# Minority Participations and Merger Control Filing Requirements in East Asia

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In July 2014, the European Commission published a White Paper with several proposals for changing the EU Merger Regulation.[1] Amongst those, the Commission is proposing to extend the scope of the EU merger control regime to also cover certain non-controlling minority participations. This proposal has led to criticism that the EU merger control regime could be overreaching. In this article we briefly contrast the current EU merger control regime applicable to minority investments with the rules applicable in a selection of East Asian jurisdictions. As will become apparent, non-controlling minority participations may already today be caught by merger control requirements in Asia.

**The notion of concentration: two camps**

With the notable exception of Hong Kong[2] and Malaysia, competition law jurisdictions across East Asia have adopted a merger control regime as part of their competition law framework.[3] Some jurisdictions like South Korea, Taiwan and Japan have had a merger control regime in place for many years. In other places (such as China, Indonesia, Vietnam or Singapore) the regime was introduced more recently.

Except for Singapore, most East Asian jurisdictions have opted for a mandatory merger control regime: a notification will be required (i) where a transaction qualifies as a "concentration"[4] and (ii) the transaction parties meet relevant notification thresholds (usually expressed by reference to both domestic and worldwide turnover, market share or asset thresholds).

The notion of "concentration" varies from one jurisdiction to another. Broadly speaking it is possible to distinguish two camps. The first camp regroups countries such as China, Indonesia and Singapore, which rely on a "change of control" test to identify those transactions falling within the scope of their merger control regime. Non-controlling minority acquisitions will not be caught but, as we will see, the notion of control also varies from one jurisdiction to the next. The second camp regroups countries such as Japan, South Korea and Taiwan, which mostly rely on formalistic criteria to identify relevant concentrations. Minority share acquisitions exceeding certain equity thresholds will be caught irrespective of whether control is acquired.

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1 European Commission White Paper "*Towards more effective EU merger control"* dated 9 July 2014. More recently, in October 2014 the European Commission published a competition policy brief on the acquisition of minority shareholdings (Minority Power – EU Merger Control and the acquisition of Minority Shareholdings).

2 Hong Kong's Competition Ordinance (Cap 619) only contains merger control provisions for concentrations in the telecommunications sector.

3 Thailand has a merger control regime but implementing regulations have yet to be adopted. In the Philippines, the Corporation Code requires mergers and consolidations of corporations to be approved by the Securities and Exchange Commission (SEC). The Department of Justice for Competition recently signed an MOU with the SEC which provides for a consultation process with respect to the competition law aspects of proposed mergers and consolidations.

4 The notion of "concentration" is a generic term used to refer to those transactions which may be subject to merger filing requirements. Please note that in some jurisdictions, "concentrations" are referred to as "business combinations" or "mergers".

## Jurisdictions relying on a control test

A number of emerging competition law jurisdictions have (sometimes) heavily borrowed from the EU model when establishing their domestic competition law regime. In East Asia, this is clearly the case for Singapore, as well as (albeit to a lesser extent) China and Indonesia. The merger control regime in these three jurisdictions uses concepts that are familiar in Europe. In particular, all three jurisdictions rely on a "change of control test" to identify relevant concentrations.[5]

Under the EU regime, the notion of control is broadly defined and refers to the possibility of exercising decisive influence on an undertaking. Such decisive influence can exist on the basis of rights, contracts or any other means. Control may be acquired on a legal or *de facto* basis and it may take the form of sole or joint control. A minority participation will usually be insufficient to confer control unless particular rights attach to it, allowing the minority shareholder to determine the strategic commercial conduct of the business (positive control) or to veto those decisions (such as the budget, the business plans, major investments or the appointment of senior personnel) which are essential for the strategic conduct of the business (negative control). In some instances, a minority shareholder can also enjoy control on a *de facto* basis, for instance where it is highly likely to achieve a majority of the votes cast at the shareholder meetings, given the dispersed nature of the remaining shares and the other shareholders' poor attendance in the past. Such *de facto* control scenarios are however relatively rare, and in most cases, minority investments with no particular rights attached (other than standard minority protection rights) will not give rise to a merger filing requirement. This could change in the future, as one of the proposals put forward by the European Commission is to expand the concept of "concentration" to also capture minority acquisitions which fall short of conferring control whilst still giving the minority investor a certain degree of influence over the business.

Whilst the notion of control in the East Asian jurisdictions is largely inspired by the EU concept, in some places the boundaries of this notion are not yet crystalized in detailed enforcement guidelines, and in practice the concept of control could possibly be broader than in the EU - as will be explained below.

