

# Antitrust & Competition

## Client Alert

Global

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April 2009

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## China merger control: global transactions subject to scrutiny, divestment conditions

- Acquisition of Lucite by Mitsubishi Rayon cleared in China, subject to significant, China-specific divestment conditions
- Filing thresholds mean that many global transactions will now be subject to review and clearance in China
- Decision underlines the need for parties to consider the competitive impact of their transactions in China, and local market conditions, even if the primary focus of a transaction lies elsewhere

On 23 April 2009, following three months of review, the Anti-Monopoly Bureau of the China Ministry of Commerce (**MOFCOM**) issued a statement clearing the acquisition of Lucite International Group Limited ("**Lucite**") by Mitsubishi Rayon Company Limited ("**Mitsubishi Rayon**"). The clearance was, however, subject to a number of substantive conditions, intended to remedy competition concerns MOFCOM had identified on certain chemicals markets in China.

This ruling is significant. It shows that MOFCOM is fully prepared to take a strong stance in applying the new Anti-Monopoly Law, not only in transactions centred close to home (as in the recent, well-publicised prohibition of Coca-Cola's attempt to buy Huiyuan Juice) but also in relation to regional or global deals, where China may not be the only country impacted.

Mitsubishi Rayon describes itself as the leading supplier of methyl methacrylate (**MMA**) in Asia. MMA is a polymer used primarily to produce poly-methyl methacrylate (**PMMA**), or acrylic glass. PMMA, in turn, is used in a wide range of applications as a glass substitute, including TV screens and motorcycle helmets.

While Mitsubishi Rayon's stated objective in acquiring Lucite is the building of a substantive MMA and PMMA presence in Europe, Lucite also has a

significant Asian business, including a manufacturing plant in China.

## **MOFCOM's Concerns**

MOFCOM states that it began its analysis by identifying the relevant markets impacted as MMA and PMMA, with the relevant geographic market for both of these being China. The basis for MOFCOM reaching this view has not been published, though draft Market Definition Guidelines, published in January 2009 and revised in March 2009, set out the overall methodology that MOFCOM applies.

Having established its frame of reference, MOFCOM evaluated the competitive impact of the transaction. According to MOFCOM, the combined business would account for 64% of MMA sales in China. This placed the combined business well ahead of the next largest producers, named as PetroChina Jilin Petrochemical Company and Heilongjiang Zhongmeng Longxin Chemical Company Limited. MOFCOM expressed fears that the combined business would be able to restrict or even exclude competitors such as these from the China market.

MOFCOM also expressed concern that Mitsubishi Rayon would be better able, as a result of the transaction, to restrict competition in the downstream PMMA market. This could be done either by refusing to supply its PMMA competitors with MMA, or giving its own PMMA business preferential terms or access to supply.

## **Remedies**

Mitsubishi Rayon and Lucite presented MOFCOM with a series of undertakings intended to remedy the competition concerns identified. Following negotiations, a revised set of undertakings was submitted by the parties. These were accepted by MOFCOM, and the transaction was cleared on this basis. MOFCOM's announcement sets out the following conditions:

1. Lucite China will agree the sale, to one or more third party buyers, and at cost price, of fifty percent of its MMA production for a period of five years following completion. In order to avoid any need for intensive ongoing monitoring, these sales must be agreed for the full five year period at the outset. An auditor must be engaged by Mitsubishi Rayon to verify that the true cost price is being charged.
2. If sufficient MMA buyers cannot be found within six months (extendable by MOFCOM, at its discretion, to one year), Mitsubishi Rayon agrees to the outright divestment of Lucite China under the supervision of an independent trustee appointed by MOFCOM.
3. Mitsubishi Rayon must continue to operate and manage Lucite's Chinese MMA and PMMA businesses separately from its own between completion and the agreement of a sale of either the requisite MMA output, or Lucite China itself. The two businesses must not exchange any commercially sensitive information (including pricing and customer information) during this period.

