THE IMPACT OF CHINESE COMPETITION LAW ON MERGER CONTROL: OVERWHELMING DISCRETION OUTWEIGHS THE SPIRIT OF THE LAW

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After its entry into the WTO, China has been obliged to open its markets to foreign enterprise. As a result, mergers and acquisitions have become popular vehicles for foreign investment. Competition law has played an important role in governing the conduct of these transactions by foreign entities. This paper provides a detailed examination of Chinese merger control law and practice, supplemented by published decisions of the Ministry of Commerce. Further, this paper examines whether the abstractness and vagueness of the law allow the authorities too much discretion in their handling of merger applications. This paper also addresses the issue of national security.

Après son accession à l'Organisation mondiale du commerce, la Chine a dû ouvrir ses marchés aux entreprises étrangères. En conséquence, les fusions et acquisitions ont connu un essor dans le cadre d'investissements étrangers. Le droit de la concurrence a été un important facteur de contrôle des transactions effectuées par des entités étrangères. Cet article examine en détail les dispositions législatives et la pratique en ce qui concerne le contrôle des fusions, ainsi que les décisions publiées du ministère du Commerce. En outre, il se penche sur la mesure dans laquelle le caractère abstrait et vague de la loi laisse aux autorités un pouvoir discrétionnaire excessif dans la façon dont ils traitent les demandes de fusion. L'article aborde aussi la question de la sécurité nationale.

1. Introduction

The Chinese Constitution establishes the Chinese economy as a socialist market economy.[2] Accordingly, the Chinese government develops its economic policies with both socialist and capitalist objectives in mind. The legal system reflects these dual impulses. After decades of transitioning from a purely socialist model

to the current system, the authorities realized that one of the keys to economic development is the promotion of efficiency. Therefore, they recognized the need to develop competition policies to promote gradual and stable economic growth.[3] In the meantime, foreign acquisitions of Chinese companies through mergers became a trend after China joined the World Trade Organization. These mergers allowed foreign investors to acquire a proximate and significant presence in the Chinese market.[4] It is not controversial to claim that these factors have shaped China's current merger policy.[5] As it stands, the recently enacted Anti-Monopoly Law (hereinafter "AML")[6] has an immense influence on the merger behaviour of foreign entities doing business in China.

The spirit of the AML, as the name suggests, is to promote and maintain fair competition in the marketplace. The author observes, however, that facilitating China's socialist market economy – especially the operation of State-Owned Enterprises (hereinafter "SOEs") – is a crucial consideration for the authorities when implementing the AML. A detailed examination of the law reveals that the abstractness and vagueness of stated limits on mergers and acquisitions ("M&As") allow the authorities an almost boundless discretion in handling merger applications. In the author's opinion, the government purposely granted this broad discretion to protect SOEs. That is, since different industries have different characteristics affecting SOEs' vulnerability, the law provides leeway for the authorities to respond to those characteristics. The authorities' overwhelming discretionary power inevitably raises the issue of whether the law is a tool used to discriminate against foreign investors. In truth, the spirit of the law may be protecting SOEs or former SOEs from foreign acquisitions rather than promoting fair competition.[7]

The issues surrounding Chinese merger review have important implications for foreign investors looking to enter the Chinese market. Indeed, Chinese merger approval is now often required to close international, multi-jurisdictional deals, including deals involving Canadian entities. Notably, in the 2012 acquisition of Saskatchewan's Viterra Inc. by Glencore, the parties had expected to obtain all regulatory approvals by July of 2012. Canada, Australia, the United States, and New Zealand had all given the go-ahead. However, Chinese approval did not occur until December of that year despite the lack of apparent competition

issues. Moreover, the AML applies based on sales into China and no Chinese establishment is actually required to trigger the application of the AML.[8] As more and more deals hinge upon it, understanding China's competition law and merger review process – and related issues – becomes ever more crucial.

This paper has three main parts. First, I discuss why the AML is drafted in a way that allows the authorities to exercise broad discretion, addressing policy objectives as well as related practical issues. Second, using published (controversial) decisions to illustrate, I discuss how the implementation of the AML's provisions may work against foreign investors. Finally, I briefly cover the National Security Review process, explaining its effects on foreign merger applications. I conclude by summarizing the practical effect of the AML and the key points to which foreign investors should direct their attention.

2. The Nexus between SOEs and the Ambiguity of the AML

China's special and unique market culture plays a major role in preventing Chinese competition law from achieving its supposed purpose. This situation is more apparent in those industries in which SOEs enjoy a leading position.

The provisions of the AML, when compared with other jurisdictions, are purposely drafted in an abstract way to allow the authorities to assess foreign investment applications based on the relevant market's characteristics. The primary consideration may be the ability of the relevant market to deal with foreign entry.

The provisions of the AML, though making reference to other jurisdictions, were drafted with 'Chinese characteristics.' In addition to implementing the provisions from the EU, the law included two new factors: the concepts of "public interest" and "the healthy development of the socialist market economy."

Some terms such as 'control' and 'efficiency' have been incorporated in the provisions, but definitions are not provided in the law nor in the supplementary notice.[9] Furthermore, the AML contains a national security review test to ensure that the national interest will not be harmed. This ambiguity has raised concerns about how the

terms should be defined and how the test should operate. The rationale underpinning the drafting is still under scrutiny.

Another concern is the ambiguity surrounding how the authority weighs the factors stipulated in the law.[10] The published decisions, unfortunately, have failed to provide the reasoning or interpretive methodology supporting their conclusions. This lack of transparency and the unequivocal nature of the drafting leads to a concern about whether the Chinese Authority is using the AML as a tool to deter foreign investment.[11] Foreign investors who hold a moderate view have suggested that it would be difficult for them to assess in advance whether they have complied with the law.[12] The incorporation of National Security Review has accelerated investors' concerns as to whether political factors would be taken into consideration and whether the law is targeting foreign investors.[13] Therefore, it is worthwhile to understand the objective of the law to assess whether it achieves the stated spirit of the law: fair competition.

3. The Objective of the Law and the Conflicting Reality

China began its economic reform almost twenty years ago. The concept of private property rights has been successfully introduced and implemented in various industries. The legal system in China is still subject to continuous reform. Chinese laws were drafted with reference to analogous statutes of other jurisdictions. However, commentators have always suggested that despite using the laws of other nations as a blueprint, China has promulgated laws that are "socialist with Chinese characteristics."[14]

The AML is not an exception. When making a direct comparison with other jurisdictions, the AML falls short of giving comprehensive coverage in many areas. Nonetheless, Mehra has observed that it is dangerous to make the unwarranted assumption that China shares a similar background with other jurisdictions.[15] Therefore it is important to understand the economic structure of China to understand the drafting of the AML and how the statutory language affects foreign investors entering the Chinese market. The formulation of competition policy is closely affiliated with economic, political and legal contexts in China.[16] The following sections illustrate these factors, including the influence of SOEs, in detail.

A. The importance of promoting the healthy development of SOEs

Article 1 of the AML states the purpose of the law:

> This Law is enacted for the purpose of preventing and restraining monopolistic conducts, protecting fair competition in the market, enhancing economic efficiency, safeguarding the interests of consumers and social public interest, promoting the healthy development of the socialist market economy.[17]

Most of this provision incorporates the typical wording of a competition law aiming to promote fair market competition. However, the latter part of Article 1 referring to the "public interest" and the "healthy development of the socialist market economy" might, in some circumstances, imply contradictions with competition-oriented objectives. For example, in a sector dominated by SOEs, conflicts could arise between free market and socialist objectives.

It is not in dispute that most of the main industries in China are dominated by SOEs, which employ a large portion of the labour force. SOEs are the largest enterprises in China and their coverage extends to a range of prominent sectors such as electricity, railroads, telecommunication and banking.[18] Administrative monopolies are not rare as the government requires factories and wholesalers to use the products or services of selected producers that are affiliated with SOEs or former SOEs that are controlled by the government.[19] With the subsidies and the effect of administrative monopolies, SOEs generally operate inefficiently when compared to private enterprises. Therefore, allowing foreign investors to enter the market would reasonably be expected to enhance efficiency and help the market achieve its market price equilibrium.

Allowing foreign investors to enter the market, however, would likely affect the operation of SOEs. It is clear that competition would extinguish the marginal firms from the market.[20] SOEs, beyond doubt, have played an important role in the Chinese economy, and their collapse would definitely affect the stability of the economy. Such a result would contradict the objective and rationale of AML to promote healthy development of the socialist market economy. Furthermore, the collapse of SOEs would lead to an unemployment problem and

surrounding adverse effects – like inflation – as the price level of effectively subsidized products returns to equilibrium. This result would certainly contradict the objective of safeguarding the public interest.

B. Exemption granted to SOEs

Article 7 sheds some light on whether the authorities would provide the SOEs with exemptions to the AML. Article 7 protects the business operations of SOEs in industries that concern the lifeline of the national economy or national security. It also protects SOEs that enjoy *exclusive* production and sale by law.[21] The word 'exclusive' has a significant implication as it is contradicts the spirit of fair competition.