## Singapore

The notion of control under Singapore's merger control regime is aligned with the EU regime. According to Section 54(3) of the Competition Act, "control, in relation to an undertaking, shall be regarded as existing if, by reason of rights, contracts or any other means, or any combination of rights, contracts or other means, decisive influence is capable of being exercised with regard to the activities of the undertaking." The Competition Commission of Singapore (CCS) has issued detailed guidance on the notion of control, which heavily borrows from the EU guidance. Interestingly, the guidelines provide for a rebuttable presumption of control in the case of ownership of between 30 and 50 percent

[5] The notion of control is also relevant under the Vietnamese merger control regime; see Article 17.3 of the Vietnamese Competition Act.

of the voting rights in an undertaking.[6] This presumption, which is absent from the EU regime, could have suggested a more stringent approach towards minority participations. In practice, however, the Singapore approach is aligned with the EU regime, except that because of the voluntary nature of the regime, very few minority acquisitions are notified to the CCS.[7]

**Indonesia**

Indonesia also relies on a control test to identify those transactions which might need to be notified if the relevant thresholds are met. The Indonesian merger control regime captures mergers, consolidations and share acquisitions. Pursuant to Government Regulation 57 of 2010 (the "Regulation"), only those share acquisitions resulting in a change of control of the target are caught. The explanatory notes to the Regulation provide further clarifications on the notion of control in the context of identifying those group entities whose turnover and assets figures must be included to assess whether the notification thresholds are met. The notion of control is being defined as "the ability to influence or determine the management policies or the business and or to influence and determine management of the business." Unfortunately the merger control guidelines[8] issued by the Commission for the Supervision of Business Competition (KPPU) do not elaborate further on the concept and the merger control decisions published to date do not shed further light on the precise boundaries of this notion. Based on the KPPU enforcement practice to date, it would appear that the notion of control is broadly aligned with the EU concept.

**China**

The notion of control is also at the heart of the Chinese merger control regime. According to Article 20 of the Antimonopoly Law, concentrations include (i) mergers, (ii) acquisitions of control by means of asset or equity purchase (iii) as well as acquisitions of control or decisive influence through contract or any other means.

Up until recently, no formal guidance was available on what the notion of control or decisive influence might entail. In an early draft of China's Ministry of Commerce (MOFCOM)'s 2009 *Measures on the Notification of Proposed Concentrations*,[9] control was defined as the ability to make decisions regarding important management and operational issues such as the appointment of board members or key personnel, financial budgets, operation and sales, pricing, material investments, etc. Whilst such decisive influence could be achieved even absent 50 percent of the voting rights, there was an express recognition

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6 See section 3.10 of the *CCS Guidelines on the substantive assessment of mergers*.

7 Since the entry into force of the Singapore Competition Act in 2008, there have been no reported notifications of minority participations and only a couple of notifications concerning the establishment of joint ventures. The public version of the clearance decisions relating to these joint venture transactions does not specify whether the relevant transaction involved minority participations.

8 See Commission Regulation No 2 of 2013 on the Third Amendment of the Commission Regulation No 13 of 2010 on the *Guidelines for Mergers or Consolidations of Business Entities and Acquisition of Shares of Other Companies*.

9 Draft *Provisional Measures on the Notification of Concentrations of Business Operators*, 13 March 2009.

in the draft that standard minority protection rights would be insufficient to confer control. However this draft guidance was not retained in the final version of the 2009 Measures. In June 2014, MOFCOM for the first time offered formal clarifications on the point. The guidance is set out in Article 3 of an updated version of MOFCOM's *Guiding Opinion on the Notification of Concentrations of Undertakings* (the "Guiding Opinion").[10] The Guiding Opinion expressly recognizes the concept of sole control, joint control and *de facto* control and lists a number of factors which are relevant for the control analysis. These factors include the shareholding structure and board composition of the target, voting rules at board and shareholder level, the appointment of senior personnel, structural links between shareholders and directors, the existence of substantial commercial relationships between parties, *etc*. These factors echo those which are also considered in the EU to establish control. However, the guidance in China stops short of describing the particular circumstances in which a finding of control will be likely. In particular, unlike in earlier drafts, no guidance is provided on the treatment of minority acquisitions.

Based on MOFCOM's enforcement practice to date, minority acquisitions which would qualify as concentrations in the EU are also likely to qualify as such in China. However the Chinese regime could possibly capture a broader range of transactions. Unfortunately there are no published precedents which may be relied on or shed more light on the notification requirements of minority investments. Unlike in the EU, the unconditional merger control clearance decisions are not published and the public announcements relating to prohibition or conditional approval decisions do not provide much further guidance on the notion of control under Article 20 of the Antimonopoly Law.

The *Alpha V/Savio* conditional approval decision[11] however hints at a possible broad notion of control. In that case, MOFCOM conditioned its approval of the acquisition by Alpha Private Equity Fund V of Savio Macchine Tessili to the divestiture by Alpha V of its 27.9 percent interest in a Swiss competitor of Savio, Uster Technologies. Alpha V was Uster's largest shareholder and MOFCOM closely reviewed the voting patterns at shareholders' meetings, minutes of those shareholders meetings, and the composition and voting pattern of Uster's board of directors, before concluding that it could not rule out the possibility that Alpha V would influence Uster's operations and that the transaction could enable Alpha V to coordinate the operations of Savio and Uster. Whilst MOFCOM's analysis was part of the substantive assessment of the transaction (not unlike that which the European Commission would review in relation to "significant links" with competitors), it suggests a broad notion of control which could be of relevance not only at the substantive review stage but also at the jurisdictional assessment stage.

