

## E-ALERT | Antitrust & China Practice

January 11, 2012

### CHINA'S MERGER CONTROL AGENCY ISSUES "FAILURE TO FILE" REGULATIONS

On January 5, China's Ministry of Commerce ("MOFCOM") issued [new regulations](#) regarding investigations and sanctioning of companies that fail to notify transactions under China's Anti-Monopoly Law ("AML"). Under the regulations, which take effect on February 1, non-compliant companies may be fined up to RMB 500,000 (approx. \$80,000 USD) and ordered to take measures deemed necessary "to restore pre-concentration conditions," such as disposing of any acquired shares or assets. Companies under investigation for a possible failure to file will also be ordered to suspend the transaction pending MOFCOM's investigation, which may last up to eight to ten months, although whether and to what extent the agency may seek to enforce such suspensions beyond business activities in China is not clear.

The regulations signal MOFCOM's increasing vigilance as an antitrust enforcer and may be a reaction to failure by some multinational companies, and perhaps by some state-owned companies as well, to file pre-closing notifications for transactions that meet China's reporting thresholds. As those thresholds are based on the parties' global and Chinese turnover, companies with sales in China should consult with antitrust counsel when planning mergers and acquisitions, to determine whether the transaction may be subject to pre-closing notification and review in China and to develop a coordinated global strategy for securing merger clearance.

#### BACKGROUND

##### Merger Thresholds in China

The AML applies to "concentrations" – mergers, acquisitions of assets or securities that confer control over another company, or the acquisition of "a decisive influence" over another company through contract or other means. A concentration is subject to pre-closing review if the total turnover of all parties exceeds either RMB 10 billion (approx. \$1.5 billion USD) worldwide or RMB 2 billion (approx. \$317 million USD) in China, and if the Chinese turnover of each of at least two parties exceeded RMB 400 million (approx. \$63 million USD) in the preceding fiscal year.

All parties to a merger share the obligation to file, but only the company acquiring control or a "decisive influence" bears the obligation for non-merger concentrations. There are no exemptions under the AML for transactions that take place outside China or that do not involve Chinese businesses or assets.

##### "Failure to File" Regulations

The AML provides for penalties where companies implement a reportable concentration without first submitting the required notification and receiving clearance. The new rules establish the process for investigating and sanctioning non-compliance. They authorize the agency to open an investigation if it has preliminary evidence of a possible failure to file or if it receives a report of a potential violation

from any person—such as a customer or competitor. The rules do not define what constitutes evidence sufficient to support opening an investigation, but the information that companies must provide during the initial stage of such a review suggests that the threshold is low. Upon being informed by MOFCOM that it has opened an investigation, the company or companies potentially responsible for notifying the transaction have 30 days to submit documents and information sufficient to explain why the transaction is not a “concentration,” why it does not meet the notification thresholds, and whether it has been consummated. MOFCOM has 60 days following the receipt of this information to reach a preliminary determination regarding whether a “failure to file” violation has occurred.

If MOFCOM preliminarily concludes that notification should have been made, the company or companies responsible for making the filing must submit the required notification materials within 30 days and suspend implementation of the transaction. The extent to which such suspensions may be applicable to business activities outside China, such as post-closing integration activities in other countries, is not clear. Upon receipt of the notification, MOFCOM will have 180 days to reach a final determination on the filing requirement and to determine whether the transaction “has or will possibly have the effect of excluding or limiting competition.” Upon conclusion of this review, the company or companies will be given a final opportunity to submit comments and materials before MOFCOM reaches its final decision.

### Penalties for Failing to File

If MOFCOM ultimately determines that a “failure to file” violation has occurred, it may impose a fine of up to RMB 500,000 (approximately \$80,000 USD) and require the company or companies “to restore pre-concentration conditions” by terminating the transaction, disposing of any acquired voting securities or assets, selling any acquired businesses, or taking other measures deemed necessary by MOFCOM. In addition to the “nature, gravity, and duration” of the parties’ failure to file, MOFCOM is required to take its competitive assessment of the transaction into account when determining an appropriate penalty. Thus, the agency may decide simply to impose a fine in “failure to file” cases where the concentration does not raise substantive competition concerns. Discretion regarding the penalty, however, rests with MOFCOM.

Given that the maximum fine, which is set by Article 48 of the AML, is relatively small, the most significant penalty for failing to file in most cases may be the cost of delay in implementing the transaction during MOFCOM’s investigation, which under the new rules may last for 240 to 300 days or longer. It remains to be seen how broadly MOFCOM’s orders to suspend transactions during those investigations will apply beyond business activities in China, but the agency has signaled that the investigations themselves may be aggressive, which suggests that it may seek to use them as a further deterrent. On January 10, for example, it issued a statement regarding the new rules in which it pointedly referred to the provisions in the AML which empower it to take tough measures to ensure compliance with its investigations—such as entering a company’s premises, reviewing and seizing evidence, compelling testimony, and imposing fines and even criminal sanctions on companies and individuals for non-cooperation.

Covington is well positioned to assist companies regarding their operations in China. If you have any questions concerning the material discussed in this client alert, please contact the following members of our firm:

<b>John Graubert</b>	+1 202.662.5938	<a href="mailto:jgraubert@cov.com">jgraubert@cov.com</a>
<b>Miranda Cole</b>	+32.(0)2.549.5264	<a href="mailto:mcole@cov.com">mcole@cov.com</a>
<b>James O'Connell</b>	+1 202.662.5991	<a href="mailto:joconnell@cov.com">joconnell@cov.com</a>
<b>Tim Stratford</b>	+ 86.10.5910.0508	<a href="mailto:tstratford@cov.com">tstratford@cov.com</a>

This information is not intended as legal advice. Readers should seek specific legal advice before acting with regard to the subjects mentioned herein.

Covington & Burling LLP, an international law firm, provides corporate, litigation and regulatory expertise to enable clients to achieve their goals. This communication is intended to bring relevant developments to our clients and other interested colleagues. Please send an email to [unsubscribe@cov.com](mailto:unsubscribe@cov.com) if you do not wish to receive future emails or electronic alerts.

© 2012 Covington & Burling LLP, 1201 Pennsylvania Avenue, NW, Washington, DC 20004-2401. All rights reserved.