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The International Comparative Legal Guide to:

Merger Control 2006

A practical insight to cross-border merger control issues

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1 Relevant Authorities and Legislation

1.1 Who is/are the relevant merger authority (ies)?

Under Articles 20 and 21 of the *Provisional Regulations on the Merger and Acquisition of Domestic Companies by Foreign Investors* (the "**Foreign M&A Regulations**"), both the Ministry of Commerce ("**MOFCOM**") and the State Administration of Industry and Commerce ("**SAIC**") are empowered to receive and review merger control filings. The same two agencies also are responsible for approval and registration of foreign investments. Both agencies have been involved in drafting the new Anti-Monopoly Law, which may result in the creation of a separate, new antitrust enforcement agency and/or merger control regime. SAIC also is designated as one of the chief enforcement agencies for China's Anti-Unfair Competition Law.

The extent of each agency's responsibilities and its reviewing standards, methods, and procedures is not clearly set forth in the Foreign M&A Regulations. This lack of clarity presents significant challenges for foreign investors preparing, submitting, and defending merger notification filings.

1.2 What is the merger legislation?

The Foreign M&A Regulations remain the primary legislation regarding merger control. Their requirements are described in detail below.

In addition, a draft Anti-Monopoly Law remains unfinished after numerous revisions over many years. It must be approved by the State Council and the People's National Congress before becoming law. The most current public draft of the Anti-Monopoly Law, dated April 8, 2005 (the "**Draft Anti-Monopoly Law**"), would affect merger control through its regulation of enterprise concentrations in the following situations:

- merger of one or more undertakings into one existing or new enterprise;
- acquisition of 20% or more voting shares or substantial assets of one or more other undertakings;
- acquisition of control through entrusted operation or joint venture;
- acquisition of direct or indirect control of the business operation or personnel matters of one or more other undertakings; and
- acquisition of control of one or more other undertakings by contract or technology transfer.

A concentration of enterprises that "eliminate(s) or restrict(s) competition, damage(s) the interests of consumers, or endanger(s) the public interest" would be considered "monopolistic conduct," and would therefore fall under the scope of the Draft Anti-Monopoly Law.

Furthermore, a pre-merger notification would have to be filed with the Anti-Monopoly Authority if certain thresholds are met with. These jurisdictional thresholds are similar to those provided by the Foreign M&A Regulations (see question 2.3), though the Draft Anti-Monopoly Law includes the total value of the transaction and a party's aggregate worldwide assets as additional thresholds to be taken into account.

1.3 Is there any other relevant legislation for foreign mergers?

Foreign mergers are subject to multiple laws and regulations in respect of foreign investment issued by various government authorities at different levels, in addition to the Foreign M&A Regulations. Two of them have specific provisions regarding merger control. One is the *Regulation on the Merger and Division of Foreign Investment Enterprises* (issued on Nov. 22, 2001), which applies to mergers between or division of types of foreign investment enterprises ("**FIEs**") and authorises MOFCOM to hold a hearing in case it believes the FIE merger will result in a monopoly. The other is the *Interim Regulations for Restructuring State Owned Enterprise with Foreign Investment* (issued on Nov. 8, 2002), which generally stipulates that the approval authority shall organise a hearing before issuance of its approval if the transaction may lead to market monopoly or impair fair competition.

However, both of them fail to give details on merger control.

1.4 Is there any other relevant legislation for mergers in particular sectors?

The *Interim Regulations on the Refrainment of Price Monopolistic Activities* issued by the State Reform and Development Committee ("**SRDC**") on November 1, 2003 focuses on regulating price monopolistic activities among business operators through collusion, abuse of dominant market position or manipulating market-oriented price.

2 Transactions Caught by Merger Control Legislation

2.1 Which types of transaction are caught - in particular, how is the concept of "control" defined?

The Foreign M&A Regulations deal with several types of transactions that involve foreign investors, including so-called "onshore" and "offshore" transactions. Onshore transactions, which involve a foreign investor and a domestic company, include both equity and asset related transactions.

Equity transactions ("**Shareholder M&As**") include agreements in which a foreign investor purchases shareholding rights from a shareholder, or subscribes to an additional capital increase of a domestically-invested enterprise, resulting in the establishment of a foreign-invested enterprise.