Given the broad enforcement discretion of MOFCOM, where a transaction involves a minority investor which will be actively involved in the management or operation of the business - either on a *de facto* basis or through special rights extending beyond the usual

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10 MOFCOM *Guiding Opinion on the Notification of Concentrations of Undertakings* dated 6 June 2014.

11 Public Announcement No. 73 2011 of MOFCOM dated 21 October 2011.

minority protection rights - the parties are well advised to proactively engage with MOFCOM to inform their filing strategy.

**Jurisdictions relying on equity thresholds**

Other jurisdictions (including Japan, Korea and Taiwan) have opted for a more formalistic approach to identify relevant "concentrations." In those jurisdictions, minority share acquisitions exceeding certain equity thresholds qualify as "concentrations" irrespective of whether control is acquired:

- In Japan,[12] share acquisitions resulting in the ownership of more than 20 percent of the voting shares in a target company will qualify as a concentration if the minority acquirer becomes the largest shareholder.
- In South Korea,[13] share acquisitions resulting in the ownership of 20 percent or more of the voting shares in the target (15 percent in case the target is a KOSDAQ-listed company) will qualify as a concentration.
- In Taiwan,[14] share acquisitions resulting in the ownership of more than one third of the voting shares or capital in the target will qualify as a concentration.

Such quantitative thresholds are easy to apply and promote legal certainty, but in practice they capture a broader range of transactions than in jurisdictions relying on a change of control test. Such formalistic approach can in part be explained by a different legal tradition, favoring a rules-based approach as opposed to a principles-based approach. Also, Japan, Taiwan and South Korea are established competition law jurisdictions whose rules are less influenced by the EU model centered around the "change of control" test. While quantitative thresholds are used as a first filter to identify relevant "concentrations," even in those jurisdictions, the concept of control may nevertheless play a role in the jurisdictional merger control assessment.

First, the notion of control is sometimes used to identify the boundaries of the corporate group whose activity level must be considered to determine whether the relevant notification thresholds are met. In South Korea for instance, a corporate group includes all companies controlled by the same person and control is referred to amongst others as "the ability to exercise considerable influence"[15] – a notion which broadly corresponds to the EU notion of control except that it does not seem to capture negative control situations.

Second, the equity thresholds are often not the only criteria to establish merger control jurisdiction. In Taiwan, for instance, minority participations below 33 percent may still trigger a mandatory merger filing requirement in "joint control" situations. Indeed, the notion of concentration also covers transactions whereby "an enterprise directly or

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12 See *Japan Fair Trade Commission (JFTC) Guidelines from the application of the Monopoly Act concerning the review of Business Combinations*, dated 14 June 2011.

13 See Article 12 of the *Korea Fair Trade Act.*

14 See Article 6 of the *Taiwan Fair Trade Act.*

15 See Article 3 of the *Enforcement Decree of The Monopoly Regulation and Fair Trade Act*.

indirectly controls the business operation of another enterprise." Whilst the notion of control seems to be more limited than in the EU (in particular it does not seem to capture negative control situations),[16] this alternative test could capture certain minority share acquisitions below 33 percent in situations where the minority shareholder benefits from particular rights allowing it to exercise positive control over the business. In Japan, whilst minority participations below 20 percent usually do not give rise to a merger notification requirement, the JFTC guidance makes clear that minority participations below that threshold could still trigger a filing requirement in cases "where a joint relationship is formed, maintained or strengthened."[17] The relevant factors for assessing such joint relationship include a review of the shareholding structure, the existence of interlocking directorates as well as any other commercial, financial and business relationships or agreements between parties. These criteria appear to be broader than the EU concept of control and may capture minority participations which would likely not qualify as "concentrations" in the EU.

Third, even in South Korea, where the notion of control is not used to identify those transactions subject to a mandatory merger filing requirement, the control analysis still plays a role at the preliminary review stage. Indeed, transactions which are being notified because relevant equity thresholds are met but which do not involve a change of control will be cleared under a simplified review procedure without proceeding to a detailed substantive competitive assessment of the transaction.[18]

**Conclusion**

From this brief overview, it appears that non-controlling minority participations may already today trigger merger control filing requirements in East Asia. This has mainly been the case in jurisdictions such as Japan, Korea and Taiwan relying on equity thresholds to identify relevant concentrations. In jurisdictions relying on a change of control test (such as China, Singapore and Indonesia) non-controlling minority participations are in principle not caught, but in some jurisdictions (including China and Indonesia), the notion of control is not yet crystalized and could possibly be broader than in the EU. Any possible expansion of the EU merger control regime to capture non-controlling minority participations could provide these authorities with further comfort to adopt an expansive reading of their jurisdiction to review minority acquisitions which today escape merger control review in the EU.

16 One possible exception would be a scenario where the veto rights would be so extensive to cover not only the key commercial and strategic commercial decisions but also daily business operation and the appointment of personnel.

17 See Section 1.1. B of the 2011 JFTC *Guidelines on the application of the Antimonopoly Act concerning the review of business combinations* dated 14 June 2011.

18 See Korea Fair Trade Commission (KFTC) *Guidelines for the Combinations of Enterprises Review* dated 28 December 2011.