Some commentators have doubts as to whether the goal of maintaining fair markets can be reconciled with the goal of protecting the operation of SOEs.[22] On many occasions, the two goals conflict with each other, as open competition would threaten the survival of SOEs. Lobby groups advocating for continued protection of state-monopolized industries assert that the current industry rules and laws leave no room for the AML to apply in those sectors.[23] Even if the AML has a role to play, it is at most limited to "safeguard[ing] the competition order in the market."[24] It is not in dispute that Article 7 would provide the platform for the authority to give special treatment to the SOEs that play national security or fundamental economic roles, or to SOEs that enjoy exclusive and monopolistic operation.[25]

Different views have been expressed on this issue. It has been suggested that the stated legislative intent is creating a foundation for perfecting socialist market mechanisms to allocate resources and develop the legal system.[26] In contrast, other commentators are of the view that the enactment of AML is targeting anticompetitive action. However, after comparing the provisions of the above articles with other jurisdictions, it is the author's view that the AML was purposely drafted to be ambiguous so as to grant the authority the discretion to tailor its response to the circumstance and background of the targeted company. This flexibility comes at the expense of certainty and transparency. If the law is implemented in a way that expands the scope of protection to every industry, foreign investors inevitably would face discrimination and disadvantage.[27] In the following sections, I analyze

the substantive test and factors relevant for merger review in order to provide a comprehensive picture of the law's implementation. I also examine the law's effect on foreign investors entering the Chinese market through M&As.

C. The complicated nature of the AML leads to differences in the construction of the law

Another key reason why the law was drafted with loopholes is that the authority does not have the requisite experience in processing merger reviews, in contrast to analogous bodies operating in developed countries.[28] Therefore, the drafting of the law reflects this immaturity and further clarifications are expected. The law was drafted to give the authorities discretion to strike a balance between protecting SOEs and encouraging fair competition. For instance, Article 1 of the AML stipulates that the law is enacted for the purpose of preventing and prohibiting monopolistic conduct, safeguarding fair market competition, improving efficiency of economic operation, and protecting customers. On the other hand, the law states that the legislative intent of the AML also comprises the public interest and promoting the healthy development of the socialist market economy. Article 1 of the AML, surprisingly, has incorporated two potentially contradicting objectives. Where improving efficiency would be done at the expense of harming the healthy development of the socialist market economy, the authority would, in the author's view, place more emphasis on the latter factor.

4. Enforcement Agencies and their Discretion under the Law

Although there are three authorities empowered to implement the AML,[29] Article 51 of the M&A provision[30] gives the Ministry of Commerce ("MOFCOM") the exclusive responsibility to review and make decisions for merger control in transnational trade.[31] This exclusive power to review and publish decisions by exercising discretion, without checks and balances, has led to a lack of certainty and transparency.

A. The operation of the system leads to uncertainty – published decisions' lack of substance

As stated in Article 30 of the AML,[32] MOFCOM is required to publish decisions in relation to foreign mergers. However, the provision only requires MOFCOM[33] to publish a decision and does not stipulate what information should be covered in the published decision. The inevitable effect is that the reviewing process lacks transparency. Furse found that the restraint on the flow of information makes it substantially more difficult for outsiders to understand and anticipate decisions made by MOFCOM.[34] The published decisions illustrate the lack of clarity in the law; for example, it is unclear how substitutability would affect the determination of the relevant product market.[35] Understanding of the law is restricted to the literal wording of the provisions, not to predictable interpretive methodology. In other words, foreign investors have no way of predicting how the law will apply to prospective transactions.

Two controversial decisions, namely the *CocaCola/Huiyuan*[36] and *Missubishi/Lucite*[37] decisions, are only four pages long each. In the first published decision, *InBev/Anheuser-Busch,*[38] MOFCOM only published one and a half pages and did not incorporate information on how it undertook its analysis and the various factors that it considered. The decision lacked substantive analysis of competition within the concerned market.[39] The reasoning was even worse in the *Coca Cola/Huiyuan* decision, where MOFCOM failed to provide a distinct definition of the relevant market, fundamentally weakening the reasoning and the prohibition. These decisions illustrate the concern that MOFCOM has too much discretion regarding foreign merger control and that the present system lacks transparency.

Notwithstanding the fact that economic policy plays an important part in the implementation of the AML, it is still a prerequisite for foreign investors to understand the competition law and the corresponding competition policy to ensure they comply with the articles of the AML. The decision-making process, nonetheless, is less transparent than in other jurisdictions.[40] In the following sections, I discuss the significant provisions that are relevant to foreign mergers and evaluate their impact.

5. The Ambit of the Law – a Vague Boundary

It is important to identify the scope of the law to ascertain whether the law would apply to a specific merger transaction. Foreign business operators should conduct a self-assessment prior to application. However, MOFCOM, when compared with the other competition authorities (in particular, the European Union and the US), has failed to make the AML's boundaries of application clear to the public. This ambiguity always leaves room for MOFCOM to exercise discretion.

The act of "concentration of business operators" has been categorized in Article 20 of the AML. Three types of concentration are subject to the control of the law.[41] The first type is a merger of two businesses. The second and third type, however, are open to interpretation as there are no clarifications on defining the technical terms "control" and "decisive influence."

A. Difficulty in apprehending the concepts of *"control"* and *"decisive influence"*

The AML has not specifically defined what constitutes *control.* It only mentions that majority acquisition would "exert a *decisive influence* on other business operators by control or any means."[42] Without a clear definition of these terms, the public cannot reliably predict the law's implementation, thus affecting the progress of the merger. Some commentators have found that it is unclear how to distinguish an acquisition of control from decisive influence.[43]

In the absence of Chinese Terminology to supplement the terms, Lorenz suggests that it is more convenient to interpret the provision by assuming that the potential for anti-competitive effects from control is stronger than decisive influence, but that both can diminish the market's competition and development.[44]

It is difficult, if not impossible, for outsiders to understand the standards of "control" and "decisive influence." In Furse's view,[45] the wording is unclear and can potentially apply to the establishment of management contracts.[46] In short, without consulting MOFCOM, foreign investors could never be certain whether control and decisive influence exist in a given case. Further, this ambiguity has arguably

been purposefully introduced, as an earlier draft of the AML defined "control" in a more detailed way. Control was originally defined in the draft AML as the ability to exercise decisive influence which would arise where any business operator was able to command a significant influence on the manufacturing and operational business of another.[47] However the draft implementing regulations has not been enacted.

B. Apparent attempt to extend the power of discretion

MOFCOM has attempted to provide an articulate definition of what constitutes "acquisition of control." Article 3 of the draft notification rules[48] stipulated the percentage threshold that would amount to substantial control.[49] However, this definition was eventually removed from the final rules. Harris found that the removal has converted the merger control process into an indeterminate one: it gives more discretion to the authority.[50]

No implication or inference can be drawn to clarify what constitutes control or decisive influence. This could be fatal for foreign investors, as their first step to interpret merger review under the AML is to understand whether the law applies to their type of transaction. The law, however, fails to provide any guidelines to them.

C. Minority share acquisition has not been discussed in the AML

It is not uncommon for foreign investors to acquire minority shareholdings to participate in the Chinese market. This allows them to gather more background information on the market, facilitating a subsequent acquisition. However, the AML has yet to provide sufficient guidelines on whether minority share acquisition is subject to the law.

The draft provision stipulated that if an acquisition, even a minority acquisition, gained the purchaser the ability to nominate directors, finalize financial budgets and make decisions on important issues, it fell within the ambit of the law.[51] The provision mirrored the European Merger Regulation (hereinafter "ECMR")[52] in regarding a minority acquisition as a transfer of control if it allows the purchaser to enjoy the "rights or contracts which confer decisive influence on the composition, voting or decisions of the organs of an undertaking."[53]

However, the definition and the explanation of the phrase "acquisition of control" was omitted from the final version. No other official guidelines have been provided by the Chinese authority. Although it is suggested that MOFCOM may address this crucial issue in the future, the lack of authoritative guidance causes unnecessary uncertainty. Foreign investors could make reference to the provisional draft, but avoiding influence through the provisional factors might be inadequate to avoid the scrutiny of the authority.

D. Attempts to interpret the concept of control by making reference to other Chinese law

Several scholars have made attempts to interpret "control" in the AML. Wu suggests drawing inferences from the Company Law 2005 which has defined both "controlling shareholders" and "actual controller."[54] This approach is shared by Harris who commented that Article 217(1) of the PRC law has provided a potentially useful guidance on the meaning of "control."[55] Furse has also suggested that "control" should not be categorized as the ability to merely exercise material influence, but a considerable ability to exclusively instruct the operations of the acquired entity.[56]

In a recently published circular on the national security review for the acquisition by foreign investor of a domestic Chinese enterprise (the "NSR circular"), "control" was defined for the purpose of the National Security Review process. Article 1(3) of the circular provides that one has *de facto* control if one's post-acquisition shareholding is 50 percent or more; or if one's shareholding is lower than 50 per cent but one's voting rights are sufficient to have a significant impact on shareholders' meetings or the Board's resolutions. Further, the shareholding amounts to *de facto* control if it gains the acquirer actual control of management decisions, human resources or technology.[57] Thus, the focus is not only on the quantity of shares but also *de facto* – that is, real and substantial – control of the company. This practical control can include management of the company and command of its resources, both tangible and intangible. It is not clear whether MOFCOM would apply the same standard in defining control over the company, but this guideline provided by the State Council sheds some light on interpreting the concept of control that the Chinese authority may employ.