Asset transactions ("**Asset M&As**") include agreements in which a foreign investor establishes an FIE to purchase and operate the assets of a domestic company, or agreements in which foreign investors purchase the assets of a domestic company and then establish an FIE to operate the assets.

However, several types of onshore mergers and acquisitions are not allowed, particularly those that result in complete shareholder control by a foreign investor in industries in which foreign investors are not permitted to operate wholly foreign-owned enterprises ("**WFOEs**"), according to the Catalogue Guiding Foreign Investment in Industry. In addition, Chinese majority control must be maintained though the merger or acquisition for those industries in which it is required.

As written, the Foreign M&A Regulations may not cover transactions undertaken by pre-existing FIEs, although they instead may be covered by other foreign investment-related regulations without antitrust review mechanisms.

Offshore transactions, which refer to M&A transactions between foreign companies, are mentioned in the Foreign M&A Regulations, but the scope of their application is not explicitly defined. If interpreted broadly, any transaction between foreign companies with a significant effect on China, meeting the appropriate jurisdictional thresholds (listed under question 2.5), would come under MOFCOM and SAIC authority.

Under Article 24, the Foreign M&A Regulations also cover direct acquisitions by foreign investors of equity interests in existing FIEs, to the extent that such transactions are not governed by separate regulations relating to the transfer of stakes in FIEs. Article 24 also states that the regulations cover transactions involving foreign investor-owned China holding companies (in Chinese legal parlance, "**foreign investment companies**") and domestic enterprises.

Transactions that do not fall within these defined categories do not appear to be covered by the regulations.

2.2 Are joint ventures subject to merger control?

Joint ventures are subject to merger control under the Foreign M&A Regulations if they involve foreign parties and fall within the applicable jurisdictional thresholds for either onshore or offshore transactions (see question 2.3).

2.3 What are the jurisdictional thresholds for application of merger control?

The thresholds for mandatory reporting are different for onshore and offshore transactions. Some thresholds relate to the size of the parties and their affiliated enterprises as measured by business turnover, cumulative annual number of acquired businesses, market share, or size of assets. Others relate to the effect of the transaction on market concentration as measured by combined market share. Each applicable threshold independently will trigger mandatory merger notification and approval.

For onshore transactions, Article 19 of the Foreign M&A Regulations provides four independent thresholds requiring merger notification and review:

- one party (if foreign, including affiliates) has in one year a China business turnover exceeding RMB 1.5 billion (approximately USD$181 million);
- one party (if foreign, including affiliates) has in one year acquired more than ten domestic enterprises in related industries;
- one party's (if foreign, including affiliates') China market share already has reached 20%; or
- as a result of the transaction, one party's (if foreign, including affiliates') China market share will reach 25%.

If one of the conditions listed above exists, and MOFCOM or SAIC believe that the transaction may cause excessive concentration in the domestic market, impede or disturb rightful competition, and harm the benefits of domestic consumers, then MOFCOM and SAIC may jointly or separately convene the appropriate departments, institutions, enterprises, and other concerned parties for a public hearing within 90 days of receiving all of the required documentation. Afterwards, MOFCOM and SAIC will decide whether to approve or reject the M&A application.

Even if one of the above conditions does not exist, a foreign investor must report the M&A transaction to MOFCOM and SAIC upon the request of domestic enterprises with probable competitive relationships, relevant authorities, or industry associations, if MOFCOM or SAIC believe that the foreign investor's M&A will involve a very large market share, or there are factors that will seriously influence market competition, the national economy, the livelihood of the people, or other similar interests.

It should be noted that, unlike in some other jurisdictions, transaction size itself is not relevant to the mandatory notification thresholds for onshore transactions. Thus, for example, a transaction in a small and economically insignificant industry still may require antitrust notification and review if the parties' combined market share will exceed 25%.

For a discussion of the jurisdictional thresholds for overseas or "offshore" M&A transactions, see question 2.5.

