale of potassium chloride concentrated in a few companies. MOFCOM found that the Uralkali/Silvinit combination would be the world's second largest potassium chloride exporter, accounting for over 1/3 of global exports. The combination, together with the largest supplier, would account for approximately 70% of world potassium chloride supply. About half of China's potassium chloride imports are from Uralkali, Silvinit and their affiliates, with about 1/3 of China's potassium chloride imports being border trades with Uralkali and Silvinit. MOFCOM found high barriers to entry to the potassium chloride market, since known reserves are concentrated in existing producers and developing or expanding mines require substantial resources, with substantial risks.

[20] MOFCOM Announcement [2011] No. 33 regarding the Anti-Monopoly Review Decision for Conditional Clearance of the Combination of Joint Stock Company Uralkali with Joint Stock Company Silvinit http://fldj.mofcom.gov.cn/aarticle/zcfb/201106/20110607583288.html (in Chinese) (visited February 17, 2012).

MOFCOM concluded that the transaction would increase concentration in the relevant market and may adversely affect competition in international trade of potassium chloride, as well as raise the likelihood of coordinated anti-competitive conduct by potassium chloride suppliers. Apparently distinguishing a geographic market of border trades (versus ocean shipping) of potassium chloride, it concluded that the combination of Uralkali and Silvinit may exclude or restrict competition in border trades of potassium chloride. Notably, MOFCOM concluded that, in light of China's reliance on potassium chloride imports and the current potassium chloride market structure, the transaction would affect China's agriculture and other relevant industries.

In order to mitigate the adverse impact on competition in the Chinese market for potassium chloride, MOFCOM approved the transaction on conditions that Uralkali/Silvinit:

1. Maintain current sales practices, and continue to sell potassium chloride directly to the Chinese market and to use its utmost best efforts to provide reliable and stable supplies of potassium chloride to China by rail and sea.

2. Continue to supply a full line of potassium chloride products in sufficient quantities to the Chinese market, including KCl products with 60% and 62% potassium oxide (encompassing white potassium [chloride] and pink/red potassium [chloride]), as well to supply its Chinese customers, satisfying the volume and types of their needs for all uses.

3. Continue its customary negotiation processes, fully factoring in the history of dealings with Chinese customers and current circumstances as well as the special characteristics of the Chinese market in price negotiations, which include spot sales and contract sales.

4. Report semi-annually or as MOFCOM requests on compliance with the decision, and appoint a monitoring trustee to supervise performance of the obligations.

MOFCOM will inspect, monitor and oversee compliance with the conditions, and may penalize non-compliance.

Uralkali/Silvinit is a transaction with worldwide impact, but MOFCOM was the only competition law enforcer that imposed conditions. This appears to be the first decision involving a transaction with parties whose primary presence in

China is sales into China. The decision reflects understandable concern with assuring secure supply of what might be considered a strategic resource. On the other hand, the conditions imposed would seem to handicap what would be the second largest supplier, leaving the largest supplier possibly at a greater competitive advantage, which would appear to be antithetical to the goals of competition law. From the enforcement perspective, the general language of the decision provides MOFCOM with great discretion in determining compliance.

Alpha V/Savio[21]

Alpha Private Equity Fund V, a French private equity fund and the largest shareholder in Uster Technologies Co., Ltd, with a 27.9% equity position, sought to acquire Savio Macchine Tessili s.p.a through a newly created subsidiary Penelope Co. Ltd. Savio is the parent of Loepfe Bros. Ltd. Uster, a public Swiss company, and Loepfe are the only 2 manufacturers in the world of electronic yarn clearers for automatic winders, accounting for 52.3% and 47.7%, respectively, of the world and Chinese markets. An electronic yarn clearer detects and repairs yarn defects at high speed during the manufacturing process. MOFCOM determined that electronic yarn clearers for automatic winders is a distinct relevant market.

MOFCOM found that intellectual property rights is a significant barrier to entry into electronic yarn clearers for automatic winders. Moreover, economies of scale are important and difficult to achieve quickly for new entrants. There have been no successful new entrants in the last 3 years, although there were efforts in 2009 to introduce new electronic yarn clearers that had gained little customer acceptance by 2010.

MOFCOM focused on the control that Alpha V might exert on Uster, and investigated Uster's shareholders' holdings, shareholder voting rights, historic attendance at shareholders meetings, board composition and governance. It concluded that there was a possibility of Alpha V influencing Uster's operations. MOFCOM found that the transaction is likely to result in Uster and Loepfe coordinating through Alpha V and Alpha V restricting or eliminating competition through its control and influence over Uster and Loepfe. Therefore, MOFCOM

[21] MOFCOM Announcement [2011] No. 73 regarding anti-monopoly review decision granting conditional approval of the acquisition by Penelope Company Ltd of Savio Macchine Tessili s.p.a http://fldj.mofcom.gov.cn/aarticle/zcfb/201111/20111107809156.html?149782665=840603354 (in Chinese) (visited February 17, 2012).

concluded that the transaction would or may restrict or eliminate competition in the market for electronic yarn clearers for automatic winders.

MOFCOM conditioned approval of the acquisition of Savio on the divestiture within 6 months of the 27.9% holding in Uster. A monitoring trustee is to supervise the divestiture pursuant to the Provisional Regulations regarding Divestitures in Concentrations and the buyer, price and date for the sale is to be reported to MOFCOM. In the meantime, Alpha V and its ultimate parent may not participate in or influence Uster's management. MOFCOM may monitor and audit compliance with the conditions.

Alpha V/Savio is distinguished by the depth into which MOFCOM considered Alpha V's minority interest in Uster. It is rare that a minority interest without any special rights would trigger a divestiture requirement to resolve competitive impact concerns. It again is a situation in which no other competition authority imposed any conditions.[22] It may reflect a conservatism on the part of MOFCOM due to its relative inexperience with merger control, particularly in the context of private equity funds and minority holdings which is an area that far more mature competition law jurisdictions have grappled with. There may also be concerns similar to that apparently motivating the decision in Uralkali/Silvinit, to ensure a necessary input to an important sector of China's economy.