E. The law fails to address whether joint ventures are considered concentrations

Joint ventures are also a popular means for foreign investors to enter the Chinese market. However, the AML fails to address the issue of whether joint ventures are a type of concentration governed by the law. In the "MOFCOM Provisional Rule on Notification of Concentration of Undertaking"[58] (hereinafter "Provisional Rules on Notification"), Article 2 stipulates that when "[t]wo or more operators ... jointly set up a new enterprise, [it] constitutes concentration under Article 20 of the law."[59] The original draft did not mention whether the joint venture provision refers to "full function" or "partial function" joint ventures.[60] At the time, it was expected that the final draft would make that crucial distinction.[61]

Surprisingly, the final draft removed the whole section relating to joint ventures. However, Article 20 of the AML indirectly includes the form of joint ventures into the ambit of the AML.[62] In the Article Explanation released by the NPCSC[63] (hereinafter "Official interpretation"), it categorized a joint venture as an acquisition of control by contract or by other means under Article 20(3) of the AML.[64] Therefore, acquiring a controlling interest through a joint venture agreement would fall into the ambit of "by contract or any other means." This provision thus becomes a flexible instrument that allows the authority to categorize different forms of acquisitions, including joint ventures, as subject to the AML.

The author speculates that the reason the entire joint venture provision was deleted from the final version of the AML was to expand the discretion enjoyed by MOFCOM. The ECMR, Article 3(4) stipulates that "[t]he creation of a joint venture performing on a lasting basis all the functions of an autonomous economic entity shall constitute a concentration."[65] Therefore only full function joint ventures would be subjected to the ECMR's control. In contrast, by indirectly assuming control over joint ventures under Article 20(3), the authority gains more comprehensive control over joint ventures.

The provision confers to MOFCOM the power to examine any form of joint venture, even those not controlled by the EU, so long as MOFCOM perceives them as competitive undertakings.[66] The broader approach

adopted by MOFCOM allows it to gain more control over M&A activities. This practice is different from other jurisdictions. The scope of the law is designed to accommodate China's socialist marketplace.

F. Concept of control under the ECMR

In the ECMR, the term "concentration" refers to an operation resulting in "a lasting change in the control of the undertakings concerned and therefore in the structure of the market."[67] Article 3 of ECMR further elaborates the concept of concentration in detail.[68] The concept of control includes the concepts of joint control and sole control depending on whether one person has decisive influence on the activities of an undertaking. Unlike the AML, the concept of "decisive influence" has been further explained. The "notice of concept of concentration" contains an approach to assessing whether a shareholder has the power to make the strategic decisions of an entity.[69] According to Varona,[70] the key to determining the presence of decisive influence is the nature of the shareholding. However, majority shareholding is not the only factor that determines control.[71]

The ability to exercise a decisive influence over the activities of an undertaking has also been indirectly defined in the ECMR. The ECMR, the Commission Interpretation[72] and case law[73] clarify what constitutes a sufficient degree of control to exercise decisive influence.[74] The commission notice suggests that control could be done by one or more "undertaking that constitute legal entities or the assets or part of the assets."[75] Generally, if the undertaking allows an actor to have contractual veto rights that influence the management of the company, then the actor has control.[76]

G. The Chinese authority should draw from European law to provide more guidelines

The European court has developed its case law to clarify what constitutes sufficient control. Furthermore, the commission notice[77] has explained the concept of control. Indeed, the European legal concept of control has developed to accommodate the concepts of majority shareholdings, veto power, property rights, and rights to the use of all or part of assets.

In contrast, the Chinese AML does not clarify what constitutes control. Comprehensive guidelines would be a welcome development, adding certainty to the marketplace. Furthermore, MOFCOM could use its published decisions to explain its reasoning, allowing outsiders to understand the Chinese understanding of control.

6. The Substantive Test for Concentration Effect Review

Article 28 of the AML stipulates one of the key tests in merger review regarding concentration effects.[78] The first part of the Article states that concentration will not be allowed if the merger "will or may eliminate or restrict competition." This language is abstract. However no further guidelines have been published by NPCSC or State Council. Published decisions made by MOFCOM have also provided no clarification. Therefore, considerable uncertainty exists in this domain.

A. Ambiguity of "Eliminate or restrict competition"

The provision is ambiguous as to what criteria MOFCOM will use to determine whether the merger "eliminate[s] or restrict[s] competition." First, as stated by Matthew Bachrack,[79] there is no elaboration on what degree of concentration would amount to a restriction of competition. Further, the public has received no indication of how MOFCOM would formulate the test for concentration.

Harris has tried to respond to this issue,[80] inferring that since the provision does not require any "substantial" or material impact on competition, the level of competition could vary by a very large extent. However, the published decisions did not include any substantive competitive impact assessments,[81] so any analysis is speculative.

Further, the wording "will or may"[82] expands the scope of MOFCOM's discretion. The wording may establish speculative restriction as a substantial platform for MOFCOM to prohibit the concentration. Accordingly, there are concerns that the provision allows for prejudicial action against foreign companies.[83] In any event, the wording at least raises concerns for foreign investors.

Whether MOFCOM would form a general presumption that all mergers and concentrations "eliminate or restrict market

competition" invites considerable debate. Is there a strong presumption of competition restriction requiring strong evidence to rebut it? Would the strength of the presumption differ for foreign investors? The authority's stance remains unknown. The author recommends that MOFCOM assess the merits of every concentration and make its decisions on a case by case basis instead of using tautologies to evaluate concentration.

B. The substantive appraisal test under the EC merger regulation

Under the European Merger Regulation,[84] the substantive test was drafted to cope with mergers that would result in non-coordinate effects in oligopoly markets[85] even though a single, collective dominance may not be established.[86] Recital 25 of the ECMR provides a more thorough and comprehensive picture to explain how the provision works. Under this recital, a merger is anti-competitive when, even in the absence of an oligopoly, it would "result in a significant impediment to effective competition."[87]

This notion of "significant impediment to effective competition" has been borrowed by the AML but applied to when mergers "eliminate or restrict competition." Unlike the AML, ECMR has further elaborated the concept of "significant impediment to effective competition." In this recital, it provides that dominant position would not be the primary factor in making the assessment.[88] The anti-competitive effect should be assessed by the effect that results from "the non-coordinated behavior of undertakings which would not have a dominant position on the market concerned."[89]

Under this provision, a merger would be disapproved if a significant impediment to effective competition is established. Heavy emphasis has been placed on the factor of effective competition.[90] Even if the merger did not create or strengthen a dominant position, if the merger leads to the elimination or substantial reduction of competition – that is, the development of an oligopolistic market – then the merger would still be prohibited.

C. Further clarification on "significant impediment to effective competition" could be made by the authority

When comparing the two provisions, the ECMR provides a detailed guideline. It places its focus on effective competition and further explains the concept by bringing in the concept of oligopolistic markets. In contrast, the AML gives no explanation as to what degree of concentration would be considered a limitation or restriction of competition; nor does it account for oligopolistic market situations. Although the word "eliminate," which refers to a monopolistic market, is clear, the word "restrict" is open to various interpretations. The abstract, unclear nature of the provision is obvious and significant when compared to ECMR provision. Again, the Chinese authority's broad discretion comes at the expense of commercial certainty regarding the law's application.

7. MOFCOM's Discretionary Power to Allow Concentration

The AML provides the criteria for MOFCOM to exercise its discretion to allow the concentration as long as "the business operators can prove either that the favorable impact of the concentration on competition obviously exceeds the adverse impact, or that the concentration meets the public interest."[91] In exercising this discretion, the "Anti-monopoly Law Enforcement Agency under the State Council may exercise its discretion not to prohibit the concentration."[92] Taken together, these provisions empower MOFCOM to allow the concentration if the advantages of the merger are not exhaustively offset by its disadvantages. This discretionary mechanism may also be triggered if the concentration affects the social and public interest.

This provision introduces the concepts of an "efficiency" element and the "public interest." In the following section, I analyze their implications and rationale.

A. Efficiency element: private or public efficiency?

The efficiency element arises in the second part of the "discretion provision."[93] However, it is unclear when the authority will regard efficiency as enhanced. The ambiguity casts doubt on whether purely private efficiency gains will provide a sufficient basis for concentration.[94] If private efficiency gains will not suffice, then a public efficiency

concept will make the application more complicated, as the computation would involve externality costs.[95] As suggested by the Coase theorem,[96] externality costs can never be easily defined and calculated by a single company.

