

A REVIEW OF RECENT MERGER CONTROL ENFORCEMENT IN CHINA



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I. AN OVERVIEW OF MOFCOM'S ACTIVITIES IN 2016

China's merger control regime under the Anti-Monopoly Law of the People's Republic of China ("AML"), which came into force in 2008, has continued to evolve in the past year.

A. Legislative Developments

From the legislative perspective, the Ministry of Commerce of the People's Republic of China ("MOFCOM") is modifying the draft of *Measures for Examination of the Concentrations between Undertakings* (the "Revised Measures") on January 6, 2017, seeking for opinions from companies, lawyers and scholars. The Revised Measures, to some extent, integrate the current Measures for Examination of the Concentrations between Undertakings, Measures for the Notification of the Concentrations between Undertakings, and Guiding Opinions on Declaring the Concentration of Undertakings, etc. Therefore, the content of the Revised Measures will be comprehensive. We anticipate that the Revised Measures can provide clearer guidance in relation to important but ambiguous issues in the merger control regime, such as assessment of change of control, calculation of turnover and what is "implementation of a concentration," etc.

In addition, according to the working plan of the Anti-Monopoly Commission ("AMC") under the Chinese State Council, new and integrated IP-related antitrust guidelines are being drafted by the relevant agencies. The agencies draft their own guidelines independently first, and then the AMC will integrate them into one single *IP-related Antitrust Guidelines*. The drafting agencies include: the National Development and Reform Commission ("NDRC"), the State Administration for Industry and Commerce ("SAIC"), the State Intellectual Property Office ("SIPO") and MOFCOM. MOFCOM drafted the merger review chapter of the integrated *IP-related Antitrust Guidelines*. It is believed MOFCOM has finished its chapter and submitted it to the AMC for integration.

Both the Revised Measures and the integrated *IP-related Antitrust Guidelines* are expected to come into force in 2017.

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Moreover, according to the “deepen reform” working plan of the State Council, MOFCOM will coordinate with other Chinese anti-monopoly enforcement agencies (i.e. the NDRC and the SAIC) to promote the *Opinions of the State Council on Establishing the Fair Competition Review System in the Development of Market System*.³ According to the Opinion, MOFCOM’s future rules and guidelines are subject to the Opinion’s fair competition review.

B. MOFCOM’s Enforcement in Practice

In practice, MOFCOM had a record year again in 2016. According to the MOFCOM spokesman, in 2016, MOFCOM received 378 merger notifications, conducted reviews of 360 cases, and concluded 395 cases. In 2016, 324 cases, or 82 percent of all cases, were concluded during the 30-calendar day Phase I period, an increase of 8 percent from that of 2015.⁴ In addition, cases that were processed under the simplified procedure accounted for 76 percent of all filings. Approximately 98.6 percent of all simplified procedure cases that were filed were concluded during the Phase I stage.

In 2016, MOFCOM publishes two approvals with remedies: *Anheuser-Busch InBev/SAB Miller*⁵ and *Abbott/LightLab*.⁶ The two cases are both horizontal mergers. For *Anheuser-Busch InBev/SAB Miller*, the relevant product was beer and the combined market share exceeded 40 percent. For *Abbott/LightLab*, the relevant product was small vascular closure device and the combined market share exceeded 95 percent. Not surprisingly, the remedies adopted in both the two concentrations are structural, i.e. divestiture.

It is also notable that one notification was withdrawn from MOFCOM: *Lam Research/ KLA-Tencor*. On October 5, 2016, Lam Research announced that it gave up the acquisition of KLA-Tencor. MOFCOM formally initiated the review process on April 21, 2016. In 2015, Lam and KLA-Tencor were the second largest and the fifth largest semiconductor manufacturers in the world. After the presumptive merger, the new enterprise would be the largest in the world. During the review process, MOFCOM had close cooperation with the anti-monopoly law enforcement agency of the United States and South Korea, and exchanged views on issues such as the review progress and fair competition, etc.

In addition to the finished high profile cases, MOFCOM is reviewing a few high profile concentrations which are simultaneously reviewed by other major antitrust jurisdictions, such as *Dow/DuPont*, *Bayer/Monsanto* and *ChemChina /Syngenta*. In such high profile cases, MOFCOM tends to ask for waivers more often than before, which indicates that the communications and cooperation between MOFCOM and antitrust authorities in other jurisdictions are more and more frequent. According to MOFCOM’s official press release on January 11, 2017,⁷ in 2016, MOFCOM cooperated with the antitrust enforcement authorities in the U.S. and EU in more than 10 merger filings. Such cooperation is beneficial to the legal certainty of enforcement and consistency within different jurisdictions.

