



TO FILE OR NOT TO FILE:
THE TREATMENT OF OFFSHORE
JOINT VENTURES
UNDER THE EU AND CHINA'S
MERGER CONTROL REGIMES

Angela Huyue Zhang
Herbert Smith LLP

&

Mark Jephcott
Herbert Smith LLP

To File or Not to File: The Treatment of Offshore Joint Ventures under the EU and China’s Merger Control Regimes

Angela Huyue Zhang & Mark Jephcott*

Joint ventures (“JV”) encompass a broad range of commercial operations. The creation and operation of a JV can be subject to competition scrutiny in every jurisdiction that it affects, and in some cases, even those jurisdictions that are not obviously affected by the creation of the JV. A common question for parties to an international JV transaction is whether the JV needs to have a sufficient “nexus” to the jurisdiction in question for the transaction to fall within its merger control regime. This note focuses on the merger regulations of the European Union and China, and their potential extraterritorial jurisdiction over newly created offshore JVs.

I. EU MERGER CONTROL REGIME

Pursuant to the EU Merger Regulation (the “EUMR”), a JV will be notifiable if: (i) it constitutes a “concentration”; **and** (ii) it meets certain jurisdictional thresholds, that is, it has a “Union dimension” (the “jurisdictional test”). On receiving the notification, the European Commission (the “Commission”) will review whether the transaction could be expected to result in a “significant impediment to effective competition” (the “substantive test”).

It is important to distinguish between the jurisdictional test and the substantive test. Transactions must be notified where the jurisdictional test is met, even where they will have no effect on competition in the European Union.

A. CONCENTRATION

The creation of a JV qualifies as a “concentration” under the EUMR if the JV performs “on a lasting basis all the functions of an autonomous economic entity.” A JV meeting this definition is referred to as a “full function” JV, and constitutes a concentration if each of the following three criteria are met:

1. “joint control” is acquired over the JV (*i.e.* each parent has a veto over strategic commercial decisions);
2. the JV is formed on a lasting basis; and

* Herbert Smith LLP. The authors would like to thank their colleagues Karen Ip, Molly Herron and Nanda Lau for helpful comments on earlier drafts. This article does not constitute legal advice and should not be relied on as such.

3. the JV is an autonomous and independent player on the market.

B. UNION DIMENSION

The creation of a JV will have a Union dimension if either the first or second set of turnover thresholds set out below is met. The relevant turnover for these purposes is that of the “undertakings concerned,” *i.e.* the parent undertakings (and their corporate groups) in a JV scenario.

First set of thresholds: (a) The combined worldwide turnover of all the undertakings concerned exceeds €5 billion; **and** (b) the EU-wide turnover of each of at least two of the undertakings concerned exceeds €250 million, unless each of the undertakings concerned achieves more than two thirds of their EU-wide turnover in one and the same EU Member State.

Second set of thresholds: (a) The combined worldwide turnover of all the undertakings concerned exceeds €2.5 billion; (b) In each of at least three EU Member States, the combined aggregate turnover of all the undertakings concerned exceeds €100 million; (c) In each of at least three EU Member States included for the purpose of point (b), the aggregate turnover of each of at least two of the undertakings concerned exceeds €25 million; **and** (d) The aggregate EU-wide turnover of each of at least two of the undertakings concerned exceeds €100 million, unless each of the undertakings concerned achieves more than two thirds of their EU-wide turnover in one and the same EU Member State.

C. FAILURE TO NOTIFY

A full-function JV with a Union dimension must be notified and cannot be implemented until it has been cleared by the Commission. Pursuant to the EUMR, an undertaking that violates this obligation may face fines of up to 10 percent of its aggregate worldwide turnover. This requirement is very real: in 2009, the Commission imposed a fine of €20 million on Electrabel, a Belgium company, for acquiring control of CNR, a French company, without having received prior approval under the EUMR.¹

II. CHINA'S MERGER CONTROL REGIME

¹ See Press Release, European Commission, Commission fines Electrabel 20 million euros for acquiring control of Compagnie Nationale du Rhône without prior Commission approval (June 10, 2009), <http://europa.eu/rapid/pressReleasesAction.do?reference=IP/09/895> and a summary of the decision Case COMP/M. 4994-Electrabel/Compagnie Nationale du Rhône, 2009 O.J. (C 279) 08.

Similar to the EUMR, a JV will be assessed under the Anti-Monopoly Law (the “AML”) if it: (i) constitutes a “concentration”; and (ii) meets certain jurisdictional thresholds.

A. CONCENTRATION

A concentration is defined under the AML as: (i) merger; (ii) acquisition of control over another undertaking by acquiring equity interests or assets; and (iii) acquisition of control or being able to exert a decisive influence over another undertaking by contract or other means. “Control” is not defined under the AML and Chinese merger rules are silent on the treatment of JVs. In practice the Anti-Monopoly Bureau of the Ministry of Commerce (“MOFCOM”) has taken the view that the creation of a JV constitutes “acquisition of control by contract or other means” and it has exercised jurisdiction over JVs that would not meet the “full-function” criteria under the EUMR.

B. TURNOVER THRESHOLDS

If a transaction qualifies as a concentration under the AML, it must be notified to MOFCOM if it meets one of the two sets of turnover thresholds set out below.² Similar to the European Union, the relevant turnover for these purposes is the group-wide turnover of the parent undertakings in a JV scenario.

First set of thresholds: combined worldwide turnover of all undertakings exceeded RMB 10 billion **and** China-wide turnover of each of at least two undertakings exceeded RMB 400 million in the previous financial year; or

Second set of thresholds: combined China-wide turnover of all undertakings exceeded RMB 2 billion **and** China-wide turnover of each of at least two undertakings exceeded RMB 400 million in the previous financial year.

C. FAILURE TO NOTIFY

Similar to the European Union, a transaction that meets the jurisdictional thresholds under Chinese merger rules must be notified and cannot be implemented until it has been cleared by MOFCOM. Where business operators fail to comply with the mandatory notification provisions, MOFCOM is empowered to terminate and/or unwind the transaction, dispose of relevant assets, shares or businesses within a certain period, and impose fines of up to RMB 500,000. To date, there is no public record of any party having been fined under the AML for

² MOFCOM may also review a transaction that falls short of these thresholds if it considers that the transaction has the effect or potential effect of eliminating or restricting competition.

failure to notify. MOFCOM has released two drafts of its rules on investigating and sanctioning non-compliance, and it can be expected that the agency will soon step up its enforcement against any violation of the notification obligations.

III. EXTRATERRITORIAL JURISDICTION

Pursuant to the EUMR and Chinese merger regulations, the relevant turnover thresholds may be achieved by the parents to the JV alone, regardless of the geographic presence of the JV. It is therefore not uncommon for a JV to be notifiable where it will operate exclusively outside the European Union/China, on the basis of its parent undertakings' group turnover achieved in the European Union/China (as applicable).

Notably, under the EU merger control rules, in cases where the jurisdictional thresholds are met by the parents, and the JV will have negligible activities in the European Union, the parties are entitled to submit a short form notification, provided that the JV will have EU turnover or EU assets of less than €100 million. However, there is still no short form notification procedure available under China's merger control regime and it remains to be seen whether MOFCOM will introduce such a procedure for offshore JVs that have little or no nexus with China.

Parties with significant sales in the European Union or China should therefore be mindful of the extraterritorial jurisdictions of the EU and Chinese merger regulations over offshore JVs.