In the US, the Department of Justice (the "DOJ") and the Federal Trade Commission (the "FTC") found it necessary to define more precisely where a proposed merger can create efficiencies without having adverse effects on competition.[97] They have articulated how efficiencies are factored into the analysis by releasing the revised version of their merger guidelines.[98] The guidelines define the efficiencies of a merger as "permitting a better utilization of existing assets, enabling the combined firm to achieve lower costs in producing a given quantity and quality than either firm could have achieved without the proposed transaction."[99] This provision introduces the concepts of utilization and cost minimization. However, the guidelines admit the difficulty of verifying and quantifying efficiencies.[100]

Attempts have been made to convert this abstract concept into a more concrete one. In order to rely on the efficiency claims, for example, the merging party must prove how and when the efficiency would be achieved, outlining the merged firm's ability and incentive to compete.[101] The guidelines suggest that the efficiency claim would not be allowed if it is too vague or speculative, or if it is unverified by reasonable means. In this regard, cognizable efficiencies are recommended since they are "merger-specific efficiencies that have been verified and do not arise from anticompetitive reductions in output or service and are assessed net of costs produced by the merger or incurred in achieving efficiencies."[102]

This guideline has been used for 16 years in the US and has provided clarity and certainty to the public. Jones views the US approach as justifiable on the grounds of strict economic theory, since the increase in consumer welfare could follow from the cost minimization.[103] Although doubts may arise as to whether such a strict economic approach would be commensurate with the values embodied in China's socialist market economy, it would be helpful if the Chinese authority took a lead from the US by further clarifying the efficiency article in the AML.

B. Public interest element

The definition of "public interest" is difficult, if not impossible, for the outsider to ascertain. It is an extremely sensitive issue in the Chinese community. Moreover, the public interest concept is controversial and ambiguous in the context of the Chinese market economy.[104] The law is silent on what factors would be taken into account to consider what constitutes public interest.

Furse has suggested that the objectives stipulated in Article 1 of the AML could help us draw some inference about the concept's content.[105] Article 1 mentions that the purpose of AML is to promote the healthy development of the socialist economy. However, this purpose is still too vague to draw any concrete inference from it. Not surprisingly, foreign parties would be in an even more difficult position to make public interest arguments as they lack the requisite turnover and market impact in China to prove their mergers will fulfill the public interest elements.[106] An inference could therefore be drawn that the public interest element is discriminatory.

The public interest element has yet to be fully ascertained, and there is concern as to whose interest would be co-extensive with the public interest. If the AML protects both business operators and customers, then whose interest should be prioritized as the public interest?[107] The goal of protecting a fair market for competition will not always align with the goal of protecting the public interest.[108] With regard to the issue of price control, competition would always drive the price down to an equilibrium level. However, it would be in the public interest for the government to maintain a price floor to control the consumption of certain products like cars and cigarettes. Such government intervention would, however, deter the authority from allowing competition as it would not further the public interest. In contrast, for some industries the government might like to maintain a price ceiling, such as for commodities or subsidized inputs to the SOEs. Competition law might come into conflict with government policy and diverge with their understanding of the public interest.

Furthermore, the public interest issue becomes more complex if the proposed merger is associated with SOEs. Article 7 of the AML states that where SOEs operate in a "lifeline" industry of the national economy,

its exclusive position shall be lawfully protected.[109] Accordingly, if foreign companies have taken action in acquiring and merging with companies in state-dominated industries, such action may *prima facie* violate the public interest as exclusive production would be superseded. The provision also confers the power to the corresponding authority to protect the SOE.[110] Thus, the public interest requirement only acts to deter M&As instead of allowing for justified exceptions.

8. "Relevant Market" Analysis in China

To determine whether a merger would be adverse to the market, it is crucial to determine whether the firm could obtain a dominant position that would diminish the market's competition. The need for determining the relevant market has been summarized by an EU case, which stated that it is the "necessary precondition for any assessment of the effect of a concentration of a concentration on competition."[111] Therefore, the main purpose of market definition is "to identify in a systematic way the immediate competitive constraints facing the merged entity."[112]

In China, the definition of "relevant market" has been stipulated in Article 12 of the AML. It has only introduced the product market concept and the geographical market concept without further elaboration.[113]

To address this uncertainty, the Anti-Monopoly Committee promulgated further guidelines in 2009 ("Relevant Market Guidelines"). They provide a more detailed definition of "relevant market" and the test that the authority would use to determine whether the merger has taken place in the relevant market.[114] The guidelines aim to provide a "scientific and reasonable definition of the relevant market" in order to identify the competitors and potential competitors, and to determine the market shares of undertakings and the degree of market concentration.[115] The Relevant Market Guidelines have introduced several concepts that have been commonly adopted in the European Union.

A. Hypothetical monopolist test

The hypothetical monopolist test or SSNIP (small but significant and non-transitory increase in price) test[116] is used to define a relevant product market by identifying each distribution made by the

monopolist. The test has been explicitly employed in the Guidelines, Article 10. It is generally adopted by the antitrust authorities in the US, Canada, New Zealand, Australia and the UK.[117] The test applies in merger situations. The Commission Notice on the definition of the relevant market states that the test would address the question of "whether consumers...would switch to other [products] when confronted with a permanent price increase of 5 to 10 per cent for another [product]."[118]

The test goes further by stating "in particular for the analysis of merger cases, the price to take into account will be the prevailing market price."[119] The key for the test is on "substitution" and, as stated by Bishop, the test addresses "whether substitution to other products or other geographic regions is a substantial, or only a trivial, limitation on the conduct of the parties offering those products."[120] Although the test is widely employed, it is problematic.

First, there is difficulty in applying the test, especially in the Chinese market. The test is a hypothetical one and MOFCOM is not experienced in judging consumers' behavior or in gathering correspondence data. The size of the Chinese market also makes the application more difficult. Second, the price elasticity test is mainly and exclusively focused on the price. This view is shared by the Office of Fair Trading (hereinafter "OFT"), the UK competition authority. The OFT has stated that the test "does not allow an assessment of whether prices could be profitably raised by market participants. However the paucity of the data available often prevents the analyst from estimating more appropriate demand models, so that antitrust markets are defined on the basis of price test alone."[121]

Given that the Chinese market has unique characteristics, it would not be feasible to simply rely on price factors to determine whether a market is monopolistic. In China, many markets are dominated by SOEs, and dominance in a relevant market might not be reflected by price change since there would not be a significant change in demand; in other words, a relatively inelastic demand exists in the market. Therefore, the test might not be applicable in the Chinese market. Hence, the Chinese Authority should modify the test to effectuate its analysis to promote the spirit of the law.

B. Relevant product market is similar to the European Union

"Relevant product" is defined in the "relevant market guidelines."[122] The focus of the definition is similar to the EC where it places a heavy analysis on the substitutability of the demand. The substitutability can be analyzed from two perspectives, namely the consumer of the product (demand substitutability) and the supplier or potential supplier of the product (supply substitutability).[123]

In the EC, the relevant product market "comprises all those products and/or services which are regarded as interchangeable or substitutable by the customer, by reason of the product's characteristics, their prices and their intended use."[124] In making its assessment, the commission mainly focuses on the demand-side factors.[125] The most fundamental factor in determining the relevant product market is substitutability. In a leading case, the European Court commented that "the concept of relevant market presupposed that there is sufficient degree of interchangeability between all the products forming part of the same market."[126] The adopted test shows that the substitutability is essential to determining the relevant product market.

Factors for determining the relevant market in the Chinese guidelines

A non-exhaustive list of demand side factors has been provided in Article 8 of the Guidelines. This list is similar to the one in the commission notice of the EC[127] where evidence of customers' behavior, quantitative tests, reliance of customers and competitors, preferences of customers, the nature and specification of products, price and switching costs would be relevant to the analysis.[128]

In the Guidelines, the consequences of a change in product price would be relevant considerations. That is, if customers would consider switching to another product, that would be relevant.[129] In such an analysis, all of the characteristics and usages of the product are relevant, including but not limited to the product's appearance, quality and specification features. In view of the aforementioned features, a relevant market can be defined if consumers would consider another product to be a close substitute to the product at issue.[130]

A similar test has been used in the case of *Euorpemballage Corp and Continental Can Co Inc*,[131] where the judge found that "the competition can only be judged in relation to those characteristics of the products in question by virtue of which those products are particularly apt to satisfy an inelastic need and are only to a limited extent interchangeable with other products."[132] The judgment shows that the product nature is vital in determining the relevant market. Demand and customer behaviour would also help or assist the determination of whether the elasticity of the demand would be affected.

The inference that could be drawn from the list is that the court has adopted the approach used in the EC by focusing heavily on the issue of substitutability.[133] The focus of the analysis is generally based on the price and intended use of the product.

However, this approach is not free from criticism as it has been implemented in China. Over generalization of the market has been made, especially in the decision of *Coca Cola/Huiyuan*.[134] The responses to the decision were generally negative. MOFCOM made a general supposition that fruit juice and carbonated drinks lie in the same product market or that the two markets are proximately linked to each other because of the similar nature of the two products. The decision failed to address the market definition issue. Without showing a factual linkage between the two markets, it simply mentioned that the merger would have adverse competitive effects on both fruit juice and carbonated drink markets. MOFCOM, it can be safely assumed, relied on a broad market definition to conclude that high market shares would be acquired by Coca Cola if they approved the merger.