GE-Shenhua[23]

The GE-Shenhua Joint Venture was established by General Electric (China) Co., Ltd. and China Shenhua Coal to Liquid and Chemical Co. Ltd, a subsidiary of the state-owned Shenhua Group Corporation Limited, to develop a coal-water slurry gasification technology and a licensing program for the technology in China. The technology transforms coal into a coal-water slurry and then into a mixture of gasses. GE would license its coal-water slurry gasification technology to the JV while CSCLC contributes its expertise in coal gasification and coal-fired power generation. The formation of the JV was announced in January 2011 during President Hu Jintao's visit to the United States.[24] A notification under the AML

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[22] The transaction may not have been subject to notification in any other jurisdiction.

[23] MOFCOM Announcement [2011] No. 74 regarding the Anti-Monopoly Review Decision for Conditional Clearance of Contemplated Joint Venture between General Electric (China) Co., Ltd and China Shenhua Coal to Liquid and Chemical Co., Ltd. http://fldj.mofcom.gov.cn/aarticle/zcfb/201111/20111107824342.html?1104118153=840603354 (in Chinese) (visited February 16, 2012).

[24] GE Press Release, January 18, 2011 http://www.genewscenter.com/Press-Releases/GE-and-Shenhua-Announce-Formation-of-Cleaner-Coal-Technology-Joint-Venture-in-China-2ddd.aspx.

was submitted to MOFCOM on April 13, 2011, and was accepted on May 16 after supplementation. MOFCOM's review went into Phase 3 before a decision was issued on November 10, 2011.

MOFCOM found that coal-water slurry gasification technology is significantly different from other coal gasification technologies in its requirements for raw materials and methods. The Shenhua Group, which includes CSCLS, is the largest supplier in China of the type of coal suitable for coal-water slurry gasification. MOFCOM also found that domestic customers for the technology sourced the technology only from suppliers within China. There are only 3 major suppliers of the technology in China, with GE holding the largest market share, and the other 2 being Chinese entities. Entry barriers are high for other coal-water slurry technology, since it is complex and requires substantial engineering expertise to master, so that there are significant commercial risks for new technologies. It is an area covered by many patents that requires substantial start up time and investment. A new technology would generally need to find a user that is willing to underwrite some of the costs of the prototype. As a result, a new technology faces significant challenges in being licensed.

Therefore, MOFCOM concluded that the JV is likely to restrict or eliminate competition in the licensing of coal-water slurry gasification technology in China, being a combination of the largest supplier of raw coal for coal-water slurry gasification and the largest supplier of coal slurry gasification technology. It found that the JV may leverage Shenhua's position in raw coal and control its supply.

As conditions for approving the formation of the JV, GE China and CSCLC are prohibited from forcing technology customers to use the JV's technology or raising the costs of using other technologies, by restricting the supply of raw coal for use with coal-water slurry gasification technology or by conditioning the license of the JV's technology on the supply of raw coal. MOFCOM would monitor compliance with the restriction.

MOFCOM's decision is significant because it is the first involving a SOE and a JV. The facts that the GE-Shenhua JV was announced by China's President and involved a SOE, but still went into Phase 3, may reflect MOFCOM's assertion of independence from non-competition considerations in its merger reviews. Together with the ongoing NDRC investigation of state-owned China Telecom and China Unicom, the GE-Shenhua result removes some doubt regarding the applicability of the AML to SOEs. The decision also makes it clear that the merger control provisions of the AML cover JVs. The identification of a

technology licensing market as the relevant market further confirms that intellectual property is integral to MOFCOM's analyses.

The analysis of the competitive impact of the JV echo monopoly leveraging concerns stated in earlier decisions. The JV appears to be a complementary one, of GE's industrial gasification technology and Shenhua's coal gasification and coal-fired power generation expertise. MOFCOM concern derives from the vertical relationship between the Shenhua Group, with its control of raw materials, and the JV with technology that processes those raw materials. While MOFCOM noted that Shenhua is the largest supplier of raw coal for use in coal-water slurry gasification, without information as to the size of other suppliers, it's unclear that Shenhua's market position in raw coal is so large as to raise concerns under U.S. antitrust standards about exclusion of downstream competitors to the JV's technology or raising the costs of using downstream competing technology. On the other hand, Shenhua's status as a SOE, which was not highlighted in the decision, may more than bolster any lack of market power from its market share. MOFCOM's decision may be recognition of this market reality while expressing the concerns in conventional antitrust terms.

Seagate/Samsung[25]

MOFCOM's decision conditionally approving Seagate's acquisition of Samsung's hard disk drive business is by far its longest and most detailed to date, reflecting a considerable amount of economic analysis. In contrast, both the EU and the U.S. enforcement authorities cleared the transaction unconditionally.

MOFCOM found that HDDs are distinguishable from other storage media such as solid state drives and flash drives in terms of capacity, price and use, and that HDDs comprise a product market. It recognized that HDDs have different end uses and may be divided into sub-markets such as HDDs for servers, desktop computers, laptop computers and consumer electronics. The relevant geographic market is global as the supply and sale of HDD are carried out worldwide.

Market concentration has increased in the last 20 years, so that there are only 5 HDD manufacturers worldwide: Seagate, Western Digital, Hitachi Storage, Toshiba, and Samsung. Their share of global and China sales were approximately

[25] MOFCOM Announcement No. 90 (2011) regarding anti-monopoly review decision granting conditional approval of Seagate Technology LLC acquisition of Samsung Electronics Co. Ltd hard disk drive business http://fldj.mofcom.gov.cn/aarticle/zcfb/201112/20111207874274.html?3102376073=840603354 (in Chinese) (visited February 17, 2012).

