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“China’s New Anti-Monopoly Law – an analysis of recent decisions regarding foreign investment and trade”

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In August 2008, the long awaited PRC Anti-Monopoly Law came into operation. Since that time, the Chinese Anti-Monopoly Bureau of the Ministry of Commerce, has had to deal with over 30 applications for merger and acquisition approval. As at the date of writing, it has approved many application, and only refused one application - the takeover of Huiyuan Beverages by Coca Cola Beverages. This article analyses a number of the decisions issued by the Anti-Monopoly Bureau, attempting to reconcile the decisions with the law and policy, as well as laying down guidelines for anticipating how the regulator will review an application and the prospects for success.

The Chinese Anti-Monopoly Law

After over 10 years of debate and drafting, China enacted its first ever real Anti-Monopoly Law in 2007, with it commencing operation on 1 August 2008. Article 1 of this law states that it was enacted for the purpose of “preventing and prohibiting monopolistic activities, protecting fair market competition, promoting efficiency of economic operation, protecting the legitimate rights and interests of consumer and social public interests, and promoting the healthy development of socialist market economy.” The law sets out various rules regarding the regulation or prohibition of monopoly agreements, including resale price maintenance, price fixing, and anticompetitive

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supply and market practices¹. Various agreements can be exempted from the prohibition of monopoly agreements, including those that relate to technology development, cost reduction and resources preservation². Chapter 3 of the law deals with abusing a dominant position in a market³. The provisions which we want to focus on for the purposes of this article are set out in Chapter 4 of the law. The other chapters of the law deal with abuse of administrative powers that effect⁴, investigation issues⁵ and legal liabilities⁶. As at the date of writing, we are still awaiting the issue of comprehensive implementing regulations for this law, although various circulars and guidelines have been issued⁷.

Chapter 4 deals with transactions which increase the concentration of undertakings within a market. Transactions involving mergers and acquisitions, share and asset deals, the acquisition of direct and indirect control via various contractual arrangements, are all caught by the law⁸. The law states that if the relevant threshold is met by a proposed transaction, then the parties are required to notify the Anti-Monopoly Bureau within the Ministry of Commerce, prior to the deal being concluded⁹. Clearly, this “threshold” is very important as it determines whether approval is required from the regulator before a deal can be concluded. In August 2009, the State Council issued the Declaration of Concentration of Business Operators, which seems to have defined the relevant thresholds¹⁰:

- The worldwide business volume of all operators involved in the concentration exceeded RMB10billion in the last accounting year, and the business volume in China of at least two operators exceeded RMB400 million in the last accounting year; or
- Business volume in China of all operators involved in the concentration exceeded RMB2billion in the last accounting year, and the business volume in China of at least two operators exceeds RMB400 million in the last accounting year.

If an entity will end up possessing 50% or more of another entity’s sharer or assets, or a third party will end up owning 50% of more of a group of entity’s shares or assets, then subject to the threshold requirements as referred above being met, the entities are required to notify the Anti-Monopoly Bureau and seek approval under this law¹¹.

The Anti-Monopoly Bureau is required to look at the following issues when reviewing an application for approval of a merger or acquisition¹²:

- Market shares of the undertakings participating in the concentration in the relevant market and their ability to control the market;
- Concentration degree of the relevant market;
- Effect of the proposed concentration on market access and technological progress;

¹ Articles 13 and 14 of the PRC Anti-Monopoly Law

² Article 15 of the PRC Anti-Monopoly Law. Also note Article 55 of the law which states that the law is not applicable to intellectual property transactions, provided that those rights are not “abused to eliminate or restrict competition”.

³ Articles 17 to 19 of the PRC Anti-Monopoly Law

⁴ Articles 32 to 37 of the PRC Anti-Monopoly Law

⁵ Articles 38 to 35 of the PRC Anti-Monopoly Law

⁶ Articles 36 to 54 of the PRC Anti-Monopoly Law

⁷ Note the Guiding Opinion on Reporting of Concentrations of Business Operators issued by the Ministry of Commerce on 7 January 2009

⁸ Article 20 of the PRC Anti-Monopoly Law

⁹ Article 21 of the PRC Anti-Monopoly Law

¹⁰ Article 3 of the Declaration of Concentration of Business Operators, State Council, August 2009

¹¹ Article 22 of the PRC Anti-Monopoly Law

¹² Article 27 of the PRC Anti-Monopoly Law. Also note Article 31 of the law which allows the Anti-Monopoly Bureau to also look at national interest issues in addition to pure competition law issues

- Effect of the proposed concentration on consumers and other related undertakings;
- Effect of the proposed concentration on the development of the national economy;
- Other factors determined by the Anti-Monopoly Enforcement Authority under the State Council.