2.4 Does merger control apply in the absence of a substantive overlap?

Yes, merger control may apply even if market share is unaffected and there are minimal competition concerns. The jurisdictional thresholds regarding onshore M&A

transactions between foreign investors and domestic companies also include turnover in the Chinese market. In the case of offshore transactions, other factors include total assets held in the PRC by one party, turnover in the Chinese market, and the number of FIEs in related industries within which a party in the transaction either directly or indirectly holds shares.

2.5 In what circumstances is it likely that transactions between parties outside your jurisdiction ("foreign to foreign" transactions) would be caught by your merger control legislation?

In the case of overseas or "offshore" M&A transactions, which involve only foreign companies, the merging or acquiring party must submit the merger or acquisition plan to MOFCOM and SAIC (either before the public announcement of the plan or at the same time the plan is submitted to the regulatory authorities of the country within which the M&A is taking place) if one of the following conditions occur:

- one party of the offshore M&A holds assets in the PRC worth more than RMB 3 billion (approximately USD$362 million);
- one party of the offshore M&A has a turnover in the Chinese market worth more than RMB 1.5 billion (approximately USD$181 million) in the current year;
- the market share of one party of the offshore M&A and its affiliated enterprises has reached 20 per cent in China;
- the market share of one party and its affiliated enterprises will reach 25 per cent in China as a result of the offshore M&A; and
- the number of FIEs in the relevant domestic industry within which one party to the transaction holds shares (either directly or indirectly) will exceed 15 as a result of the offshore M&A.

MOFCOM and SAIC will then either issue an approval or disapproval of the transaction upon determining whether the M&A will cause excessive concentration in the domestic market, impede or disturb rightful competition, or harm the benefits of domestic consumers. Exemptions from plan submissions for offshore M&A transactions are identical to those for onshore transactions (see question 3.2).

For offshore transactions, the scope of potential reporting obligations is even broader. The Foreign M&A Regulations may require reporting of transactions even if they have no competitive effect in China, so long as one party's China market share, business turnover, or assets exceed the threshold limits. Further, many terms listed in these jurisdictional thresholds are undefined, and MOFCOM tries to encourage parties to report when there is any doubt by interpreting those undefined terms broadly.

2.6 Please describe any mechanisms whereby the operation of the jurisdictional thresholds may be overridden by other provisions.

The Foreign M&A Regulations include a provision covering exemptions to the jurisdictional thresholds for onshore and offshore M&A transactions (see question 3.2).

3 Notification and its Impact on the Transaction Timetable

3.1 Where the jurisdictional thresholds are met, is notification compulsory and is there a deadline for notification?

For both onshore and offshore M&A transactions, if the jurisdictional thresholds for reporting the M&A plan to MOFCOM and SAIC are met, then notification to MOFCOM and SAIC is compulsory.

The Foreign M&A Regulations do not specify a time period within which the parties to a transaction must report an onshore transaction meeting the reporting thresholds. However, they must submit their merger filings (and perhaps evidence of clearance) in order to obtain foreign investment approval and registration.

The regulations expressly require that the parties to a reportable offshore transaction notify MOFCOM / SAIC of their merger plan before it is publicly announced or at the same time that it is submitted to regulators in the country in which the transaction will occur. However, as indicated by oral consultations with MOFCOM officials, notification of offshore M&A transactions in practice may occur within 7 days after the submission to regulatory officials in the country within which the M&A occurs.

3.2 Please describe any exceptions where, even though the jurisdictional thresholds are met, clearance is not required.

Under Article 22 of the Foreign M&A Regulations, the parties to a reportable transaction may seek an exemption from regulatory review if the transaction "can improve conditions for fair market competition," "restructures loss-making enterprises and assures employment," "introduces advanced technologies and managerial talent and improves the enterprise's international competitiveness," or "can improve the environment."

Interpretation of these exceptions is reserved to substantial administrative discretion of MOFCOM / SAIC on a case by case basis.

3.3 Where a merger technically requires notification and clearance, what are the risks of not filing?

The Foreign M&A Regulations do not provide a mechanism for penalising non-compliance with their merger reporting or other requirements. There is no express authorisation for MOFCOM/SAIC to seek the reversal of a transaction that was not properly reported for merger review. Thus it is unclear whether any such non-compliance might result in administrative or civil fines, a cease and desist order, rescission or unwinding of a transaction, or even criminal penalties, although all are possibilities. MOFCOM believes the new merger control regime to be enforceable on its face and already has received many filings for merger clearance. It does not appear that any parties have been publicly penalised for non-compliance.