33%, 29%, 18%, 10% and 10%, respectively. The HDD market is fairly transparent. MOFCOM considered HDDs to be commodities and their manufacturers to be fairly undifferentiated in their product lines. Customers can readily switch suppliers. There are relatively few major buyers, and manufacturers often have common distributors to market to other buyers. Prices paid by the major buyers, the large computer manufacturers, generally set market prices. HDD manufacturers can therefore fairly readily discern competitors' technology, costs, prices, output and sales.

Major computer makers often use confidential bidding for HDD procurement, with quarterly bilateral negotiations with HDD makers. To ensure continuity and security of supply, the computer makers generally divide their purchases among 2 to 4 HDD makers, allocating the purchase volumes according to the prices and other terms and conditions of sale offered. In each round of negotiations, the most competitive HDD maker will get the largest order, while the least may get none. This process requires HDD makers to compete. MOFCOM concluded that maintaining the current procurement process is crucial to maintaining competition in the HDD market.

On the other hand, MOFCOM found that large computer makers generally are indifferent to price increases that are not targeted towards any particular customer, because they can pass on the increases in the computers sold to consumers, who are dispersed and have no countervailing buying power. HDD makers generally direct pricing for distributors and distributors have insufficient purchasing power to resist the HDD makers. MOFCOM noted that Western Digital's loss of substantial production capacity from recent floods in Thailand led to HDD price increases by all manufacturers, and price increases in computers that apparently resulted from computer makers passing on those HDD price increases.

MOFCOM also found that capacity usage in HDD manufacturing has been increasing steadily since 2008, with about 90% usage in the fourth quarter of 2010. Innovation is a major factor in the HDD industry, with profit margins dropping quickly as an innovation spreads through the industry, so that manufacturers have constantly sought to reduce costs through innovation. MOFCOM concluded that competition is a major driver of innovation in the HDD industry and any reduction of competition would substantially reduce the motivation for and speed of innovation on the part of manufacturers.

Moreover, the substantial intellectual property and technical expertise needed to establish a HDD manufacturing facility is a substantial barrier to entry. Economies of scale in HDD manufacturing and the large minimum viable scale of

a HDD facility also present huge risks and barriers to entry. There have been no new entrants into HDD manufacturing in the last 10 years. MOFCOM concluded that it is difficult to enter the HDD market.

MOFCOM found that the transaction would eliminate a major competitor, reduce competitive pressure on the remaining HDD makers and enhance their ability to obtain purchase orders under the prevailing bidding process. Given the relative transparency of the HDD market, which already enables HDD makers to predict competitors' behavior, the transaction will enhance their potential for coordinated action to restrict or exclude competition. MOFCOM noted that China is one of the major personal computer consumer nations and concluded that the transaction would adversely affect Chinese consumers. It would exclude and restrict competition in the HDD market.

As a result, MOFCOM imposed the following conditions:

1. Samsung will be maintained as an independent competitor, including by (a) establishing a new Seagate subsidiary to independently price Samsung's existing HDD product line ("Samsung Products") and independently market the Samsung HDD brand, with both Seagate and Samsung sales teams reporting to and under the supervision of the monitoring trustee, (b) having Samsung's existing sales staff continue to sell Samsung Products during the transition in ways that will not jeopardize the competitiveness of those products, and report sales to and be supervised by the monitoring trustee, (c) maintaining the pricing independence of the Samsung sales team, with a firewall to prevent exchange of competitive information between the Samsung and Seagate teams, with only one designated Samsung sales person reporting to only one designated Seagate person, only on non-competitive matters, with the identities of both to be reported in advance to the monitoring trustee and the substance of any communications between them to be reported simultaneously or in advance to the trustee and subject to the trustee's supervision, (d) maintaining independent operation of Samsung's production line, with Samsung's equipment, processes and production system, and technical support and innovation to improve the productivity and competitiveness of Samsung Products that is reported to the monitoring trustee throughout and subject to the trustee's supervision, (e) establishing an independent reasonable pricing mechanism for Samsung Products under the supervision of the monitoring trustee, and (f) establishing an independent R&D center for Samsung Products, with technical support from Seagate including Seagate's standard processes to

improve the capacity and competitiveness of Samsung Products, all reported to and under supervision of the monitoring trustee.

2. Seagate will maintain and expand the capacity of Samsung Products within 6 months, and thereafter set the capacity and volume of Samsung Products reasonably according to market demand conditions. The capacity and volume of Samsung and Seagate products shall be reported monthly to the monitoring trustee.

3. Seagate may not substantively change its current business model, or expressly or implicitly require customers to purchase HDDs exclusively from Seagate or any entities it controls.

4. Seagate may not require TDK China Co. Ltd to supply HDD heads exclusively to Seagate or any entities it controls, or limit the volume of HDD heads that TDK may supply to other HDD manufacturers.

5. Seagate will invest at least $800 million annually for 3 years, and fund R&D in innovation at rates comparable to that in recent years, to ensure providing customers even more innovative products and solutions.

6. Seagate will appoint a monitoring trustee pursuant to the Provisional Regulations regarding Divestitures in Concentrations, to supervise its compliance with the conditions.

MOFCOM also provided that, after 12 months, Seagate may seek release from the first 2 conditions. Seagate must submit an implementation plan within a week of appointing the monitoring trustee, and MOFCOM will monitor Seagate's performance.

MOFCOM apparently put little if any weight on the facts that a growing number of computers have no hard disk drives, different size disk drives are not interchangeable in their end use, and it is a significant adjustment to switch HDD production from one size to another. Historically, HDD makers have specialized in particular formats. The high capacity utilization rate that has typified HDD manufacturing in recent years may reflect industry elimination of excess capacity and projections of decreasing future demand.

In contrast, the European Commission concluded that there were several HDD markets worldwide, based on their end uses.[26] It found that the primary impact of the transaction would be in 2 HDD markets in which Samsung was not a particularly strong competitor, leaving 3 strong competitors in 3.5" desktop computer HDDs and 4 strong competitors in 2.5" mobile equipment HDDs, so that customers would have sufficient alternative suppliers. The EC also found that the removal of Samsung is unlikely to create a risk of coordination among the remaining HDD makers. Moreover, it concluded that TDK would still be able to sell a sufficient volume of HDD heads to the combined Seagate/Samsung to be a viable business.