In *Mitsubishi/Lucite*,[135] MOFCOM identified three markets that are not obviously related as the 'relevant markets' without providing explanations. As stated by Furse, MOFCOM failed to explain what methodology or factors they have used to determine the scope of the relevant market.[136] MOFCOM just listed the product's characteristics without providing its reasoning or explaining the supposed nexus of the different markets.

In *GM/Delphi*,[137] MOFCOM again failed to identify the link between the two corresponding product markets. The authority simply indicated that the two markets have a vertical relationship without elaborating

on why the vertical relationship affected the determination of the relevant market. At most, the published decision only mentioned that GM's product is involved in the automotive market and Delphi is involved in 10 independent automotive parts markets. The factors listed in the guidelines have never been mentioned by a published decision.

In *Panasonic/Sanyo*,[138] the decision identified three product markets,[139] namely the coin-type lithium secondary battery, civil Ni-MH battery, and No-MH car battery. Although the competition effect of the merger was stipulated in the reasoning, the reason as to why those three markets were chosen as the relevant product market was neglected. The guidelines have been nominally distributed to the public but the reasoning behind their implementation has never been disclosed.

In summary, the stipulated factors in the guidelines have not been incorporated into the published decisions. Hence, no inferences can be drawn from the decisions to understand how the system operates and how the authorities would define the relevant market.[140]

On the other hand, arbitrary decisions could result from emphasizing substitutability and literally applying the guidelines without engaging in in-depth analysis. Evidently, such an approach led to placing similar products into the "same" market, without considering their shared relevance. As suggested by Jones, the characteristics and intended use of the commodities alone will not be particularly useful to the determination of the relevant market.[141] A fair and comprehensive analysis could never be conducted by using the written methods employed by the Chinese Authority in its decisions. It is uncertain whether the authority purposefully employed this defective method of conducting the test to protect the SOEs or whether they have simply failed to identify the deficiencies of such an approach.

9. Factors Relevant to Merger Review in China

Since the *Coca Cola/Huiyuan* decision, concerns have been raised about whether the AML is drafted to deter foreign mergers and foreign participation in the Chinese market. In this section, I analyze Article 27 of the AML to evaluate how MOFCOM applies this provision and whether the provision has a discriminatory effect.

Pursuant to Article 27, MOFCOM must consider whether a concentration has taken place during the merger review.[142] Looking at the language employed in Article 27, there is on its face no discriminatory wording that would suggest that unfair treatment is given to foreign mergers. The factors listed in Article 27 are similar to those listed in the ECMR. However, in Article 27(5), the wording of the provision has raised concerns. It stipulates that "national economic development" would be a relevant factor for consideration. Some commentators question whether such a provision would be used as a tool not to protect fair market conditions but to protect the SOEs from competition.[143]

In *Coca Cola/Huiyuan*, MOFCOM rejected the application for a merger on the grounds that such a merger would cause an anti-competitive effect in the fruit juice beverage market. Some reputable commentators agreed and stated that within China the merger would enable the merged entity to leverage its dominance into the fruit juice market.[144] However, proponents for the merger argued that the authority failed to establish and substantiate the presumption of an adverse competitive effect, the presumption being that the merged parties have the tendency and capacity to bundle and tie the goods to leverage power in one market into power in another.[145]

MOFCOM's second ground to reject the merger was related to branding. Branding is a key element of effective competition within the beverage market. However, the intellectual property issue is not directly relevant to the competition law issue. Therefore, it is not evident why this was a reason to reject the merger.

Third, MOFCOM found that the merger might squeeze out small and medium enterprises from the juice market, and that this was not conducive to the continued healthy industrial development of the Chinese fruit juice market.[146] It is arguable that the third part of MOFCOM's reasoning has no underpinning in the competition law. MOFCOM was concerned that medium-sized enterprises might be excluded from the fruit juice market by either competition from Coca Cola or from the supply source. The decision emphasized economic policy rather than the spirit of the competition law. It is reasonable to conclude that the authority felt the industrial policy consideration outweighed the need to maintain a fair market.[147] The importance of facilitating the healthy development of the market once again played an important role in the

outcome of the decision. Therefore, the inference could be drawn from this decision that economic policy would play a large part in MOFCOM's application of the competition law if the decision involves SOEs.

The reasoning provided by MOFCOM has been severely criticized by the public. It has been suggested by The Economist that MOFCOM is engaging in protectionism and utilizing the AML as a tool to discriminate against foreign investors.[148] It is safe to assume that government policy or political pressure plays a role in ascertaining "national economic development" under Article 27(5) of the AML. Literal interpretation of the law would not be sufficient to determine whether an application for a merger would be approved.

A. MOFCOM's tendency to impose post-merger conditions

An application for a merger might be hindered even if the merger has fulfilled all of the legal requirements. The authority may rely on its predictive analysis and impose conditions on the merger.

MOFCOM has imposed conditions on several deals by virtue of the high market shares enjoyed by the merging companies. Pursuant to Article 27, MOFCOM may impose conditions, taking into account "market share in the relevant market and their controlling power"[149] and "the degree of market concentration in the relevant market."[150] Furthermore, there is a propensity for MOFCOM to impose conditions when the authority finds material business duplication. The enforcement strategy of MOFCOM of creating a *prima facie* case indicates that merging parties bear the burden of proof to rebut a dominant position subsequent to the merger application.[151]

In *Mitsubishi/Lucite*,[152] MOFCOM found that there was an overlap in the production and sales of methyl methacrylte (hereinafter "MMN"). As to the issue of market share, the parties' post-acquisition combined market share would jump to 64 percent – much higher than the second and the third competitors in the market.[153] Therefore, MOFCOM imposed conditions on this transaction.

In *Pfizer/Wyeth*,[154] in accordance with MOFCOM's available data, the authority found that the merger would result in a significant increase in the combined market share, specifically 49.4%. The post-merger

market share would be much higher than the other competitors, such as 18.35% for Intervet. This increase in market share would give the new company the ability to use its scale to expend the market, thus controlling market price. Therefore, MOFCOM imposed conditions on the merger.

GM/Delphi[155] involved a vertical acquisition between automotive and automotive parts companies. MOFCOM raised concerns about whether GM would gain access to inside information concerning its competitors, whose main supplier of automotive parts in China was Delphi. The foreclosure-related concerns prompted MOFCOM to impose conditions.[156] Some commentators have found issues with the "foreclosure-related concerns" by stating that MOFCOM's concern was not substantiated by any evidence. Zhang has stated that the authority "often established no horizontal cases by presuming foreclosure theory without realizing the necessity of the heavy burden of proof for presumption of such competition harms."[157] Because the decision lacks any substantial support or analysis to justify its conclusions, it is unconvincing.

The above decisions invite the inference that high market shares often result in MOFCOM imposing conditions on mergers. Horizontal mergers that will result in the merged operation having a market share of 45 percent or above may be subject to conditions unless competitive concerns are successfully rebutted.[158] The imposition of conditions is based on the general presumption that an increase in market share would spontaneously lead to market power and the manipulation of market price, and would limit or exclude vertical material supply to marginalize competitors.[159] The authority has demonstrated its concern with the potentially anti-competitive impact on a market if the parties increase their control over that market.[160]

B. Conditions may be imposed on speculative grounds

A foreign merger might be severely affected even where only a minority market share is acquired, as MOFCOM may impose conditions if it speculates that anti-competitive effects may result despite their low probability of actually arising.

In *InBev/Anheuser*, MOFCOM found that "[f]ollowing establishment of the case file, MOFCOM has reviewed the materials submitted, consulted with relevant government agencies, and solicited opinions from relevant beer industry associations, principal domestic manufacturers of beer and raw materials, and distributors of beer products. Based upon Article 28 of the Anti-Monopoly Law, MOFCOM has decided not to prohibit this merger transaction."[161] It has been suggested that the combined market share prior to the deal was just 13 percent. The authority, nonetheless, decided to impose a condition to "prevent the formation of a structure that impairs competition." The decision showed that the authority is not concerned with the current market structure but with a potential increase in the market share.[162] One commentator found that the methodology adopted by the authority is a "forward looking condition" in view of the concern that further M&A by the merged party might lead to an unhealthy level of market concentration.[163] Therefore, speculation on market dominance would provide a sufficient basis for MOFCOM to impose conditions on a merger.

Such an approach, based only on speculation, is inappropriate. The lack of convincing reasoning should cause outsiders to rightfully question MOFCOM's integrity.

C. MOFCOM is likely to impose conditions on deals affecting SOEs

The authority has rejected only one merger application. However, its decisions demonstrate that economic policies are likely to play a crucial role in the merger review process. It is likely that when a foreign merger involves SOEs or industries dominated by SOEs, MOFCOM would be willing to impose conditions on the merger, creating indirect restrictions on foreign investments.