Last but not least; MOFCOM published four decisions regarding the punishment of failure to notify since 2016. For comparison, in 2015, MOFCOM also published four punishment decisions for failure to notify. In 2014, MOFCOM published three. In the latest published punishment decision, MOFCOM held that Canon and Toshiba Medical violated the AML because they failed to notify Canon’s acquisition of Toshiba Medical before implementation. Therefore, MOFCOM imposed a fine of RMB 300,000 (about USD \$43,500) upon Canon.⁸

³ Order of the State Council [2016] No. 34, published on June 1, 2016, and are promulgated for implementation as of June 1, 2016.

⁴ See, Qin Zhengyang, “MOFCOM: 2016 Antitrust Review Achieved Remarkable Results”, [秦正阳：“商务部：2016反垄断审查取得显著成效”] *China Review Network*, January 5, 2017, available at: <http://hk.crntt.com/doc/1045/3/2/3/104532391.html?coluid=45&kindid=0&docid=104532391&mdate=0106105655>.

⁵ See, the official website of MOFCOM: <http://fdj.mofcom.gov.cn/article/ztxx/201607/20160701369044.shtml>.

⁶ See, the official website of MOFCOM: <http://fdj.mofcom.gov.cn/article/ztxx/201612/20161202440204.shtml>.

⁷ See, “MOFCOM’s Annual Review in 2016, Volume 20”, available (in Chinese) at: <http://www.mofcom.gov.cn/article/ae/ai/201701/20170102499312.shtml>.

⁸ See, MOFCOM’s official website: <http://fdj.mofcom.gov.cn/article/ztxx/201701/20170102495433.shtml>.

II. SOME NEW PRACTICE DEVELOPMENTS IN 2016

A. Continue to Strengthen the Investigation towards Failure to Notify

It is notable that in practice, MOFCOM continues to strengthen its investigation towards the failure to notify concentration before implementation.

In relation to the punishment method, fines are the main punishment method. The amount is around RMB 300,000-400,000 (about USD \$43,500-\$58,000). Although the monetary punishment seems light, MOFCOM's publication of its punishment decision will have significant negative impact on a company's reputation, especially when the company is a reputable publicly listed company. In addition, MOFCOM will ask the companies concerned to stop the concentration immediately and file the notification from the very beginning, which can be very time consuming. Therefore, for a concentration which reaches the turnover thresholds, it is highly inadvisable for the notifying party(s) to implement the concentration before obtaining MOFCOM's approval. Moreover, according to MOFCOM Anti-Monopoly Bureau's Deputy Direct General, Mr. Han Chunlin, "MOFCOM will further strengthen the investigation and punishment towards the activity of illegal failure to notify."⁹

B. Stricter Formality Requirement of the Notification Form

According to MOFCOM's recent practice, formality requirement tends to be stricter than before. It seems MOFCOM is paying more and more attention to quantity analysis and details rather than just general and brief descriptions. This tendency is evident typically from the following two aspects.

1. Defining Relevant Product Market

It seems that MOFCOM recently requires the notifying party(s) to provide more comprehensive and detailed descriptions in defining the relevant product market than before.

According to Article 4 of the *Guidelines of the State Council's Anti-monopoly Commission Concerning the Definition of Relevant Markets* ("Guidelines of Relevant Markets"),¹⁰ the scope of the relevant market mainly depends on the degree to which the commodities (territories) can be substituted for one another. The substitutability includes demand side and supply side.

According to MOFCOM's practice, it normally asks the notifying party(s) to provide: (i) an introduction of the relevant product; (ii) an analysis regarding whether the relevant product constitutes an independent relevant market; and (iii) an analysis regarding whether the relevant product market can be further segmented.

First, for an introduction of the relevant product, MOFCOM requires the notifying party(s) to provide a comprehensive, detailed and thorough introduction of the relevant products.

Second, for the analysis regarding whether the relevant product constitutes an independent relevant market, although in the absence of explicit rules, according to MOFCOM's practice, it requires the notifying party(s) to provide analysis on demand and supply substitutability, including the detailed analysis from all of the following aspects:

- Market price;
- Switch cost;

9 See, Wang Xiao: "Chinese Anti-Monopoly Enforcement is Fully Accelerating", [王晓: 我国反垄断执法全面提速], www.comnews.cn, January 23, 2017, available at: <http://epaper.comnews.cn/news-1157550.html>.

10 *The Guidelines of Relevant Markets* was enacted by Anti-monopoly Commission under the State Council, and came into force on May 24, 2009.