MOFCOM seems have reached inconsistent conclusions in finding that computer makers make use of a sophisticated system to ensure the most economic yet secure supply of a crucial input, HDDs, but have little incentive to resist price increases. MOFCOM may have misread the ability of computer manufacturers to pass on cost increases to consumers. It may also have reached an inapt conclusion from the market reaction to the shortage caused by the Thai floods. The price increases following the floods more likely reflect the natural interactions of supply and demand, not any exercise or lack of market power.

This is the first decision in which MOFCOM provided a potential sunset on its conditions. If Seagate is relieved of the first 2 conditions after 12 months, the remaining conditions would appear not to be onerous, although the restriction on changing its business model may provide broad scope for MOFCOM to act. Moreover, removal of the first 2 conditions would eliminate any constraint on the potential for coordinated competitive action that MOFCOM cited as a basis for the conditions. The net result of the conditions may simply be to delay the consummation of the transaction by 1 year.

The conditions imposed regarding TDK would appear to reflect concern about monopsony power or the ability to disadvantage competitors by controlling an input. However, in that case, the appropriate condition should be general to all makers of HDD heads instead of limited to TDK. The specific recognition that China is one of the major personal computer consumer nations may also reflect concern over the deal's impact on the manufacturing facilities in China of HDD and computer makers. The decision may be another instance of concern for a significant Chinese industry.

[26] Press Release IP/11/1213, October 19, 2011 http://europa.eu/rapid/pressReleasesAction.do?reference=IP/11/1213.

Tiande-Henkel JV[27]

Tiande Chemical Holdings Ltd. and Henkel Hong Kong Holding Ltd. proposed the formation of a 55-45 joint venture to produce specialty chemicals, particularly cyanoacrylate monomer, a product of ethyl cyanoacetate and a key input into cyanoacrylate adhesives. The notification was submitted on August 8, 2011 and accepted on September 26 after supplemental submissions, and MOFCOM conditionally approved the transaction on February 9, 2012 after extending its investigation into Phase 3.

After considering the uses, production, substitutes and import-export patterns for the 3 products, MOFCOM concluded that there were 3 separate relevant product markets -- ethyl cyanoacetate, cyanoacrylate monomer, and cyanoacrylate adhesives. It concluded that the relevant geographic market was global. MOFCOM also studied the distribution channels and market relationships for the products, and considered the impact of the transaction on competition in the market in China. MOFCOM concluded that the formation of the JV may exclude or restrict competition in the market for cyanoacrylate monomer.

MOFCOM found that there are only 2 major producers worldwide of ethyl cyanoacetate, with Tiande being one of the 2. Entry barriers into ethyl cyanoacetate production are very high. Ethyl cyanoacetate is produced from cyanide and chloroacetic acid, both dangerous chemicals. Ethyl cyanoacetate production has significant environmental impact, and its production, shipment, storage and sale is strictly regulated. Given environmental and other government controls, there are remaining worldwide only the 2 producers. Both produce ethyl cyanoacetate in China and sell worldwide. The market shares of the 2 manufacturers worldwide and within China are about 45% to 50%, so that the market Herfindahl-Hirschman Index is very high, 4050, indicating very high concentration. Tiande has market power in ethyl cyanoacetate.

The proposed JV intends to produce cyanoacrylate monomer from ethyl cyanoacetate, through a newly formed subsidiary. MOFCOM found adequate competition in cyanoacrylate monomer. Over 70% of cyanoacrylate monomer worldwide is produced in China. Tiande currently does not produce cyanoacrylate monomer. Henkel Hong Kong's parent, Henkel AG & Co., KGaA,

[27] MOFCOM Announcement No. 6 (2012) regarding anti-monopoly review decision granting conditional approval of formation of Joint Venture between Tiande Chemical Holdings and Henkel Hong Kong http://fldj.mofcom.gov.cn/aarticle/ztxx/201202/20120207960466.html?701599113=840603354 (in Chinese) (visited February 20, 2012).

produces cyanoacrylate monomer primarily for internal consumption in the production of cyanoacrylate adhesives. Henkel has strong positions in the cyanoacrylate monomer and adhesives markets in terms of brand, technology, capital and expertise. Historically, Henkel has purchased about 5% of Tiande's ethyl cyanoacetate production. The JV is expected to purchase most of its ethyl cyanoacetate requirements from Tiande, accounting for about 25% of Tiande's capacity.

MOFCOM concluded that, after the JV is formed, Tiande may discriminate between the JV and other cyanoacrylate monomer makers in sales of ethyl cyanoacetate, because of Tiande's relationship with the JV and its controlling position in ethyl cyanoacetate. In that way, Tiande may extend its market power to the JV, and weaken the competitiveness of other cyanoacrylate monomer makers.

Therefore, MOFCOM required Tiande to supply ethyl cyanoacetate to downstream customers on equitable, reasonable and non-discriminatory terms, including prohibiting Tiande from charging unreasonably high sales prices, giving the JV favorable supply conditions, and exchanging competitive information with Henkel and the JV. The parties must report annually and at MOFCOM's request on their compliance with the conditions, and appoint a monitoring trustee to oversee their compliance. They are to present an implementation plan as soon as possible after the appointment of the trustee and to implement the plan following MOFCOM's approval.

MOFCOM apparently is the only competition law authority reviewing the transaction to impose conditions.[28] Given Tiande's strong position in ethyl cyanoacetate, there would appear to be some potential for leveraging that position to favor the JV and disadvantage other cyanoacrylate monomer makers. However, it's unclear how strong that concern should be when the JV appears to be significantly a vehicle for Henkel to exit the manufacture of cyanoacrylate monomer that it has historically consumed internally.

