

Chinese Merger Control Developments: GE/Shenhua JV and Alpha V/Savio Conditional Approvals

Two recent decisions by China's Ministry of Commerce ("MOFCOM") shed light on MOFCOM's evolving approach to remedies proposed to resolve competition concerns in Chinese merger review cases:

- On November 10, MOFCOM approved the establishment of a joint venture ("JV") between General Electric (China) Co., Ltd. ("GE China") and China Shenhua Coal to Liquid and Chemical Co., Ltd. ("Shenhua"), subject to the condition that the JV may not force potential licensees for coal-water slurry gasification technologies to use the JV's technology or raise these licensees' cost of using other technologies by restricting feedstock supply or conditioning it on purchasing the JV's technology.¹ According to MOFCOM, GE China has the highest market share among only three main players in the Chinese market for technology licensing for coal-water slurry gasification, while Shenhua's parent company, Shenhua Group, was the largest supplier of feedstock for coal-water slurry gasification in China in 2010. The GE China/Shenhua JV decision is MOFCOM's first conditional joint venture clearance since the implementation of the Anti-Monopoly Law (the "AML") in August 2008, and is notable for imposing behavioral remedies to address vertical concerns in a technology licensing market.
- On October 31, MOFCOM cleared Alpha Private Equity Fund V's ("Alpha V's") acquisition of Savio Macchine Tessili S.p.A. ("Savio"), subject to the condition that Alpha V divest its 27.9% interest in a Swiss competitor of Savio, Uster Technologies AG ("Uster").² According to MOFCOM, Uster and Savio (through its wholly owned subsidiary Loepfe Brothers Ltd.) are the only two producers in the world of electronic yarn clearers for automatic winding. The Alpha V/Savio case is notable because although MOFCOM required Alpha V to divest its interest in Uster,

¹ The decision is available at <http://fdj.mofcom.gov.cn/aarticle/zcfb/201111/20111107824342.html?3789882512=3182119977>.

² The decision is available at <http://fdj.mofcom.gov.cn/aarticle/zcfb/201111/20111107809156.html?2190732749=41285420>.

MOFCOM did not explicitly determine that Alpha V controls Uster. This decision is particularly relevant for private equity groups that may hold a large number of significant but non-controlling portfolio company interests.

I. GE CHINA/SHENHUA JV

GE China and Shenhua proposed to form a joint venture to supply technology licensing and project services for coal-water slurry gasification. MOFCOM started its 30-day Phase I review on May 16, 2011 (about four weeks after the notification was filed), and initiated an in-depth Phase II review on June 15, 2011, which was extended on September 13, 2011. The final conditional clearance was handed down on November 10, 2011.

MOFCOM defined the relevant product market as technology licensing for coal-water slurry gasification and the relevant geographic market as China. MOFCOM found that the market is highly concentrated, with only three main market players, of which the most important is GE China. Coal-water slurry gasification has very specific feedstock requirements, and Shenhua Group was the largest supplier for such feedstock in China in 2010. MOFCOM alleged that the JV might leverage Shenhua Group's market power in feedstock supply and, therefore, concluded that the transaction would likely result in the elimination or restriction of competition.

To resolve these concerns, MOFCOM accepted the following conditions proposed by Shenhua and Shenhua Group. The JV may not force potential licensees of coal-water slurry gasification technology to use the JV's technology and may not raise these licensees' cost of using other technologies by restricting feedstock supply or conditioning feedstock supply on purchasing the JV's technology.

The GE China/Shenhua JV decision is MOFCOM's first published decision regarding joint ventures since China's AML took effect. The notifiability of joint ventures under the AML has been hotly debated, particularly the treatment of non-full-functional joint ventures and joint ventures that are not jointly controlled. Unfortunately, MOFCOM's decision does not provide sufficient detail to determine how it analysed the notifiability of the joint venture in this case.

MOFCOM's current rules on merger remedies deal only with structural remedies (asset or business divestitures).³ MOFCOM has issued no formal guidance regarding behavioral remedies. The GE China/Shenhua JV is an interesting confirmation of

³ MOFCOM's Provisional Rules on Assets or Business Divestiture in Implementing Concentrations between Undertakings took effect in July 2010. MOFCOM is currently in the process of shaping a more comprehensive set of merger remedies rules, which are expected to be promulgated in 2012.

MOFCOM's willingness to consider behavioral remedies to address vertical competition concerns. Unfortunately, the decision does not discuss in detail how the remedies in this case addressed the theories of harm identified by MOFCOM.

II. ALPHA V/SAVIO

Alpha V proposed to acquire Savio, an Italian textile machinery producer. Savio's Loepfe Brothers subsidiary manufactures and sells electronic yarn clearers for automatic winding. Alpha V is a member of a French-based private equity group and owns 27.9% of Uster, a Swiss company that also supplies electronic yarn clearers for automatic winding. MOFCOM started its 30-day Phase I review on September 5, 2011 (about six weeks after the notification was filed), and initiated an in-depth Phase II review on September 30, 2011. The final conditional clearance was handed down on October 31, 2011.