In order to obtain foreign investment approval and registration for onshore transactions, however, Articles 12 and 15 of the Foreign M&A Regulations require that the

parties submit their merger filings (and perhaps evidence of antitrust clearance) to the foreign investment approval authorities. With regards to offshore M&A, China affiliates of the offshore M&A parties may need to go through formalities with original approval and registration authorities for change of names, directors, legal representatives etc. due to offshore M&A. Accordingly, if the relevant authority determines that a transaction should have been reported for antitrust review, it may simply refuse to approve or register the transaction or change, rendering it legally ineffective even if consummated by the parties. In extreme cases, the authorities could issue rectification orders and even suspend or revoke the business licence of the relevant FIEs.

3.4 Is it possible to carve out local completion of a merger to avoid delaying global completion?

Generally speaking, parties may not carve out the Chinese aspects of a reportable transaction once the jurisdictional thresholds are met unless exemption is obtained. However, later anti-trust application in China may not necessarily delay the global completion of an offshore M&A transaction, because (i) notification for offshore M&A transactions can occur within one week of filing with the authorities for the country in which the M&A is taking place; and (ii) the Foreign M&A Regulations are silent on consequence of non-compliance though potential enforcement risk exists (see question 3.3).

3.5 At what stage in the transaction timetable can the notification be filed?

For both onshore and offshore M&A, the Foreign M&A Regulations do not specify at what stage in the transaction timetable the notification shall be filed. However, with regards to onshore M&A, evidence of clearance may be a necessary document for new FIEs' approval and registration. In addition, the Foreign M&A Regulations expressly require that the parties to a reportable offshore transaction notify MOFCOM/SAIC of their merger plan before it is publicly announced or at the same time that it is submitted to regulators in the country in which the transaction will occur.

3.6 What is the timeframe for scrutiny of the merger by the regulatory body? What are the main stages in the regulatory process?

The only required process is set forth in Article 20 of the Foreign M&A Regulations, which provides that, for onshore transactions, MOFCOM / SAIC may first determine that a transaction "might cause excessive concentration in the domestic market, impede or disturb rightful competition, and harm domestic consumers' benefits," in which case the ministries will "jointly or separately convene the appropriate departments, institutions, and enterprises as well as other concerned parties for a public hearing within 90 days of receiving all requisite documents." After this hearing, MOFCOM / SAIC "will then decide whether to approve or reject the application according to law." No similar procedure is provided for offshore transactions, which are not explicitly barred from closing pending merger review.

Without implementing rules, the Foreign M&A Regulations do not make regulatory compliance and deal planning easy. There are many potential opportunities for extra-competitive concerns and administrative discretion to enter and affect the review and decision processes. Moreover, given the absence of clear procedures and timing, there is no way accurately to predict how long merger review may take. For example, the regulations themselves do not specify:

- how MOFCOM / SAIC make the preliminary determination that the transaction is of competitive concern and requires a hearing;
- whether and how the parties may provide information and argue their case prior to such preliminary determination;
- what "requisite documents" are to be provided by the parties;
- what information may be provided by or required of third parties;
- the timeline for MOFCOM/SAIC to request and parties to provide documents or information;
- how MOFCOM/SAIC determine what governmental departments, institutions, enterprises and concerned parties may participate in the hearing;
- the procedures for conduct of the hearing itself;
- the timeline for MOFCOM/SAIC to make their final determination; and
- what legal principles, arguments, and analytical methods MOFCOM/SAIC will consider in the review process.

This is compounded by a lack of clarity regarding the division of reviewing responsibilities between MOFCOM and SAIC. There is no assurance that the two agencies will employ consistent and transparent review standards. Thus, China's merger review process may present formidable challenges for foreign investors whose transactions require notification and review.

In practice, however, MOFCOM has taken a more active role in enforcement of the merger control requirements of the Foreign M&A Regulations, has made available a basic outline of the information required of reporting parties (see question 3.8), and has established a procedure by which filings will be "deemed" approved if MOFCOM takes no action within thirty (30) days of its formal acceptance of a merger control filing.