Unless the JV is expected to produce far more cyanoacrylate monomer than Henkel has historically, then even if the JV sources from Tiande far more of its ethyl cyanoacetate than Henkel has historically, there may be little impact on other cyanoacrylate monomer makers. Tiande would still have substantial

[28] The transaction was notified to several jurisdictions in Europe, but apparently not to the EC or the U.S., given its size. Tiande will invest €32.4 million and Henkel will invest €10.8 million into the JV. http://tdchem.hi2000.com/images/LTN20110703079.pdf (visited February 20, 2012).

production that it must sell to third parties. Presumably, the other major ethyl cyanoacetate manufacturer will benefit from additional sales to other cyanoacrylate monomer makers if sales historically made by Tiande to those makers are being diverted to the JV and if purchases Henkel made historically from the other ethyl cyanoacetate manufacturer are being diverted to Tiande so that Tiande may have less capacity to sell to other monomer makers. Without information on Henkel's historic cyanoacrylate monomer production and the JV's expected production capacity relative to that history, it is difficult to ascertain how serious a threat the JV may be to cyanoacrylate monomer competition. In fact, if the JV's expected capacity is substantially larger than Henkel's needs so that the JV must sell some of its cyanoacrylate monomer production on the open market, the JV arguably creates a new entrant into the cyanoacrylate monomer market, increasing competition in a market that MOFCOM concluded has adequate competition.

MOFCOM may have applied a very conservative standard to the vertical integration created by the JV, and have again acted to ensure the raw material access of a significant Chinese industry that currently supplies over 70% of cyanoacrylate monomer worldwide.

Conclusion

The rapidly increasing sophistication of MOFCOM's analyses of transactions bodes well for the future of merger control under the AML. On the other hand, the decisions also reflect the continuing balance of competition and non-competition factors that MOFCOM faces. These may be the result of structural factors that China confronts, far beyond the purview of the AML, which may ultimately limit the effectiveness of the AML, despite the best efforts of MOFCOM, NDRC, SAIC and the Anti-Monopoly Commission.[29]

[29] See, Wentong Zheng, Transplanting Antitrust in China: Economic Transition, Market Structure, and State Control, 32 U.Pa.J. Int'l L. 643 (2010).

BUSINESS LAW TODAY
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M&A Under China's Anti-Monopoly Law

Emerging Patterns

By Yee Wah Chin

China's Anti-Monopoly Law is becoming a major hurdle for larger cross-border transactions.

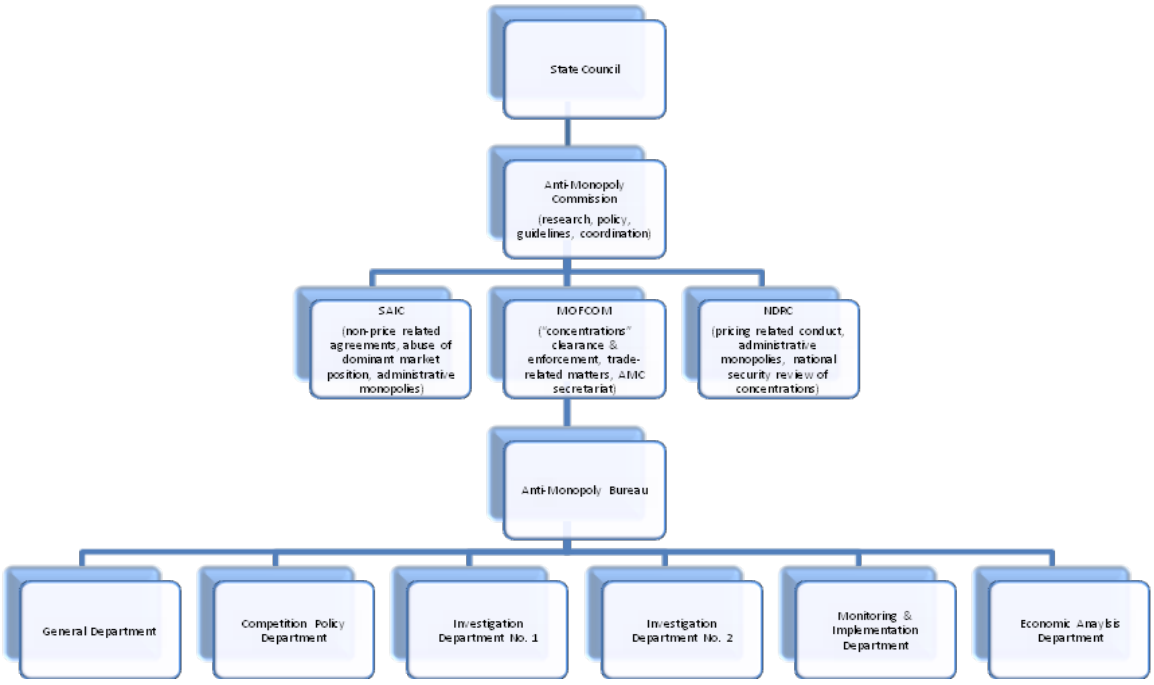
China's Anti-Monopoly Law (AML) became effective on August 1, 2008, following 13 years of drafting. Since then, businesses and lawyers with interests in China have closely followed every development. While there have been draft and final regulations issued by the enforcement agencies on most aspects of the AML, and complaints citing the AML have been filed in the courts and with the agencies alleging monopolistic conduct, the most closely watched developments have been on the M&A front. All but one of the announced government enforcement actions to date have involved transactions. It is clear that China's merger control regime is becoming the third major antitrust hurdle for large, cross-border transactions, along with the United States and the EU. This article summarizes the AML, reviews provisions relating to mergers and acquisitions, and discusses patterns emerging in China's application of the AML in the M&A area.

Overview of AML

The AML is China's first comprehensive antitrust law, and generally is within the mainstream of modern competition laws. It includes the three pillars of most modern antitrust laws, with chapters on (1) "monopoly agreements," or cartels and other multiparty anticompetitive conduct; (2) "abuse of dominant market position," dealing with unilateral conduct; and (3) "concentrations," which covers mergers and acquisitions and joint ventures. The AML also includes distinctive provisions: a chapter on abuse of administrative power that is directed toward rampant local protectionism and articles on state-owned enterprises in sectors that are economically vital or implicate national security, businesses that have exclusive distribution rights pursuant to law, and trade associations.