- Production/ Manufacturing process;
- Functions of the product; and
- Industry opinions.
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Third, in order to assess whether the relevant market needs to be further segmented, MOFCOM requires the notifying party(s) to provide detailed analysis from all of the following aspects:

- Demand substitutability of the segmented products;
- Supply substitutability analysis (including the production switch) of the segmented products;
- Market price of the segmented products;
- Production/manufacturing process of the segmented products;
- Functions of the segmented products; and
- Industry opinions.

In addition, MOFCOM, more and more, requires notifying party(s) to add quantitative analysis and supportive data in relation to demand and supply substitutability analysis, the existence of neighboring market, the possibility of conducting tying/bundling, etc.

2. Defining Relevant Geographic Market

In relation to defining geographic market, recently, MOFCOM's formality requirement in this section can be very strict. MOFCOM strictly requires the notifying party(s) to provide the following information of the relevant products:

- The relevant product's import and export volume and percentage in the last year;
- HS code;
- Tariff rate (both MFN and GEN);
- Transportation cost ratio of the sales price of the product, etc.

The above remarks need to be supported by quantitative analysis and supportive data.

In practice, MOFCOM values the above factors carefully when analyzing the geographic scope. For example, if the export percentage of a product is high, international transaction cost and the tariff rate are low; MOFCOM may define the relevant geographic market as worldwide. On the other hand, if the import percentage of a product is low while the international transaction cost and the tariff rate are high, MOFCOM may regard the relevant geographic market as national. Nevertheless, it is notable that for some special products (such as drugs and pesticides), the import volume and percentage are high and the transportation cost is low. However, the geographic market of such products could be regarded as national because of the strict regulatory framework in China.

3. Possible Consequence of Failing to Provide the Information Required

If the notifying party(s) fails to satisfy the above formality requirements, most likely, MOFCOM will ask the party(s) to provide the above information in the responses to supplemental questions. However, MOFCOM might ask the notifying party(s) to refile the case if it believes absence of the above information has substantially affected the quality of the notification (e.g. making the notification misleading or incomplete).

C. Applying Simplified Procedure with More Caution: Revocation of Simplified Notification

Article 2 of the *Interim Provisions for the Standards of the Simplified Procedure of the Concentrations between Undertakings* (“Simplified Notification Standard Provisions”)¹¹ provides the criteria of applying simplified notification procedure.¹²

If a concentration is notified as a simplified case to MOFCOM, it should satisfy the above criteria. Otherwise, MOFCOM has the discretion to revoke the simplified notification. In 2016, it seems MOFCOM adopted a more cautious way to assess whether a notification qualifies the criteria in Article 2 of the Simplified notification Standard Provisions. Typically there are three possibilities:

1. Revocation Because of Failure to Define the Neighboring Market

MOFCOM may ask the party(s) to revoke the simplified notification if either the first three criteria in Article 2 of the Simplified Notification Standard Provisions are not satisfied.

One of the most common situations of revocation faced by the notifying parties may be the failure to define neighboring market and if the market share in this market exceed 25 percent. Under the Chinese merger regime, there are no explicit rules about how to define the neighboring market. According to Footnote 37 of the standard normal notification form, neighboring market means a series of products which has complementary nature or the same group of customers and the same end use. MOFCOM mainly relies on two factors to assess the existence of neighboring market: (i) whether the products of the parties can be sold to the same group of customers; and (ii) whether the products of the parties are for the same end use. If the answers to the two questions are yes, MOFCOM normally will regard such products as “neighboring products” and thus define the neighboring market. Please note, MOFCOM seldom leaves the market definition open.

For a simplified notification, if the notifying party fails to identify the products of the parties which can be sold to the same group of customers and be used for the same end use, plus either of the relevant products’ market shares exceeds 25 percent, MOFCOM may ask the notifying party to revoke the simplified notification because the concentration fails to meet the requirement of Article 2 (3) of the Simplified Notification Standard Provisions.

2. Revocation Because the Segmented Market Share Exceeds the Thresholds

Another common reason for revocation is that the segmented market share exceeds the thresholds. In 2016, MOFCOM usually asks the notifying party(s) whether the relevant product market provided can be further segmented. Especially for some simplified cases, even if MOFCOM agrees that there is no need to further segment the relevant product market defined in the notification form, it may still ask for the market share data of the segmented markets. If MOFCOM finds that the market share of the segmented market(s) exceeds the thresholds provided by Article 2(1), (2) or (3) of the Simplified Notification Standard Provisions, the simplified notification may be revoked by MOFCOM.