10. National Security Review

The AML's discriminatory nature is more apparent in the National Security Review (the "NSR"). The authority is not only sensitive to deals with a military aspect. The authority is currently also concerned with knowledge-based resources, including intellectual property. The drafting of the second part of the NSR provision emphasizes this point. Some commentators have written that the focus of the NSR is not only

national security concerns, but also the protection of local industries and SOEs from foreign intrusion.[164] Some commentators have regarded the NSR as an expansion of the ambit of the merger review process to a political assessment without any linkage to economic or antitrust analysis.[165] SOEs' operation and research and development activities would constitute the authority's primary concerns under the NSR. Further, the NSR has been viewed as a powerful tool to take "revenge" on the blockage of attempts by Chinese enterprises to acquire overseas businesses.[166]

Article 31 of the AML does not establish the scope of the NSR's application.[167] This omission has raised concerns about whether MOFCOM would arbitrarily use it as a tool to restrict a merger if foreign applications are made. Further, most of China's largest companies are SOEs. Some commentators suggest that the NSR or the Security Review System (hereinafter "SRS") could be easily applied if a foreign merger involves key industrial sectors or "well known trademarks or traditional brands."[168] Such cases would inevitably invite close scrutiny in the concentration and merger review process.[169]

The China state council has issued the SRS circular[170] to relieve concerns. However, the subsequent notice has triggered another concern. MOFCOM has issued the SRS Notice[171] to supplement the implementation. The SRS applies exclusively to foreign investors. Accordingly, this explicitly indicates that Article 31 is discriminatory in nature against foreign investors, who must ensure that their merger application complies with the corresponding requirements of the SRS Notice.

A. Discriminatory nature of the National Security Review

The first part of the SRS Circular identifies the ambit of application of the NSR. The NSR applies where the relevant industry is a business focusing on military and security: that is, where the business operates within an industry encompassing the national security of the "important agricultural products, energy resources, critical infrastructure, transportation service, key technologies and major equipment manufacturing and other enterprise."[172] From the above circular, it seems that typical elements of national security – such as military and

defence – are the focus of the NSR. However, the authority has also extended its application to assets less directly related to the military, both tangible and intangible.

There are several propositions for why drafting occurred in this way. First, it has been suggested that a number of industries might have found their way into the NSR by virtue of industrial policy considerations that play a role in MOFCOM's review.[173] Furthermore, the Chinese authorities are reluctant to facilitate takeovers relating to prominent domestic Chinese enterprises. It is reasonable to assume that the Chinese government would like to maintain dominance in industries that, in its view, are critical to national security and economic development.[174] The dual capacities of the government, namely as the owner of the enterprise and the regulator of the market, suggest that the government will discriminate against foreign investors simply because a merger affects one or more of those industries.

The government might not be able to avoid involvement in the NSR process, as its passive and involuntary involvement may be inevitable.[175] Its industrial policy would be a crucial part of the NSR. For example, the collapse of SOEs in crucial industries would trigger domino effects such as unemployment, undermining the maintenance of a stable society. Therefore, in this regard, national security may be interpreted as the maintenance of the status quo. The NSR may be used as yet another tool to uphold the dominance of the SOEs.

Furthermore, the authority may wish to retain control of resources in key industries. Knowledge from research and development would be treated as key national assets and would not be transferred to foreign entities. When conducting the NSR, the authority would likely liaise with the relevant department to make sure their decision is consistent with the government's policy. Economic competition analysis might be superseded by political considerations.[176] The lack of transparency in the process would further exacerbate the problem. Hence, the NSR may be used as a government tool to maintain strict control over key resources. Any mergers involving such valuable assets would be subjected to close scrutiny.

B. Relevant factors for consideration under the National Security Review

The NSR Notice[177] described four factors for consideration in foreign merger review: (i) the impact on equipment, facilities, domestic production and service capacities;[178] (ii) national economic stability;[179] (iii) basic social order of life and key technology;[180] and (iv) R & D capabilities.[181] As with the factors relevant to merger review generally, it is difficult for potentially merging entities to interpret the content and substance of the NSR elements. Indeed, the situation is even worse when compared to the factors listed in Article 27, as no published decisions have applied Article 2 of the NSR Notice. Therefore, the criteria do not facilitate any self-assessment on whether the merger will fall within the scope of the NSR.

C. Sham arrangements to avoid the National Security Review will fail

The SRS Notice[182] has clarified that the review process may not be avoided by adopting a proxy application. MOFCOM would look at both the substance and actual impact of the arrangement. The form would not be the ultimate presiding factor for application.[183] Attempts at acquiring a company, *inter alia*, by trust, multi-level re-investment, leasing, loans protocol control or foreign trade would fail if the acquisition falls within the scope of the NSR. It is understandable that if the merger falls within the ambit of review, any attempt to make artificial arrangements to circumvent the NSR would fail.

D. Difficulty of ascertaining whether the application falls within the ambit of the National Security Review

Notwithstanding that the State Council and MOFCOM have released guidelines on the implementation of the NSR, it is still difficult for the applicants to self-assess whether their proposed application would fall under the ambit of the NSR. The only indicator that the authorities have produced is a very broad and non-exhaustive list of industries without going further into what specific factors trigger the NSR. This uncertainty may hinder foreign investment, as foreign entities might not be able to predict when a merger might be blocked. It is always difficult to comply with rules that are unascertainable and equivocal.

Although the procedures for the NSR have been clarified,[184] the scope of the NSR has become even more vague. This raises concerns as to whether MOFCOM would have the discretion to treat any merger as a sensitive one. Furthermore, the NSR may be used as a tool for the Chinese Authority to take "revenge" on the US authority where the US had previously prohibited a Chinese company's merger application in the US. In short, international politics and protectionism might play a role in the application of the NSR.

11. Conclusion

The AML grants the Chinese authority the mandate to promote both fair competition and the socialist market economy. However these two objectives may contradict each other, especially when the targeted merger takes place in markets where SOEs enjoy a dominant position. Therefore, the law is drafted to confer broad discretionary power to the authority. The provisions are drafted in an abstract way and published decisions offer little insight into the authority's reasoning and methodology, precluding foreign investors from understanding the law's application. Mergers in industries categorized as critical to China's national security and economic development can be subject to close scrutiny.[185] It is reasonable to infer that the Chinese Government intends to retain or strengthen its dominant role in such industries.[186] Therefore, the discretionary power of the authority plays an important role in ensuring that SOEs maintain control in those industries.

Although some commentators suggest that MOFCOM has consulted the decisions of other jurisdictions' antitrust agencies,[187] the AML has been applied in a way that accords with Chinese characteristics. The system is not transparent enough to allow investors to understand how the system really works. Failing to combat administrative monopolies would logically lead the public to believe that the authority does not intend to truly encourage fair, competitive markets. This lack of transparency and commitment to competition undermines the credibility of the law and the enforcement agency.[188]

The NSR only applies to foreign merger activities. Yet the government is playing the dual roles of enterprise operator and industry regulator. Therefore, the government is incentivized to use the NSR to discriminate against foreign investors. The State Council's guidance

publication reinforces the discriminatory aspect of the NSR. Foreign investors are recommended to consult MOFCOM in advance to ascertain whether their targeted merger would fall within the ambit of the authority's NSR scrutiny.

MOFCOM has demonstrated a reluctance to completely block all merger applications to prevent an outcry from foreign investors and governments. However, control over post-merger behaviour is still a primary concern of the Chinese authority. It will impose conditions on the merger to ensure that the transaction will not cause a significant impact on the market, especially in markets where SOEs play an important role. Such conditions include restrictions on market share percentages and the imposition of price controls that allow the government to maintain control over the economic sector.

The AML is still in a developmental stage, as is the Chinese economy. MOFCOM seeks to ensure that the Chinese economy develops gradually and maintains stability. Further, MOFCOM is attempting to establish its credibility as an antitrust regulator and avoid the criticism that it is preventing foreign investors from entering the Chinese market. However, the current legislation gives the authority an overwhelming discretion, undermining the spirit of fair competition supposedly endorsed by the law. Significant reforms are necessary to increase transparency and predictability, particular for foreign investors.

Endnotes

[1] Bachelor of Business Administration (Hons), Juris Doctor, Postgraduate Certificates in Law (pending), City University of Hong Kong.
[2] *Constitution of the People's Republic of China* (China), art 15.
[3] Bruce M. Owen, Su Sunn & Wentong Zheng, "China's Competition Policy Reforms: The Anti-monopoly law and beyond" (2008) 75 Antitrust Law Journal 231 at 232 [Owen].
[4] Mark Williams, "Foreign Investment in China: Will the Anti-Monopoly Law be a barrier or a facilitator?" (2009) 45 Tex. Int'L L.J. 127 at 133 [Williams].
[5] Xinzhu Zhang & Vanessa Yanhua Zhang, "Chinese Merger Control: Patterns and Implications" (2010) 6:2 Journal of Competition Law and Economics 477 at 478 [Zhang].
[6] *Fan Long Duan Fa* [Anti-Monopoly Law] (China), 2007 [AML].
[7] Anu Brad, "Chinese Anti-Trust Law: The New Face of Prtectionism?," *Huffington Post* (1 Aug 2008) online Huffington Post <http://www.huffingtonpost.com/anu-bradford/chinese-antitrust –law-the_b_116422.html>.