The law establishes a multilevel and multifaceted enforcement structure under the State Council, the chief executive body. It creates a new entity, the Anti-Monopoly Commission (AMC), to (1) research and draft competition policy, (2) organize and publish studies on the state of competition, (3) develop guidelines, (4) coordinate enforcement, and (5) fulfill assignments from the State Council. The AML specifies that the State Council will designate Anti-Monopoly Enforcement Authorities (AMEA) that will be responsible for enforcement. The State Council designated three existing agencies to share enforcement responsibilities: (a)

Chart 1: AML Enforcement Structure



the Ministry of Commerce, (b) the State Administration for Industry & Commerce (SAIC), and (c) the National Development & Reform Commission (NDRC). MOFCOM is the secretariat for the AMC as well as the AMEA responsible for merger control and enforcing the AML against anticompetitive conduct in international trade. The SAIC is assigned to enforce the AML with respect to all other violations except for pricing conduct. The NDRC is responsible for prosecuting pricing-related violations. The statute specifies the investigatory authority of the AMEAs, including mandating at least two officials on each investigation and written records of interrogations. The confidentiality of trade secrets is expressly protected. Chart 1 illustrates the AML enforcement structure.

The AML provides a range of remedies. Investigations may be suspended and terminated upon targets addressing the AMEA's concerns. In the case of "monopoly agreements," leniency is available to a participant who discloses the violation and cooperates with the investigation. Otherwise, and also in the case of abuse of dominant market position, "illegal gains" may be confiscated and fines may be imposed of between one and 10 percent of the previous year's turnover. Trade associations that organize monopoly agreements are subject to fines of up to RMB500,000 and cancellation of their registration. Fines and criminal sanctions are authorized for obstructing investigations. The law is notably lacking in significant remedies against competitive abuse of administrative powers. It provides for administrative review and review under the administrative law of AMEA decisions. There are administrative and criminal penalties for AMEA staff members who abuse their powers. Violators may be civilly liable for damages caused to others, creating a private right of action. The Supreme People's Court has designated the intellectual property tribunals of the People's Courts to handle AML cases, apparently because the tribunals may be the sections of the People's Courts most experienced in handling complex matters. Otherwise, intermediate-level courts will adjudicate AML cases.

AML Provisions and Implementing Actions Relating to "Concentrations"

The AML establishes a premerger notification system, requiring transactions above a size threshold set by the State Council to be notified to the designated AMEA (MOFCOM) and undergo a waiting period before closing. Transactions within a corporate family are exempt. The law establishes a three-phase review period of 30, 90, and 60 days. If MOFCOM does not act by the end of a phase, the transaction is deemed approved. The waiting period begins when MOFCOM accepts a notification. Consummation of a transaction in violation of the AML may result in an order to divest, a fine of up to RMB500,000, or other orders to restore the status quo ante.

The AML sets forth the principle that businesses may, voluntarily and through fair competition, combine according to law to expand scale and increase their competitiveness. MOFCOM is to consider in its reviews factors including the parties' market shares, market concentration, and the impact of the transaction on market access, technological advance, consumers, other interested businesses, and national economic development. Transactions that will or may eliminate or restrict competition will be prohibited. Where the pro-competitive effects of the transaction outweigh its adverse effects, or where the transaction may benefit the public interest, MOFCOM may decide not to prohibit the transaction. It may permit a transaction upon conditions. Both prohibitions and conditional approvals must be published. Perhaps most distinctively in this area, the AML provides that where foreign capital is involved in a concentration that implicates national security, the transaction will undergo separate review pursuant to relevant regulations.

Since the AML became effective, the State Council has announced the size-of-transaction thresholds, the AMC has issued market definition guidelines, and MOFCOM has issued procedural measures on premerger notifications and reviews of notified transactions as well as guidance on notification contents and the review process, and provisional rules on required divestitures. Drafts have been circulated regarding the substantive standards for merger review and the treatment of unnotified transactions.

Interaction with Other Laws Relating to M&A

There are reports that a multiministry committee is being formed to conduct national security reviews of transactions, pursuit to a Plan for National Security Review Mechanism that was announced at the March 2010 annual session of the National People's Congress. How that will affect transactions involving non-Chinese parties will be closely watched.

The AML itself does not distinguish between foreign and domestic businesses. However, until July 2009, foreign investors were also subject to premerger notification and competition review under the Provisions on M&A of a Domestic Enterprise by Foreign Investors (Foreign M&A Provisions). In July 2009, the Foreign M&A Provisions was amended to conform its premerger notification and review provisions to the AML, so that foreign buyers would be subject to only one competition notification and review requirement, that under the AML. Significantly, the 2009 amendments retained the requirement of a

Table 1: Notification Review Timelines

	Submitted	Accepted	2d Phase	3d Phase	Decision
InBev/Anheuser-Busch	9/10/08	10/27/08	—	—	11/18/08
Coca-Cola/Huiyuan	9/18/08	11/20/08	12/20/08	—	3/18/09
Mitsubishi Rayon/Lucite	12/22/08	1/20/09	2/20/09	—	4/24/09
GM/Delphi	8/18/09	8/31/09	—	—	9/28/09
Pfizer/Wyeth	6/9/09	6/15/09	7/15/09	—	9/29/09
Panasonic/Sanyo	1/21/09	5/4/09	6/3/09	9/3/09	10/30/09
HP/3Com	12/4/09	12/28/09	1/27/10	—	4/7/10*
Novartis/Alcon	4/20/10	4/20/10	5/17/10	--	8/13/10

* No decision was published as it was an unconditional approval.

notification to and review by MOFCOM of transfers of control of domestic businesses that involve a critical industry, implicate national economic security, or own any famous trademarks or venerable Chinese brands. This clause, though not cited in MOFCOM's AML decisions, may underlie the difficulties experienced by foreign companies in several merger investigations. MOFCOM's AML decisions thus far raise questions of whether national brands will play an outsized role in premerger reviews even though the AML is silent in this respect.