4. Unless prior MOFCOM approval is obtained, Mitsubishi Rayon must not make any further acquisitions impacting the MMA, PMMA or related markets in China, or set up any new plants involving production of MMA, PMMA or related products in China, for a period of 5 years following completion.

Violation of the conditions is stated as carrying a penalty for Mitsubishi Rayon of between RMB250,000 (US\$36,600) and RMB500,000 (US\$73,200). MOFCOM also has the ability to unwind the transaction in the event of non-compliance.

## **Analysis**

This case highlights MOFCOM's willingness to intervene in multinational transactions where it believes that competition in China may be adversely affected. It also demonstrates MOFCOM's ability both to identify concerns and agree relatively complex undertakings to remedy them. In this case, the use of a two-tiered remedy gives the parties an opportunity to implement a less drastic approach than outright divestment of assets, while providing MOFCOM with the reassurance of outright divestment should the more novel approach of selling a percentage of future production fail.

MOFCOM's announcement highlights the extent of consultation that took place with other stakeholders. In addition to requesting written comments on the transaction, discussion sessions were organised at which rival producers and trade associations were able to set out their concerns. The outcome of this case again emphasises that MOFCOM will place significant weight on third party comments.

More generally, this case underlines the need for transaction parties to consider merger filings at an early stage in order to avoid unnecessary (and potentially costly) delays. It is notable in this case that, by the date originally announced by the parties for closing the transaction (late January 2009) the transaction was still awaiting clearance in jurisdictions including mainland China and Taiwan.

The express restriction of future M&A or expansion activity echoes the undertakings obtained from InBev in relation to its acquisition of Anheuser-Busch, the only other conditional clearance under the AML to date. In that case, Anheuser-Busch agreed not to buy further shares in four named Chinese brewers without obtaining prior approval from MOFCOM. Similar practice can be found in the US merger control regime. It was, for many years, customary for the US Federal Trade Commission and Department of Justice, in cases raising serious issues, to obtain an undertaking from the buyer not to make further acquisitions on the same markets for a ten year period. Such commitments may now become a standard feature of the Chinese system.

## Practical Implications

- Companies and their advisers must plan ahead if they wish to close transactions in a timely manner. Pre-closing merger reviews now exist in over 70 jurisdictions. These can have very significant timing implications, and even alter the shape of the final transaction. Competition issues should therefore be considered at an early stage.
- Even where China is not the primary focus of a transaction, parties must consider the impact of the deal in China. In this case, conditions were imposed in China due to local competition issues being identified, even though the deal had already been cleared unconditionally in a number of other Asian and European jurisdictions. This ruling confirms that MOFCOM can and will intervene in global transactions where it believes local competition issues exist.
- A significant period of pre-filing correspondence with MOFCOM can be expected, especially where there are issues or a high volume of opposition from customers or competitors. In this case, the review period commenced on 20 January 2009, almost one month after the merger report was initially filed (22 December 2009).
- The views of competitors, customers and trade associations will be actively sought by MOFCOM, and should be anticipated.
- Where significant competition issues are likely to be identified, parties should actively engage with MOFCOM in proposing remedies. As in other jurisdictions, the burden is on the parties, not the regulator, to put forward solutions.
- Where MOFCOM finds remedies acceptable, it appears to be open to clearing transactions before expiry of the full review period (in this case, MOFCOM could have taken until 20 May 2009 to complete its review).
- Although the maximum fine for non-compliance, and indeed outright failure to file, is relatively low (RMB500,000), the ability also exists for MOFCOM to unwind or prohibit transactions under the AML. It remains to be seen how MOFCOM will enforce these powers in practice (particularly where implementation takes place primarily or entirely outside the jurisdiction), though it is already clear that MOFCOM takes enforcement of the AML seriously.
- Companies must also keep in mind their relationship with Chinese authorities more generally, and the wider reputational impact of non-compliance with the AML or failing to file.

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