The Coca Cola/Huiyuan Decision

In early September 2008, Coca Cola, the world's largest beverage maker, offered to buy the well known Chinese juice maker, China Huiyuan Juice Group Co., Ltd. ("Huiyuan"), for US\$2.4b (3 times the capitalisation value of Huiyuan). Beijing-based Huiyuan is the largest fruit juice company in China, with an apparent share of over 46 percent in the 100 percent pure juice market in 2007/8, according to ACNielsen figures. It posted sales revenue of RMB2.7 billion (US\$397m) in 2007. Huiyuan was listed on the Hong Kong stock exchange in late 2007.

Coca Colas has been active in China for many years. It was suggested that Coca Cola had well over 70% of the carbonated beverages market in China by various commentators following the case and decision by the Anti-Monopoly Bureau.

Within hours of the deal being announced, local Chinese opposition was beginning to grow. Sina.com was alive with chatter as to the negative effects that this deal would have on the Chinese market and national image¹³:

"BEIJING, Sept. 4 (Xinhua) -- The public was reminded of the sore memories of lost domestic brands when Coca-Cola announced its offer to take over China Huiyuan Juice Group Limited, a Hong Kong-listed company that owns the Huiyuan juice business throughout China.

While Coca-Cola and Huiyuan both seem satisfied with the deal, many ordinary Chinese think otherwise. In an online poll posted by major portal Sina.com, more than 80 percent of the over 76,000 interviewees voted against the acquisition of the leading domestic juice maker. A similar proportion held the opinion that the acquisition, if successful, would verge on a foreign capital's attempt to wipe out domestic pillar brands.

Established in 1992 in east China's Shandong Province, Huiyuan spent years developing its nationwide network and had raised its annual output capacity to 2.2 million tonnes.

Having just been listed among the top 25 domestic brands last year by China Brand Union Association, Huiyuan had the largest share in the Chinese juice market and was the pride of many Chinese as an example of a domestic brand that competes successfully among its international rivals.

"Huiyuan would become a brand under Coca-Cola, which has achieved a major strategic triumph. It will get not only the top brand in China, but also the market. It would take Coca-Cola back to the top of the Chinese beverage market," said brand marketing expert Li Guangdou.

"But it would mean a heavy loss to Chinese domestic brands, which are under severe crisis now," said Li. Though the global beverage maker said it would keep the Huiyuan brand after the acquisition, analysts doubted whether it would give support equivalent to its original juice brand Minute Maid.

¹³ See <http://english.sina.com/business/2008/0904/184005.html>

Their worries are not without reason -- seven years after being sold to multi-national giant Procter and Gamble, the annual production of formerly major domestic brand Panda washing powder was reduced from 60,000 tonnes to 4,000 tonnes, as its new owner set the brand aside and showed more interest in promoting its own labels.

Three major shareholders of Huiyuan are said to have accepted the offer. They held approximately 66 percent of the Huiyuan shares. But the 2.4 billion-U.S. dollar deal still waits government approval.

The application has been sent to the Ministry of Commerce for approval, but the detailed timetable or result has not been disclosed.

According to DLA Piper UK LLP lawyer Liu Cheng, whether the deal would get approval is closely related to its influence in the industry after the acquisition, and whether the Chinese anti-trust law would include the juice market under its regulation.

If the market share of Huiyuan and Minute Maid together exceeds 50 percent, it might pose difficulty in winning approval, said Liu.”

On 18 September 2008, the Coca Cola Company submitted its relevant application materials to the Ministry of Commerce in accordance with the PRC Anti-Monopoly Law. On September 25, October 9, October 16 and November 19, Coca Cola provided supplementary materials as requested by the Anti-Monopoly Bureau. On November 20, the Anti-Monopoly Bureau considered that the materials submitted by Coca Cola “met the standards stipulated in Article 23 of Anti-monopoly Law”. In its decision, the Ministry of Commerce stated that “Because of the large scale and considerable influence of this concentration, the Ministry decided to give the matter further examination and consideration, after completing the initial stage of examination on December 20 2008, and informed the Coca Cola Company in writing.”¹⁴ The examination process was stated to have been completed by 20 March 2009 – exactly 90 days, after the examination time was extended¹⁵.