Strikingly, MOFCOM did not determine whether Alpha V's 27.9% interest gives Alpha V control over Uster such that the transaction would result in a horizontal overlap, although MOFCOM reviewed Uster's shareholding structure, voting system in shareholder meetings, historical attendance records at shareholder meetings, and the composition and voting system of the board of directors. The decision does not discuss whether Alpha V enjoys veto rights under shareholder agreements or Uster's constituent documents or whether any such rights would be sufficient to confer "joint control" under EU and other international merger review regimes. MOFCOM concluded only that "a possibility that Alpha V may participate in or influence Uster's business activities cannot be ruled out."

MOFCOM defined the relevant product market as electronic yarn clearers for automatic winding and found that the market is highly concentrated. Uster and Loepfe have 52.3% and 47.7% of the sales of the relevant product worldwide, with similar market shares in China. MOFCOM concluded that the transaction likely would result in the elimination or restriction of competition. Perhaps reflecting its uncertainty about the degree of control Alpha V exercises over Uster, MOFCOM did not articulate a clear theory of harm. MOFCOM indicated that Alpha V would eliminate or restrict competition through its control and influence over Uster and Loepfe, suggesting a traditional unilateral effects analysis. On the other hand, MOFCOM noted that after the concentration Uster and Loepfe could coordinate their businesses, suggesting a coordinated effects analysis.

To eliminate its concerns, MOFCOM accepted the following conditions proposed by the Parties:

- Within six months following the decision, Alpha V will divest its interest in Uster.
- Until the divestiture is complete, Alpha V cannot participate in or influence Uster's business activities.

MOFCOM's Alpha V/Savio decision would not have been surprising had it been a straightforward horizontal overlap case. However, requiring a divestiture in a foreign-to-foreign transaction without even a determination whether the transaction involves a horizontal overlap is unusual. There is no indication that MOFCOM considered a less intrusive behavioral remedy, such as creating firewalls between Savio and Uster.

Tellingly, no other international antitrust authority appears to have objected to the Alpha V/Savio transaction. It is also interesting that MOFCOM's decision refers only to members of the Alpha V group, without considering Alpha V's relations with other funds of the Alpha group.

III. CONCLUSION

MOFCOM's two latest conditional approval decisions shed some light on MOFCOM's evolving remedy policy. Since the AML entered into force, MOFCOM has imposed conditions on nine deals (three in 2011), eight of which involved non-Chinese acquirers and targets and one of which (GE China/Shenhua JV decision) involved a joint venture between a non-Chinese and a Chinese company.⁴ Both the GE China/Shenhua JV decision and the Alpha V/Savio decision reflect MOFCOM's flexible approach to remedies in merger control cases.

MOFCOM has so far only promulgated provisional rules on divestiture remedies⁵ and has expressed concerns about effective enforcement, monitoring and supervision of behavioral remedies. In its nine conditional decisions, however, MOFCOM appears to have applied structural and behavioral remedies about evenly.

A comparison of the relative speed of MOFCOM's approval of the GE China/Shenhua JV and Alpha/Savio suggests the value of offering remedies early in the process. After Alpha V offered remedies in Phase I, Alpha V/Savio was approved early in MOFCOM's Phase II review period. By contrast, in the GE China/Shenhua JV review, the final remedies were only proposed towards the end of Phase II and the case went through an extended Phase II review. The only other case, among the nine conditional clearances, in which Phase II review was extended, was Panasonic/Sanyo.

⁴ MOFCOM blocked one multinational's acquisition of a Chinese target, Coca-Cola's purchase of Huiyuan, soon after the AML entered into force. In another recent case involving the acquisition of a Chinese company by a non-Chinese company, however, MOFCOM cleared the transaction. See http://www.xfy.com.cn/uploadfile/2011/11/8/634563329414843750e_A110901.pdf.

⁵ For a detailed discussion, please refer to our alert memo, available at: http://www.cgsh.com/chinas_mofcom_issues_provisional_rules_on_divestiture_remedies/.

The Alpha V/Savio decision may be significant for private equity funds, which commonly hold significant minority, but non-controlling, stakes in many different companies. The decision indicates that, when preparing to notify proposed acquisitions in China, private equity groups should analyze overlaps between the target and existing portfolio companies in which the acquirer has a significant but non-controlling interest, as well as controlled portfolio companies.

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If you have any questions, please feel free to contact any of your regular contacts at the firm or any of our partners and counsel listed under Antitrust and Competition in the “Practices” section of our website at <http://www.clearygottlieb.com>.

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