3.7 Is there any prohibition on completing the transaction before clearance is received or any compulsory waiting period has ended?

No, such prohibition is not in place in the Foreign M&A Regulations. However, M&A transactions possibly may not be completed due to lack of other regulatory clearance as discussed in question 3.3. The Draft Anti-Monopoly Law provides that business operators will be prohibited from completing the transaction within 45 days of receipt of the concentration review documents by the Anti-Monopoly Authority.

3.8 Where notification is required, is there a prescribed format?

Although there are prescribed forms to apply for an onshore

asset or shareholder M&A transaction, no forms exist for notification of either onshore or offshore M&A transactions to MOFCOM and SAIC if the appropriate jurisdictional thresholds are met. In practice, the government ministries (particularly MOFCOM) have requested that merger review filing include some or all of the following: (1) introductions to the parties and their affiliates; (2) a description of the transaction, the affected industries, and the business rationale for the transaction; (3) a summary of the merger or acquisition agreement; (4) financial information for each party; (5) China sales turnover and market share information for each party in relevant markets; (6) description of the competitive situation, the parties' largest competitors, and the competitive effects of the transaction in China; (7) filing requirement and status in other jurisdictions; and (8) other information the parties wish to submit. The precise information required will likely vary in each case. MOFCOM sometimes has made one or more additional requests for information after submission of an initial notification filing, and does not consider a filing complete until all subsequent information requests have been satisfied.

3.9 Who is responsible for making the notification and are there any filing fees?

In the case of an overseas M&A transaction, the merging or acquiring party is responsible for submitting the merger or acquisition plan to MOFCOM and SAIC if the jurisdictional thresholds for such a report have been met. In the case of an onshore M&A transaction, the foreign investor must report the situation to MOFCOM and SAIC if the jurisdictional thresholds have been met. In practice, the two parties often file a notification together.

The Foreign M&A Regulations make no mention of a filing fee.

4 Substantive Assessment of the Merger and Outcome of the Process

4.1 What is the substantive test against which a merger will be assessed?

In addition to the jurisdictional thresholds that, if met, require a foreign investor to report the situation to MOFCOM and SAIC, the appropriate authorities will consider whether (i) the merger or acquisition might cause excessive concentration in the domestic market; (ii) impede or disturb rightful competition; or (iii) harm the benefits of domestic consumers. These factors are all taken into account in the determining whether an onshore or offshore M&A transaction should be approved or rejected.

4.2 What is the scope for the involvement of third parties (or complainants) in the regulatory scrutiny process?

Third party involvement can impact the clearance requirements for onshore M&A transactions. Even if one of the jurisdictional thresholds are not met (see question 2.3), a foreign investor can be required to submit a report to MOFCOM and SAIC at the request of a domestic competitor or probable competitor, relevant authorities, or industry associations. If MOFCOM and SAIC find it necessary (see question 4.1), then those authorities have the power to jointly or separately convene the appropriate departments, institutions, and enterprises as well as other concerned parties for a public hearing, after which the authorities will decide whether to approve or reject the transaction.

4.3 What information gathering powers does the regulator enjoy in relation to the scrutiny of a merger?

The Foreign M&A Regulations do not explicitly mention any information gathering powers aside from the required reports and documentation.

However, the most Draft Anti-Monopoly Law specifies the inspection powers which the Anti-Monopoly Authority possesses, including searches, requisition of documents and information, inquiries about financial information, and closing down the concerned business locations. The Anti-Monopoly Authority would also hold the power to fine if the person under investigation refuses to submit information or submits fraudulent information

4.4 During the regulatory process, what provision is there for the protection of commercially sensitive information?

The Foreign M&A Regulations do not include any provisions regarding the protection of commercially sensitive information. In theory, the approval and registration authorities have complete discretion over whatever merger control information is to be released by the government, which has caused concern from applicants.

The issue seems to have attracted the attention of the government, as the Draft Anti-Monopoly Law includes a provision regarding confidentiality, stating that the "Anti-Monopoly Authority and its staff shall keep confidential the commercial secrets obtained during the investigations."