The crux of the decision was as follows:

- After concentration, Coca-Cola may extend its dominant position in the carbonated drinks market to the fruit drink market, and eliminate existing juice enterprises, limit competition, and damage the lawful rights and interests of consumers.
- Branding is the key factor for influencing effective competition in the beverage market, and after concentration, the Coca Cola Company may markedly enhance its dominance and competitiveness in the market by using its control of the two well-known brands “Meizhiyuan” and “Huiyuan Juice” (both owned by Huiyuan), together with its existing dominant position in the carbonated beverages market and the corresponding effect, would be the concentration will set up barriers to entry for potential competitors to enter the juice drinks market.
- The concentration would narrow the space of domestic small and medium-sized fruit juice enterprises, restrain the domestic enterprises’ ability to carry out independent innovation and competition in the juice drink market, cause adverse effects on effective competition of the Chinese juice and drink market, and generally would not be conducive to the sustainable development of China juice industry development.

¹⁴ Under Article 25, a decision can be issued within 30 days. Under Article 26, this time can be extended to 90 days in the discretion of the Anti-Monopoly Bureau.

¹⁵ Interestingly, the decision issued by the Ministry of Commerce was dated 20 March, but it was issued on 18 March

- Coca Cola could not prove that the concentration would bring more positive effects than negative effects in relation to competition, or that the concentration was in the public interests.

The decision notes that, in typical Chinese government style, Coca Cola was invited to propose a solution to the issues raised above¹⁶. It is not known what further submissions were put forward, but it is known that senior executives from the US personally attended the offices of the Ministry of Commerce in order to put forward their proposals. These proposals were ultimately rejected by the Ministry of Commerce.

Initial reactions from commentators were along the lines of the decision being a purely protectionist decision, given the great politicisation of the transaction that had occurred since September 2008. On the other hand, more recently, well thought out critiques of the decision have begun circulating, pointing out that they could understand such a decision being made, especially if “market” was defined to be the “drinks/beverages market” and not just the “100% juice market” – it may be fair to say that Coca Cola possibly dominates the “non-alcoholic beverages market” in China, and when another relatively strong competitor, with around 50% of a submarket (or 10% of the beverages market) is added to Coca Cola’s fold, concerns must start to arise - indeed in supermarkets in China, juices and carbonated beverages are generally sold side by side. However, it seems to us that the decision did not actually define the “market” as the non-alcoholic beverages market, but did impliedly define it as the 100% fruit juice market – the problem with this analysis, is that looking at the market concentrations in this market, it seems very difficult to conclude that the concentration would be enough to have an adverse effect on competition within such a market – it is necessary to assume that once the deal was complete, Coca Cola would engage in anticompetitive practices, such as product tying, exclusive agreements, and others, in order to try to reduce competition as much as possible, in order to be able to rationalise the decision by the Ministry of Commerce. It is submitted that the Ministry of Commerce was wrong in making these assumptions – indeed, it could have approved this transaction, and then used its powers to clamp down on such anticompetitive behaviour, when or if, it arose in the future. As far as we know, Coca Cola has not elected to appeal this decision.

The InBev/Anheuser Busch Decision

On 13 July 2008, Belgian beer giant InBev (the owner of Stella Artois) and US based beer giant Anheuser Busch (the owner of Budweiser) announced that InBev was to buy Anheuser Busch for US\$49.91b. Given both entities held interests in large Chinese based breweries, as well as them owning around 13% of the beer beverages market in China, the transaction would need approval from the Ministry of Commerce under the PRC Anti-Monopoly Law for concentrating those Chinese assets. At that time, Anheuser Busch owned 28.56% of Tsingtao (China’s second largest brewery) and InBev had a 29% in Zhujiang Brewery (China’s fourth largest).

On 10 September 2008, InBev submitted its application materials to the Ministry of Commerce. On 27 October 2008, the Ministry of Commerce accepted the application and began consideration of the matter. On 18 November 2008 (less than 30 days from acceptance), the Ministry of Commerce issued its decision in this case, approving the transaction, subject to the merged entity:

- Not increasing Anheuser Busch’s existing 27% equity share in Tsingtao Brewery, subject to gaining approval;
- Not increasing InBev’s existing 28.56% equity share in Zhujiang Brewery, subject to gaining approval; and
- Not purchasing any stake in China Resources Snow Breweries and Beijing Yanjing Brewery, two of China’s largest domestic brewers, subject to gaining approval.

¹⁶ This was rumoured to involved an agreement by Coca Cola to sell of the “Meizhiyuan” and “Huiyuan Juice” brands after the deal was completed.

