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China Merger Control: New Carrots and a Bigger Stick

China has recently taken two important steps to improve its merger control process: providing additional guidance on its new simplified merger procedures while promising publication of decisions penalizing firms for closing deals without first obtaining official approval.

Under China's Anti-Monopoly Law (AML), parties entering into concentrations such as mergers, acquisitions and joint ventures must obtain clearance from the Anti-Monopoly Bureau of the Ministry of Commerce (MOFCOM) prior to implementation so long as certain revenue thresholds are met.[1] Prior to this year, all transactions received the same standard of review from MOFCOM, regardless of whether a deal would be likely to pose material concerns from a competitive or industrial policy perspective.[2] Because simple and complex transactions were treated alike, review of even no-issue cases routinely extended well into China's Phase II, lasting four or five months. Anecdotal evidence suggests that, in part as a result of these long review periods,[3] an increasing number of firms simply elected not to file. Failure to file when required exposes firms to fairly limited financial penalties (up to a maximum of RMB 500,000, or about US$80,000) but also can result in an order by MOFCOM to unwind the transaction and divest shares or assets.[4] In addition, given MOFCOM's other roles in supervising foreign investment and approving business licenses, the reputational damage of a failure to notify could have significant detrimental effects on a company's practical ability to do business in China.

As discussed in our previous memorandum,[5] in February 2014 MOFCOM introduced new interim provisions for qualifying cases for "simplified" merger review (the Interim Provisions).[6] However, lacking procedural guidance, the Interim Provisions left

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1 Under the Provisions of the State Council on the Thresholds for Declaring Concentrations of Undertakings, parties must file with MOFCOM where at least two of the firms involved have individual sales to Chinese customers of at least RMB 400 million (about US$65 million) in the preceding year, and either the parties' aggregate worldwide revenue exceeds RMB 10 billion (about US$1.6 billion) or the parties' aggregate turnover in China exceeds RMB 2 billion (about US$322 million).

2 Under AML Art. 27(5), MOFCOM is explicitly empowered to consider not only competition concerns but also those relating to national economic development and industrial policy.

3 Certain evidence also suggests that domestic Chinese firms, and particularly large Chinese state-owned enterprises, have not notified qualifying transactions at the same rate as international firms, likely due to at least to the perception that the risks of prosecution for failure to file would be lower. *See* Yan Sobel, *Domestic-to-Domestic Transactions – A Gap in China's Merger Control Regime?*, Antitrust Source, Feb. 2014.

4 AML, Art. 48.

5 *See* Skadden, *China Introduces Simplified Merger Review Provisions to Bring Process Improvements Over Time* (Feb. 2014).

6 Under the Interim Provisions, a transaction may qualify for the simplified review procedure if: (i) the parties' shares in an overlap market are less than 15 percent; (ii) the parties' shares in an upstream or downstream market are less than 25 percent; (iii) the parties' shares in other adjacent markets "related to the transaction" are less than 25 percent; (iv) the transaction involves a joint venture outside of China that will not engage in business activities in China; (v) the transaction involves acquisition of a firm outside of China that will not engage in business activities in China; or (vi) the transaction involves a business moving from joint control to sole control by a prior parent.

many questions open as to how this qualification would be implemented and what practical effects could be expected. MOFCOM has now supplemented the Interim Provisions with its Guidelines for Notification of Concentration of Undertakings Under Simplified Merger Review Procedure (the *Guidelines*). The Guidelines, published on April 18, 2014, on a trial implementation basis, help to answer some (but not all) of the questions raised by the Interim Provisions.

Under the Guidelines, parties seeking to use the simplified review procedure may (but need not) engage in prior consultation with MOFCOM to ascertain whether a transaction is likely to qualify.[7] While consultation is not mandatory, application for acceptance under the simplified review procedure is,[8] meaning that parties must affirmatively apply to MOFCOM to receive the benefits of the simplified procedure — MOFCOM will not move a transaction into the simplified review procedure *sua sponte*, even if the review criteria are otherwise present.

Notification pursuant to the simplified review procedure will not differ significantly from that required for ordinary cases. While information relating to demand and supply structure, market entry, horizontal and vertical cooperation agreements, and possible efficiencies can be dispensed with, the documentary burdens, corporate formalities, and detailed share information and competitive assessment (the most labor-intensive parts of preparing a notification) have been retained.[9]

After review by MOFCOM, and supplementation if necessary, the Anti-Monopoly Bureau will make a determination as to whether the case can be accepted under the simplified review procedure.[10] As part of the application, parties must also for the first time prepare a public notice setting forth limited details relating to the transaction, including a short overview of the deal, a brief introduction of the parties, and the grounds for applying for the simplified review procedure. This notice will be made available on MOFCOM's website for ten days for review and comment.[11] As a result, application for consideration under the simplified review procedure will now make the existence of a transaction public before closing — prior to this (and as will still be the case for ordinary review) MOFCOM has not made (and has not been obliged to make) public any of its decisions, except for its 22 conditional approvals and single prohibition.[12]

During the period of public comment, any third party may submit written comments to MOFCOM regarding whether the transaction should qualify for the simplified merger review. Objections must be supported by evidence, which must be verified by MOFCOM.[13] In the case of a verified objection, MOFCOM will give the notifying parties the opportunity to be heard before making a final determination as to whether to withdraw the notification.[14]

The Guidelines provide a helpful framework that explains the shape of the new qualification process for the simplified review procedure. Unfortunately, they do not provide still-needed guidance on the simplified review procedure itself. As a result, key questions, such as those relating to how long the simplified review is expected to take and the degree to which the simplified review will be able to

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7 Guidelines, Art. 1.

8 *Id.,* Art. 2.

9 *See id.* Art. 3.

10 *Id.* Art. 7.

11 *Id.* Art. 8.

12 MOFCOM has also begun publishing a quarterly list of transactions approved, identifying them by parties' name only, but this simple list comes by necessity long after a deal's closing and therefore presumably has little effect on confidentiality regarding the existence of a deal.

13 Guidelines, Art. 9.

14 *Id.* Art. 10.

minimize or eliminate the time-consuming interagency review procedures for ordinary cases, have not yet been answered.

Nevertheless, the advent of the new simplified review procedure should give firms added incentive to notify transactions in a timely manner and, if the carrot does not prove sufficiently sweet, MOFCOM also has unveiled a newly improved stick to convince still-hesitating companies. On March 20, 2014, MOFCOM announced that, effective May 1, it will begin publicizing its decisions penalizing parties that have closed notifiable transactions in advance of MOFCOM approval.[15] MOFCOM also provided a "hotline" to help third parties report any transactions they believe should have been notified.[16]

MOFCOM has never before published any decisions finding an infringement of the AML for a failure to notify, although it has privately contacted parties involved in suspected noncompliant undertakings in the past either to verify that the thresholds were not met or, if they were, to require filing and any necessary rectification efforts. The historically confidential nature of these decisions has made it difficult to obtain reliable information regarding when MOFCOM is likely to act for a failure to file and what penalties it has imposed. Publication of such decisions going forward will provide firms with better information in undertaking their filing analyses.

These two developments signal MOFCOM's continued dedication to improving its merger control process. Nevertheless, without detailed guidance and practical experience in the functioning of the new simplified review procedure, careful and meticulous planning will remain necessary to navigate the sometimes perilous paths of Chinese merger control.

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15 *See MOFCOM to Announce Administrative Penalty Decisions Against Non-Compliant Undertakings*, available at: http://www.gov.cn/xinwen/2014-03/20/content_2642405.htm.

16 The hotline has been established at country code 86 (10) 6529 8998.

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