5 The End of the Process: Remedies, Appeals and Enforcement

5.1 How does the regulatory process end?

According to the Foreign M&A Regulations, the application process ends for onshore transactions after the FIE Approval Certificate and the FIE business license are issued by the approval and registration authorities. However, if the jurisdictional thresholds in which the situation must be reported to MOFCOM and SAIC are met, then the regulatory process for onshore and offshore transactions technically ends with a decision of approval or rejection of the transaction after a public hearing. If a public hearing is not ordered within 90 days of the authorities' receipt of all the requisite documents, then the transaction is technically approved. However, in practice, a 30 day period is more realistic; if a public hearing is not ordered and the transaction is not rejected within 30 days of receipt of the documentation, then the transaction is "deemed" approved. Parties typically do not wait for an official indication of approval once the period of inaction by the authorities has exceeded 30 days.

5.2 Where competition problems are identified, is it possible to negotiate "remedies" which are acceptable to the parties?

The Foreign M&A Regulations do not specify any remedies, and because merger control is such a recent concern in China, the issue of negotiated remedies has not publicly come up in practice. However, it may be beneficial to arrange negotiations among the parties and authorities with respect to potential remedies.

5.3 At what stage in the process can the negotiation of remedies be commenced?

The Foreign M&A Regulations make no mention of the remedy issue. If this proves necessary, the parties would likely enter into discussions with MOFCOM and SAIC immediately after notification that there are regulatory concerns with the transaction, since approval otherwise would not be forthcoming.

5.4 How are any negotiated remedies enforced?

The Foreign M&A Regulations make no mention of the remedy issue or of its enforcement. However, the Draft Anti-Monopoly Law stipulates that if the conditions or restrictions in an approval are violated, the Anti-Monopoly authority may declare the concentration void, order the business operator concerned to dispose of all or part of its stock, to transfer part of its business, or impose other necessary penalties, and may also impose fines between RMB 100,000 to RMB 10,000,000 or not exceeding 10% of turnover in the relevant market in the preceding year. If the business operator concerned fails to comply with the foregoing measures prescribed by the Anti-Monopoly Authority, the Anti-Monopoly Authority may order the business operator concerned to dissolve or cease its business operation.

5.5 Will a clearance decision cover ancillary restrictions?

All "ancillary" restrictions contained within the merger agreement would be covered under a decision by the approval authorities, although no guidelines exist in this respect.

5.6 Can a decision on merger clearance be appealed?

Although the Foreign M&A Regulations do not provide for any appeal mechanism, the PRC Administrative Appeals Law (which dictates the particular authorities responsible for administrative review) provide the right for dissatisfied parties to appeal any administrative decision or commence lawsuit proceedings, MOFCOM or SAIC could review their own decisions, as they are the highest merger control administrative authorities. However, dissatisfied parties may technically appeal to the State Council, which oversees MOFCOM and SAIC.

Furthermore, the Draft Anti-Monopoly Law states that interested parties dissatisfied with the Authority's decisions may file for judicial review in an intermediate people's court where the Anti-Monopoly Authority is located.

5.7 Is there a time limit for enforcement of merger control legislation?

There are no regulations regarding time limits for the enforcement of merger control legislation.

6 Miscellaneous

6.1 To what extent do the regulatory authorities in your jurisdiction liaise with those in other jurisdictions?

The Anti-Monopoly Office (recently established by MOFCOM) and MOFCOM itself frequently liaise with foreign antitrust administrative authorities, which is also one of the responsibilities of the future Anti-Monopoly Authority in accordance with the Draft Anti- Monopoly Law.

6.2 Please identify the date as at which your answers are up to date.

July 31, 2005.

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Peter Wang leads Jones Day's antitrust / competition practice in China and its litigation practice in Shanghai.
Peter regularly advises on China- and U.S.-related antitrust / competition issues. He has handled merger control filings in China, as well as significant U.S. government antitrust investigations of proposed mergers and acquisitions, including America Online's merger with Time Warner and Procter & Gamble's acquisition of Clairol from Bristol-Myers Squibb. In addition, he has been involved in a number of antitrust litigation matters, including on behalf of BFGoodrich in connection with its acquisition of Coltec.
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