[8] Michael Han & Alex Potter, "China" in John Davies ed, *Merger Control 2010* (London: Getting the Deal Through, 2009) 90 at 91.
[9] *State Council Gazette*, online The Central People's Government of the People's Republic of China <http://english.gov.cn/documents/gazettes/>.
[10] "Guide of the Anti-Monopoly Committee of the State Council for the Definition of the Relevant Market" (24 May 2009) online Ministry of Commerce of the People's Republic of China <http://www.mofcom.gov.cn/article/zhengcejd/bj/200907/20090706384131.shtml>.
[11] Mark Furse, *Antitrust Law in China, Korea and Vietnam* (Oxford: Oxford University Press, 2009) at 105 [Furse 1].
[12] John Hickin, "China's Anti-Monopoly Law Merger Control Regime – 10 Key Questions Answered (Part II)," *Mayer Brown JSM* (5 March 2010) at 5 [Hickin].
[13] H. Stephen Harris, Jr et al, *Anti-Monopoly Law and practice in China* (Oxford: Oxford University Press, 2011) at 137 [Harris].
[14] Furse, *supra* note 11 at 68.
[15] Sallil K. Mehra & Meng Yanbei, "Against Antitrust Functionalism: Reconsidering China's Antimonopoly Law" (2009) 49 VA. J. Int'L L 379 at 385 [Mehra].
[16] Owen, *supra* note 3 at 238.
[17] AML, *supra* note 6 at art 1.
[18] Owen, *supra* note 3 at 239
[19] *Ibid* at 255.
[20] David Hirshleifer , Jack Hirshlefier & Amihai Glazer, *Price Theory and Applications: Decisions, Markets and Information*, 7th ed (Cambridge: Cambridge University Press, 2005) at 202.
[21] AML, *supra* note 6 at art 7. AML The provision states that the authority "shall protect these lawful business operations conducted by the business operators therein, and shall supervise and control these business operations and the prices of these commodities and services provided by these business operators, so as to protect the consumer interests and facilitate technological advancements."
[22] Huang Y., "Pursuing the Second Best: The History, Momentum and Remaining Issues of China's Anti-Monopoly Law" (2008) 75 Antitrust Law Journal 117 at 127.
[23] *Ibid.*
[24] AML, *supra* note 6 at art 11. "A trade association shall strengthen the self-discipline within the industry, lead the business operators in the industry toward lawful competition, and maintain the market competition order."
[25] Williams, *supra* note 4 at 137.
[26] Mehra, *supra* note 15 at 397.
[27] *Ibid* at 137.
[28] *Ibid* at 149.
[29] The State Administration for Industry and Commerce (SAIC); the National Development and Reform Commission (NDRC); and the Ministry of Commerce (MOFCOM).

[30] *Regulations on Foreign Investors Merging with or Acquiring Domestic Enterprises* (China), 2006 at art 51 [M&A Regulations]. "According to the provisions of the Antimonopoly Law...the foreign investor shall make a declaration with the MOFCOM and shall not carry out the deal without declaration."

[31] Michael Faure & Roger Van den Bergh, "Critical Issues in the Enforcement of the Anti-Monopoly Law in China: a Law and Economics Perspective" in *Competition Policy and regulation, recent developments in China, the Us and Europe*, Michael Faure ed (UK: Edward Elgar Publishing, 2011) at ch. 4.

[32] AML, *supra* note 6 at art 30. "The Anti-monopoly Law Enforcement Agency under the State Council shall timely publicize a decision on prohibiting the concentration of business operators or a decision on attaching restrictive conditions to the concentration of business operators."

[33] MOFCOM is the publishing authority.

[34] Mark Furse, "Merger Control in China: the First Year of Enforcement" (2010) 31:3 E.C.L.R 98 at 104 [Furse 2].

[35] Zhang, *supra* note 5 at 493.

[36] Ministry of Commerce Announcement No. 22 (China), 2009 [MCA 22].

[37] Ministry of Commerce Announcement No. 28 (China), 2009 [MCA 28].

[38] Ministry of Commerce Announcement No. 95 (China), 2008 [MCA 95].

[39] More coverage would be given in the later session.

[40] Zhang, *supra* note 5 at 475.

[41] AML, *supra* note 6 at art 20. "First, merger of business operators. Second, a business operator acquires control over other business operators by acquiring their equities or assets. Third, a business operator acquires *control* over other business operator or is able to exert a *decisive influence* on other business operators by control or any means."

[42] AML, *supra* note 6 at art 20(3).

[43] Moritz Lorenz, "The new Chinese Competition Act" (2008) 29:4 E.C.L.R. 257 at 261.

[44] *Ibid.*

[45] Furse 1, *supra* note 11 at 38.

[46] *Ibid* at 38.

[47] Draft implementing regulations (Legislative Affairs Office of the State Council, 27 March 2007)

[48] *MOFCOM Provisional Rules on Notification of Concentration of Undertaking* (China), 2009.

[49] AML, *supra* note 6 at art 3. "The acquisition of more than 50 percent of the voting shares or assets acquiring the power, including by contract or other means to have a majority power to decide or appoint the members of the board of directors and to make any key management on the operation decisions of any undertaking."

[50] Harris, *supra* note 13 at 129.

[51] *Provisional Rules on Notification of Concentration of Undertaking* (China), 2009.

[52] *European Merger Regulation Council Regulation* (2004) 139/2004 OJ L124/1 [ECMR].
[53] *Ibid* at art 3(2)(b).
[54] Wu Z., "Perspectives on the Chinese Anti-Monopoly Law" (2008) 75 Antitrust Law Journal 73 at 87.
[55] Harris, *supra* note 13 at 129.
[56] Furse 1,*supra* note 11 at 99.
[57] *Guo Ban Fa* [Circular on National Security Review for the Acquisition by Foreign Investor of Domestic Chinese Enterprise] (China), 2011, at 6.
[58] *MOFCOM Provisional Rule on Notification of Concentration of Undertaking* (China), 2009.
[59] *Ibid* at art 2.
[60] Identified in the ECMR.
[61] Hickin, *supra* note 12 at 5.
[62] Harris, *supra* note 13 at 131.
[63] Standing Committee of the National People's Congress, *Anti-monopoly Law of the People's Republic of China: Article Explanation, Legislation Cause and Related Provision*, (Beijing: Peking University Press, 2008) at art 164.
[64] AML, *supra* note 6 at art 20(3). "Control over other business operators or is able to exert a decisive influence on other business operators by contract or any other means."
[65] ECMR, *supra* note 52 at art 3(4).
[66] Hickin, *supra* note 12 at 5.
[67] ECMR, *supra* note 52 at Recital 20.
[68] *Ibid* at art 3(1). "A concentration shall be deemed to arise where a change of control on a lasting basis resulting from (a) the merger of two or more previously independent undertakings or part of undertakings, or (b) the acquisition, by one or more person already controlling at least one undertaking, or by one or more undertakings whether by purchase of securities or assets, by contract or by any other means, or direct or indirect control of the whole or parts of one or more other undertakings."
[69] *Notice of Concept of Concentration* (1998) OJ C66/5 at 39 [NCC].
[70] Juan Briones Alonso et al, *Merger Control in the European Union, Law, Economics and Practice* (Oxford: Oxford University Press, 2008) [Alonso].
[71] *Ibid* at 2.32.
[72] NCC, *supra* note 69.
[73] *McCormick/CPC/Rabobank/Ostmann*, (1993) Case IV/M330 (Commission of the European Communitities).
[74] Alonso, *supra* note 70 at 2.68.
[75] NCC, *supra* note 69 at 11.
[76] *Ingersoll-Rand/Dresser*, (1993) Case IV/M121 (Commission of the European Communitities).
[77] NCC, *supra* note 69.
[78] AML, *supra* note 6 at art 28. "Where the concentration of business operators will or may eliminate or restrict competition, the Anti-monopoly

Law Enforcement Agency under the State Council shall make a decision to prohibit the concentration."

[79] Matthew Backrack, Cunzhen Huang & Jay Modreall, *Merger Control under China's Antimonopoly Law: The first Year* (Chinese Business Law Review, 2009) at 2 [Backrack].

[80] Harris, *supra* note 13 at 155.

[81] Zhang, *supra* note 5 at 486.

[82] AML, *supra* note 5 at art 28.

[83] Furse 1, *supra* note 11 at 105.

[84] ECMR, *supra* note 52.

[85] *Ibid* at art 2(3). "[A] concentration which would significantly impede in effective competition in the common market or in a substantial part of it, in particular as a result of the creation or strengthening of a dominant position, shall be declared compatible with the common market."

[86] Alison Jones & Brenda Sufrin, *EU Competition Law: Text, Cases & Materials*, 3rd ed (Oxford: Oxford University Press, 2010) at 1008 [Jones].