11 Announcement of the Ministry of Commerce [2014] No.12, on March 11, 2014.

12 Article 2 provides: A concentration of undertakings that falls under any of the following circumstances may be treated as a simplified case:

- (1) all the undertakings participating in concentration hold less than 15 percent of market share in total in the same relevant market;
- (2) both upstream and downstream undertakings participating in concentration hold less than 25 percent of market share in the upstream and down stream market;
- (3) the undertakings participating in concentration who neither in the same relevant market nor have any upstream and downstream relationship hold less than 25 percent of market share in their respective markets that relate to their transaction;
- (4) although joint ventures are established outside China by the undertakings participating in concentration, the joint ventures (“JV”) do not engage in any economic activities in China;
- (5) although the undertaking participating in concentration acquire the equities or assets of overseas enterprises, the overseas enterprises do not engage in any economic activities in China; or
- (6) the joint venture jointly controlled by more than two operators is controlled through concentration by one or more of them.

3. Revocation Because of the “Misunderstanding” of Article 2(4) and (5)

Article 2(4) of the Simplified Notification Guidelines describes a situation where a JV is established outside China and has no economic activities in China. According to the Simplified Notification Guidelines, in this context, simplified procedure should be applicable.

However, in practice, it is not clear, according to the Simplified Notification Guidelines, about how to ensure that the JV “has no economic activities in China.” Even, based on the agreement, the parent companies in the transaction will establish a JV having no connection with China, MOFCOM may query that how to ensure the new JV will not have any economic activities in China in the future. In particular, if the geographic market of the relevant product is defined as worldwide, it could be very hard to convince MOFCOM that the JV “has no economic activity in China” in future since the sale of products may have impact on the Chinese market. In this context, MOFCOM may hold that Article 2(4) is not applicable and therefore revoke this simplified notification.

Article 2(5) describes a situation where an undertaking purchases the equities or assets of overseas enterprises, the overseas enterprises do not engage in any economic activities in China. The issue is similar. It could be hard to convince MOFCOM that, even the overseas enterprise (target) is not active in China when it is acquired, the target will not engage in any economic activities in China in the future.

Therefore, as MOFCOM’s attitude towards Article 2(4) and (5) tends to be conservative, if one wants to apply simplified procedure based on Article 2(4) and (5), s/he may need to be prudent.

III. FUTURE TRENDS

From the legislative perspective, it can be expected that with the issuance of the Revised Measures as well as other guidelines, the legal certainty of MOFCOM’s merger review enforcement will be further increased.

From MOFCOM’s practice in merger control, based on the above observations, first of all, MOFCOM continued to publish a series of punishment decisions regarding failure to notify in 2016. In the future, MOFCOM may further strengthen the enforcement to illegal failure to notify. The punishment for failure to notify may be more severe.

Second, it seems that MOFCOM’s requirements regarding the quality and formality of the notification documents tend to be stricter recently. If the notifying party(s) fails to satisfy the requirements, MOFCOM may ask the notifying party(s) either (i) to provide the information required in supplemental questions; or (ii) to withdraw. In the foreseeable future, this trend may continue.

Third, for simplified cases, it seems MOFCOM tends to be cautious about applying the simplified procedure to prevent the parties’ abuse. This tendency may also continue in the foreseeable future.

IV. CONCLUSION

Given the above, for practitioners, from the legislative perspective, legal certainty of MOFCOM’s enforcement will be further increased. In particular, when MOFCOM deals with high profile cases, close and frequent communication and cooperation between MOFCOM and other major jurisdictions will benefit the consistency of the outcome of a notification in different jurisdictions.

According to our observation of MOFCOM’s recent practice and anticipation of MOFCOM’s future enforcement trend, it is important to follow its rules. In particular:

First, for a concentration which reaches the turnover thresholds, it is advisable to notify the concentration and obtain MOFCOM’s approval before implementing the concentration. Not only because MOFCOM maintains the practice of publishing its punishment decision regarding failure to notify, but also, MOFCOM’s Deputy Direct General clearly emphasized that MOFCOM will further strengthen the investigation towards failure to notify in the future.

Second, it is advisable to follow MOFCOM's formality requirement and improve the quality of the notification form, which seems to be stricter than before.

Third, for one who wants to apply for simplified procedure, s/he should pay attention to the following three issues: (i) whether there exists neighboring market(s) in this transaction and, if yes, whether the market share of the relevant product in the neighboring market(s) exceeds 25 percent; (ii) whether the relevant product market defined in the notification form can be further segmented and, if yes, whether the market share of the relevant product in the segmented market still qualifies the criteria provided by Article 2(1), (2) and (3) of the Simplified Notification Guidelines; and (iii) whether Article 2(4) and (5) will be accepted by MOFCOM if there is no solid evidence showing that the new JV or the overseas target will not have any economic activities in China in the future.