Emerging Patterns

As of June 2010, there were over 140 transactions notified, and six decisions published. MOFCOM stated on August 12, 2010, that 95 percent of the notified transactions were cleared unconditionally, and that over 60 percent were cleared during the first phase of 30 days following acceptance of the notifications. On August 13, 2010, a seventh decision was announced. The seven decisions published to date reflect economic and competition analysis, though in some cases arguably analysis that has been abandoned by other jurisdictions. The analysis should become more refined with experience. What is of greater concern and more difficult to ameliorate is an emerging pattern of a merger control process that may be politicized and trumped by industrial policy and nationalism. The fact that all the published decisions relate to transactions involving non-Chinese entities may reflect that. Also, MOFCOM has introduced more procedural flexibility than is apparent in the AML.

The flexibility that MOFCOM has introduced into the process is revealed in its handling of filings. Since the AML time frame applies only after a notification is accepted, MOFCOM has effectively elongated that time frame by the time it takes to accept a notification, sometimes by months. Table 1 illustrates this effect.

Thus, although the AML may contemplate that a review would end after a maximum of 180 days, or six months, after a notification is filed, the reality has exceeded in one case over nine months. On the other hand, although the default under Chinese law is that "days" are "business days," MOFCOM has treated "days" under the AML to mean "calendar days" and adhered to the AML timeline once it accepts a notification. This provides parties with some certainty. Nonetheless, the practical effect is that, in a transaction that MOFCOM concluded had no anti-competitive effect, it took over two months to complete its review and impose conditions. Hopefully, the fact that MOFCOM accepted the Novartis/Alcon notification on the day it was submitted indicates that there will be less advantage taken in the future of the flexibility that has been introduced into the AML time line.

Moreover, although a transaction is deemed approved if MOFCOM fails to act within the AML time frame, MOFCOM effectively prohibits a transaction by simply refusing to accept a notification and therefore to start the clock. An example of this "pocket veto" may be the attempt by the Internet portal company Sina.com to acquire an interest in Focus Media, a Chinese advertising and digital media company. The transaction was announced in December 2008 and notification submitted to MOFCOM. MOFCOM never accepted the notification, and the parties finally abandoned the deal in September 2009 since they could not close it without the expiration of the waiting period, which never began. Similarly, the proposed acquisition of General Motor's Hummer division by Sichuan Tengzhong Heavy Industrial Machinery may have been abandoned in February 2010 after being announced in June 2009, in significant part because MOFCOM apparently never accepted notification of the transaction. This may be one method to deter transactions that MOFCOM does not want to approve, without publishing any reasons. In both cases, it is unclear that there was any competitive impact reason for blocking the deal while there may have been industrial policy reasons to do so.

Nationalism may be reflected in the treatment of the InBev/Anheuser-Busch transaction. The merged entity would have accounted for only 13 percent of the beer industry in China. The four largest brewers in China together accounted for around 41 percent of industry revenues. In its conditional approval of the deal, MOFCOM found no anticompetitive impact from the transaction yet prohibited InBev from increasing its holding of the 27 percent of Tsingtao Beer that Anheuser-Busch held or its own 28.56 percent holding of Zhujiang Brewery, and from buying interests in two other Chinese beer brewers without prior MOFCOM review even if the transactions would otherwise be exempt from AML review. InBev must notify MOFCOM of any changes in controlling shareholders. MOFCOM stated that the conditions were imposed because of the size of the transaction and the market position of the resulting entity, to minimize potential adverse effects in China's beer market. In the United States and EU, a transaction that is found not to be anticompetitive would have been cleared unconditionally. MOFCOM's approach seems to reflect concern over greater foreign control over a noted Chinese brand, Tsingtao, and foreign control over Chinese companies generally. It also may reflect a concern that, if there are anticompetitive consequences later, which would presumably fall under the jurisdiction of the SAIC and/or the NDRC, those agencies may fail to act, so that a prophylactic was adopted.

Nationalism may have been an even greater factor in the prohibition of the Coca-Cola/Huiyuan deal. The public reaction was vociferous and overwhelmingly negative, in the Internet and in the media, to the prospect of Coca-Cola ownership of the Huiyuan brand. Competition concerns were less apparent. Coca-Cola accounted for over 60 percent of carbonated soft drink sales in China, but Huiyuan, China's largest juice manufacturer, was insignificant in that area. The combined entities would have accounted for under 30 percent of juice sales in China. MOFCOM based its prohibition on (1) Coca-Cola's post-acquisition ability to leverage its dominant position in carbonated drinks to fruit juice, thus affecting other fruit juice competitors and harming competition and consumers; (2) the potential of the merged entity to eliminate competitors, limit competition, and harm consumer welfare by tying, bundling, and other exclusionary practices; (3) the increased entry barriers resulting from the control that Coca-Cola would have on two major juice brands, Minute Maid and Huiyuan, when coupled with its position in carbonated drinks that may increase its dominance in juice; (4) the decreased opportunities for domestic small and medium-sized juice businesses to compete and innovate; (5) the adverse impact on competition in the China juice market and development of the Chinese juice industry; (6) the lack of offsetting positive effects or public interest; and (7) the lack of adequate remedies offered by Coca-Cola. This explanation is controversial among the antitrust bar and leaves the impression that it was the pretext for a

decision based on nationalism and political expediency.

The outcomes and stated analyses in the InBev/Anheuser-Busch and Coca-Cola/Huiyan transactions raise questions regarding the application of the Foreign M&A Provisions. MOFCOM made no reference to the Foreign M&A Provisions in its decisions, but it may be difficult to escape the conclusion that at least the national brands article of the Foreign M&A Provisions played a role. It may be nationalism more than industrial policy that prevailed in these two cases, since there appeared less an issue of protecting or building a national champion and more the national pride in retaining domestic control of a local brand name.