[87] ECMR, *supra* note 52 at Recital 25. The whole provision reads, "concentration involving the elimination of important competitive constraints that the merging parties had exerted upon each other, as well as a reduction of competitive pressure on the remaining competitors, may, even in the absence of likelihood of coordination between the members of the oligopoly, would result in a significant impediment to effective competition."

[88] *Ibid.* "The article should be interpreted as extending beyond the concept of dominance."

[89] *Ibid.*

[90] Jones, *supra* note 86 at 1009.

[91] AML, *supra* note 6 at art 28.

[92] *Ibid* .

[93] *Ibid.*

[94] Backrack, supra note 79 at 2.

[95] Ronald H Coase, "The Problem of Social Cost" (1960) 3:1 *Journal of Law and Economics* at 1.

[96] In law and economics, the Coase theorem explains the economic efficiency of an economic allocation or outcome in the presence of externalities.

[97] "Joint announcement by the Federal Trade Commission and the Department of Justice in the US for the revised guidelines on Efficiencies in Merger" (8 April 1997).

[98] *Ibid.*

[99] U.S. Department of Justice and the Federal Trade Commission, *Horizontal Merger Guidelines* (8 April 1997) at s. 4, para 1.

[100] *Ibid* at s. 4, para 1.

[101] *Ibid* at s. 4, para 4.

[102] *Ibid* at s. 4, para 5.

[103] Jones, supra note 88 at 1041.

[104] Xiaoye Wang, "Highlights of China's New Anti-monopoly Law" (2008) 75

Antitrust L.J. 133 at 142 [Wang].
[105] Furse 1, *supra* note 11 at 106.
[106] *Ibid.*
[107] Wang, *supra* note 104 at 143.
[108] *Ibid.*
[109] AML, *supra* note 6 at art 7. "With respect to the industries controlled by the State-owned economy and concerning the lifeline of national economy... or the industries lawfully enjoying exclusive production and sales, the State shall protect these lawful business operations conducted by the business operators therein."
[110] *Ibid.*
[111] *France v Commission, Societe Commerciale des Potasses et de l'Azpte (SCPA) v Commission, Case C-68/94 and C-30/95 (Joined Cases Judgment, 31 March 1998) ECR I1375 & 4 CMLR 829 (European Court, Court of First Instance) at para 143.*
[112] *Horizontal Merger Guidelines*, (2004) OJ C31/5 at para 10.
[113] AML, supra note 6 at art 12. "[R]elevant market" ...refers to the commodity scope or territorial scope within which the business operators compete against each other during a certain period of time for specific commodities or services."
[114] *Guidelines on the Definition of Relevant Markets by the Anti-Monopoly Commission under the State Council* (China), 2009 ["Guidelines on Relevant Markets"].
[115] *Ibid*, at art 2.
[116] Harris, *supra* note 13 at 92.
[117] Jones, *supra* note 86 at 66.
[118] *Commisssion Notice on the Definition of the Relevant Market for the Purpose of Community Competition Law*, (1997) OJ C372/5, (1998) 4 CMLR 177 at para, 18 [Commission Notice].
[119] *Ibid* at para, 19.
[120] W.Bishop, "Editorial: the Modernization of DGIV" (1997) ECLR Vol18, 481–484.
[121] "Quantitative Techniques in Competition Analysis, Research Paper 17" (October 1999) online Office of Fair Trading <http://www.oft.gov.uk/shared_oft/reports/comp_policy/oft266.pdf> at para 2.25.
[122] Guidelines on Relevant Markets, *supra* note 116 at art 2. "Products of the same group or category which are regarded to be close substitutes by the customer, by reason of the products' characteristics, their intended use, and their prices. Those products are in strong competition relationship and may service as the product market."
[123] Mark Furse, *Competition Law of the EC and UK*, 6th ed (Oxford: Oxford University Press, 2008) at 281.
[124] Commission Notice, *supra* note 118 at para 7.
[125] Jones, *supra* note 86 at 1012.
[126] *Hoffmann-La Roche & Co. AG v Commission of the European Communities*,

(1979), Case 85/76 (Court of Justice of the European Communities).
[127] Commission Notice, *supra* note 118 at para 7.
[128] Jones, *supra* note 86 at 1012.
[129] Guidelines on Relevant Markets, *supra* note 114 at art 8(1).
[130] *Ibid* at art 8(2).
[131] *Europemballage Corp and Continental Can Co Inc v Commission* , (1973) Case 6/72 [1973] ECR 215.
[132] *Ibid* at para [32].
[133] Price differences among products, the sales channel of the products and the customer's preference or reliance on certain products would also be relevant considerations.
[134] MCA 22, *supra* note 36.
[135] MCA 28, *supra* note 37.
[136] Furse 2, *supra* note 34.
[137] MCA 28, *supra* note 37.
[138] Ministry of Commerce Announcement No. 82 (China), 2009.
[139] *Ibid* at para 4.
[140] Zhang, *supra* note 5 at 483.
[141] Jones, supra note 86 at 62.
[142] AML, *supra* note 6 at art 27. "The following factors shall be taken into account in the examination of the concentration of business operators: market share in the relevant market and their controlling power; The degree of market concentration in the relevant market; The impact of the concentration on the market access and technological advancements; The impact of the concentration of business operators on the consumers and other business operators; The impact of the concentration of business operators on the national economic development; and Other factors that may affect the market competition and shall be considered as deemed by the Anti-monopoly Law Enforcement Agency under the State Council."
[143] John Hickin, "China's Anti-Monopoly Law Merger Control Regime – 10 Key Questions Answered (Part I)," *Mayer Brown JSM* (2 March 2010) at 2 [Hickin 2].
[144] William Kovacik, "China not abusing antitrust law – US trade official," Reuter Report (July 6 2009) online Reuter Report <http://www.reuters.com/article/marketnews/idAFPEK34831220090706?rpc=33>.
[145] *Zhang*, supra note 5 at 488.
[146] MCA 22, *supra* note 136 at para 4.
[147] Hickin 2, suprate note 145 at 2.
[148] "Hard to Swallow," *The Economist* (19 March 2009) online The Economist <http://www.economist.com/business/PrinterFriendly.cfm?story_id=13331326)>. "It reflects a political response to critical comments by America's new administration…even if China publicly urges other countries to commit to opening their markets to Chinese investment and trade, it is imposing yet another barrier to outsiders."
[149] AML, *supra* note 6 at art 27(1).

[150] *Ibid* at art 27(2).
[151] Zhang, *supra* note 5 at 488.
[152] MCA 28, *supra* note 37.
[153] *Ibid* at para 5.
[154] Ministry of Commerce Announcement No. 77 (China), 2009.
[155] MCA 28, *supra* note 37.
[156] Harris, *supra* note 13 at 161.
[157] Zhang, *supra* note 5 at 491.
[158] Hickin, *supra* note 12 at 2.
[159] *Ibid.*
[160] Zhang, *supra* note 5 at 483.
[161] MCA 95, supra note 38 at para 2.
[162] Zhang , *supra* note 5 at 483.
[163] Hickin, *supra* note 12 at 3.
[164] Furse 1, *supra* note 11 at 38.
[165] John M. Toth, "Cross-border M&A deals: Nationality Security Interest Reviews Raise Flags," Counsel to Counsel (January 2008) online Squire Sanders <http://www.squiresanders.com/pdf/Corporate/C2C0108_SquireGP.pdf>.
[166] The US congress has prohibited the application of a Chinese Petroleum enterprise to take over Unocal in the United States. It is the consensus of commentators that political pressure had a material impact in the decision.
[167] AML, *supra* note 6 at art 31. "Where…[there is an] acquiring a domestic enterprise… and the national security is involved…the examination on the national security shall also be conducted according to the relevant provisions of the State."
[168] The published decision of the *Coca Cola* case has highlighted this factor as one of the concerns of the authority.
[169] Hickin, *supra* note 12 at 3.
[170] *Guo Ba Fan* [Circular of the Establishment of a Security Review System Regarding Mergers and Acquisitions of Domestic Enterprises by Foreign Investors No. 6] (China), 2011 [Circular of the State Council].
[171] Notice of Implementation of Security Review System Requirement over Foreign Investor Acquiring a Domestic Enterprise (Ministry of Commerce No.53) (China), 2011 [SRS].
[172] Circular of the State Council, *supra* note 170 at art 1(a).
[173] MCA 22, *supra* note 36.
[174] Owen, supra note 3 at 240.
[175] Zhang, *supra* note 5 at 492.
[176] *Ibid* at 493.
[177] SRS, *supra* note 171 at art 2.
[178] *Ibid* at art 2(a).
[179] *Ibid* at art 2(b).
[180] *Ibid* at art 2(c).
[181] *Ibid* at art 2(d).
[182] *Ibid.*
[183] *Ibid* at art 9.
[184] SRS, *supra* note 171 at art 5; Circular of the State Council, *supra* note 170 at art 4.

[185] Apparent examples are electricity, petroleum, banking, insurance, and aviation.
[186] Owen, *supra* note 3 at 240.
[187] Zhang, *supra* note 5 at 491.
[188] Owen, *supra* note 3 at 256.

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