Once again, we see that the Ant-Monopoly Bureau and the Ministry of Commerce wanted to focus on what could happen in the future, rather than focussing on the facts before it. It approved the transaction, but wanted to lay down guidelines so that the new entity could not look at carrying out potentially anticompetitive activities in the future. This practice of predicting the future is interesting, and most likely disproportionate and unnecessary. The US Federal Trade Commission used to follow similar practices, but stopped doing so in 1995, given that it was realised that any future activities would involve automatic filing and approval any way under the relevant antitrust legislation, thus it was redundant to refer to such future obligations in its decisions. The fact that this transaction was approved as not surprising, given the low direct market shares of the parties, but the conditions imposed when granting approval, served as a warning to future applicants that the Ministry of Commerce and Anti-Monopoly Bureau were taking its obligations very seriously and looking to make its presence felt within the international community. Some would say that what happened next, in the Coca Cola/Huiyuan case, should not have caused such a surprise.

The Mitsubishi/Lucite Decision

On 11 November 2008, Lucite International Group Ltd. announced that it had agreed to a US\$1.6 billion cash takeover by Japan's Mitsubishi Rayon Co. Ltd., which would give the Japanese company ownership of the perspex and lucite acrylic plastic brands. This transaction is to make Mitsubishi the world's biggest manufacturer of methyl methacrylate monomers ("MMA"), a key material in products ranging from liquid crystal display television screens and mobile phones to kitchen tops and automobile headlights. Both Mitsubishi Rayon and Lucite have sales and manufacturing operations in China, thus the jurisdiction of the Chinese Ministry of Commerce and Anti-Monopoly Bureau has been attracted - their sales within China exceeded around US\$60 million in the last 12 months, according to government sources. Mitsubishi Rayon has already invested US\$230 million in three synthetic fibre ventures in China. According to announcements issued by Lucite, it is said that Lucite International has a large MMA plant in China, with a total investment of US\$1.12 hundred million, and a current capacity is 93,000 t/a (which can be doubled without any need to increase investment). Indeed both parties' China plans are well developed in terms of manufacturing, sales and distribution, but commentators have claimed that the merged entity would possess a non-dominant market share in China, being around 40% of the MMA market.

As at 15 April 2009, the transaction had received approvals from the antitrust regulators in all relevant jurisdictions (including Taiwan), except for China. This led to concerns being raised that China was going to use the case for political gain or to advance protectionist principles. Government sources confirmed that concerns have been raised by local Chinese MMA manufacturers, as well as customers, as to the potential that this transaction has to lessen competition within the market for MMA. However, the transaction was nowhere near as politically charged as the Coca Cola/Huiyuan transaction.

The decision in this case is anxiously awaited by the parties, lawyers, economists and governments. It is hoped that the law will be applied sensibly in this case, and the concerns of local Chinese entities kept in perspective.

Conclusions

We have together the following snapshot of guidelines to keep in mind when proceeding with an application under the PRC Anti-Monopoly Law, given the decisions referred to above:

- If a major Chinese brand or major Chinese owned technology is involved, I suggest:

- setting up a public relations initiative to assist in alleviating concerns that will be raised by Chinese consumers, competitors and other stake holders
- be prepared to be flexible when dealing with the Anti-Monopoly Bureau, as to structuring via licensing, post merger undertakings and finding compromises or solutions to perceived approval obstacles
- It appears that the time limits set down in the law, for the issuing of a decision, are going to be adhered to by the Anti-Monopoly Bureau – however, it is important to realise that the initial 30 day period, does not commence until the Anti-Monopoly Bureau has officially “accepted” the application
- In the more controversial cases, it will take four months from acceptance of an application, for a decision to be issued
- The Ministry of Commerce is required to publish decisions in which it refuses approval, or issues approval subject to conditions – it is not required to publish decisions which unconditionally approve a transaction, but it will simply notify the parties in such cases
- When preparing the application materials, it is vital to follow the law and relevant circulars issued by the Ministry of Commerce carefully – utilisation of consulting companies, economists, lawyers and accounting firms are a must, as the Anti-Monopoly Bureau expects to receive significant and intricate materials commensurate with the importance of the transaction to the parties – choosing the right business partners is a very important step in setting yourself up for approval
- It is important to anticipate likely adverse reaction (and ultimately, the submissions put forward to the Anti-Monopoly Bureau) once a deal is announced, as the Anti-Monopoly Bureau will listen to that reaction and invite submissions from industry participants – you may or may not get a chance to respond to those submissions
- It is important to put forward submissions regarding future plans and competition safeguards that will be place – give thought to offering suggested conditions that could be referred to in an approval decision issued by the Anti-Monopoly Bureau

As can be seen from the decisions discussed above, obtaining approval from the Anti-Monopoly Bureau for even the most simple and insubstantial deal, is not an easy task at present. In time, it is hoped that the decision making process will become more transparent and predictable.