Industrial policy may be reflected in the conditions MOFCOM imposed on Mitsubishi Rayon's acquisition of Lucite. This transaction cleared competition law reviews elsewhere without fanfare, yet went into the second phase in China. The merged entity would have accounted for 64 percent of methyl methacrylate monomers produced in China, but new capacity was expected to come online shortly that may lower the merged entity's position below 40 percent. There was significant competition internationally. The key factor appears to have been the concern of Chinese competitors and customers. MOFCOM also noted that both Mitsubishi Rayon and Lucite are vertically integrated, so that there was the potential for exclusion of competitors in downstream markets. MOFCOM conditioned its approval on (1) Lucite China selling at cost 50 percent of its annual MMA production for five years to an approved third party, with a divestiture trustee to be appointed to complete that sale if it is not completed in six months; (2) Lucite China operating independently from Mitsubishi Rayon China's MMA monomer business until divestiture; and (3) the merged entity refraining for five years from further acquisitions or new plant construction in China in MMA monomer, PMMA polymer, or cast acrylic sheet without prior MOFCOM approval. A similar prohibition on greenfield expansion was last imposed in the United States 40 years ago, in *Ford Motor Co. v. United States*, 405 U.S. 562 (1972), requiring Ford to divest Auto-Lite, a spark plug and automotive parts manufacturer that Ford purchased in 1961, and prohibiting Ford from manufacturing spark plugs for 10 years. This draconian condition on Mitsubishi Rayon would seem justifiable only on industrial policy grounds, to promote domestically owned industry, when the transaction raised little competitive concerns by most competition analyses.

Two of the more recent decisions raise fewer questions because the results were consistent with those in other antitrust jurisdictions. In approving GM's acquisition of Delphi, MOFCOM imposed firewalls and other conditions to ensure that GM's and Delphi's competitors would not be disadvantaged by the vertical integration. In Pfizer/Wyeth, with the merged entity accounting for almost 50 percent of swine mycoplasma pneumonia vaccine in China, the next largest competitor at only 18.35 percent, and high entry barriers, MOFCOM required Pfizer to divest two brands of the vaccine in China within six months to a MOFCOM-approved buyer. However, the conditions for an approved divestiture apparently meant that effectively only a Chinese buyer would be approved and that significant intellectual property would be transferred, leading to concerns that China may have taken the opportunity to further industrial policy. Harbin Pharmaceuticals was the buyer, becoming the largest producer of swine vaccine in China.

The decision on Panasonic's acquisition of Sanyo is notable for both the lengthy process and the extraterritorial conditions imposed. For the first time, MOFCOM defined worldwide relevant markets and required divestitures outside China, of battery plants in Japan. The later unconditional approval of the HP/3Com transaction, which received early termination of the Hart-Scott-Rodino waiting period in the United States and unconditional clearance in the EU, raised hopes of a continuing development toward rigorous competition analysis, as it might have been an opportunity to further industrial policy in the guise of remedying a competition concern by requiring a divestiture entailing technology transfer.

The latest published decision, granting conditional approval of Novartis's acquisition of Alcon, offers mixed support for those hopes. MOFCOM for the first time expressly considered the possible increased likelihood of coordinated anti-competitive conduct as a result of a transaction. The Novartis/Alcon combination would have accounted for almost 20 percent of contact lens care product sales in China, which by itself was unproblematic. MOFCOM was concerned that the combination, together with Novartis's distribution arrangement and strategic partnership with Hydron Contact Lens, the largest seller in China which accounted for over 30 percent of sales of lens care products in China, would create competitive issues by increasing the likelihood of coordination over price, volume and territory by two players that together account for over 50 percent of sales in China. It required Novartis to terminate the distribution arrangement with Hydron within 12 months. On the other hand, MOFCOM also required Novartis to exit the distribution in China of ophthalmic anti-infective and anti-inflammatory compounds where it had less than 1 percent of sales and refrain from re-entering for five years, because the transaction would have resulted in a combined market share of over 60 percent. This minimal 1 percent increase in market share would be unlikely to result in the imposition of any condition in developed antitrust jurisdictions, especially since Novartis had expressed the intent of shutting down its business in that product line globally. Moreover, the remedy imposed, exit rather than divestiture, would seem to lessen instead of preserve competition. The decision offered little guidance as to the reasoning behind the conclusion of anti-competitive concern or remedy.

The strongest indicator that industrial policy trumps competition principles may be the fact that major transactions among Chinese companies have been completed without any AML notification, and any MOFCOM enforcement. State-sponsored reorganizations of the telecommunications, auto, and airline industries in the last few years have involved transactions that clearly exceed the notification thresholds, without any notification to or review by MOFCOM. A notable example is the China Unicom/China Netcom transaction in October 2008. A number of mergers of state-owned enterprises have been announced as approved by the State Council without any reference to the AML or MOFCOM.

Conclusion

There appear to be emerging patterns of industrial policy and nationalism trumping competition policy, greater procedural flexibility in the merger control regime than apparent at first glance, and analytic

approaches that may have been abandoned elsewhere. Nonetheless, the increasingly detailed published MOFCOM decisions reflect a policy of increasing transparency and applying economic analysis in merger control, to be in the antitrust mainstream. Moreover, MOFCOM's sensitivity to perceptions of discriminatory enforcement of the AML is reflected by the fact that the Director General of its Anti-Monopoly Bureau held a press conference on August 12, 2010, apparently for the specific purpose of emphasizing that China never discriminated against foreign companies in the enforcement of the merger control provisions of the AML and that conditions were placed on transactions because they would otherwise adversely affect competition. Hopefully this sensitivity will temper deference to industrial policy and nationalism.

Yee Wah Chin is of counsel at Ingram, Yuzek, Gainen, Carroll & Bertolotti, LLP in New York City.

Additional Resources

For other materials related to this topic, please refer to the following.

Business Law Today

Keeping Current: Antitrust
China Passes Comprehensive Anti-monopoly Law
By Jonathan S. Gowdy
Volume 17, Number 3
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