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I. INTRODUCTION

Long ago, the U.S. Supreme Court confirmed that partial acquisitions are subject to the Clayton Act's prohibition against transactions that may substantially lessen competition. Since that time, the Department of Justice ("DOJ") and Federal Trade Commission ("FTC") have challenged many partial acquisitions (as have private plaintiffs—typically firms attempting to fend off hostile tender offers). And, after years of explaining their views in consent decrees and litigated cases, the agencies included an entire section on partial acquisitions in the 2010 *Horizontal Merger Guidelines*. While the agencies have challenged partial acquisitions in a variety of contexts and have imposed a variety of remedies, all such challenges share an underlying theme—there must be more than an "ephemeral possibility" that a transaction may cause competitive harm.[2] As one court has explained, in order to violate the Clayton Act, a transaction must create an "appreciable danger" of anticompetitive effects.[3]

Merger enforcement in China is not as well-established as it is in the United States and the Ministry of Commerce of the People's Republic of China ("MOFCOM") is still developing its substantive and procedural standards. There is no doubt, however, that, as in the United States, partial acquisitions can violate China's Anti-Monopoly Law ("AML"), although MOFCOM has provided little guidance to date on how it will apply the AML to partial acquisitions. MOFCOM's recent enforcement action in the Alpha V-Savio transaction required remedies because MOFCOM "could not rule out the possibility" that a partial acquisition "might have" anticompetitive effects. Whether this recent action suggests that MOFCOM may be adopting something akin to an ephemeral possibility standard, and will be much less tolerant of partial acquisitions than their counterparts in the United States, remains to be seen.

II. U.S. ANTITRUST ANALYSIS OF PARTIAL STOCK ACQUISITIONS

A. Relevant U.S. Antitrust Laws

Section 7 of the Clayton Act provides that "[n]o person…shall acquire…the whole *or any part*" of the stock or assets of another entity where "the effect of such acquisition may be substantially to lessen competition, or to tend to create a monopoly."[4] (emphasis added). While

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[2] *United States v. Marine Bancorp, Inc.*, 418 U.S. 602, 623 (1974).

[3] *Hosp. Corp. of Am. v. FTC*, 807 F. 2d 1381, 1389 (7th Cir. 1986) ("Section 7 does not require proof that a merger or other acquisition has caused higher prices in the affected market. All that is necessary is that the merger create an appreciable danger of such consequences in the future." (citing *United States v. Philadelphia Nat'l Bank,* 374 U.S. 321, 362 (1963)).

[4] 15 U.S.C. §18. In addition to §7 of the Clayton Act, acquisitions can also be challenged under §1 of the Sherman Act (15 U.S.C. §1). A pre-consummation challenge under §1 of the Sherman Act alone is less likely to be

the Clayton Act expressly applies to the acquisition of "any part" of a company, neither the statute itself nor court doctrine interpreting it has established a threshold or minimum stock purchase amount that triggers potential competitive concerns. As a result, there are no bright line rules as to when a partial acquisition does (or does not) violate the U.S. antitrust laws and the analysis of any particular partial acquisitions is highly dependent upon the specific facts of each proposed transaction.[5]

B. DOJ and FTC Guidance on Partial Stock Acquisitions

Prior to 2008, the U.S. antitrust agencies' enforcement guidance on partial acquisitions was provided through consent decrees and litigated matters. For example, in 1998, DOJ challenged Northwest Airlines' proposed acquisition of 15 percent of Continental Airlines. In opposition to Northwest's motion for summary judgment DOJ explained that partial acquisitions could harm competition in several ways:

1. The acquiring firm might have a unilateral incentive to compete less vigorously with the target firm;
2. The target firm might have a corresponding incentive to compete less vigorously against a significant shareholder of its stock;
3. The acquisition might weaken the target firm's ability to compete by creating uncertainty with the target firm that can lead to loss of key employees and organizational morale; and/or
4. A partial acquisition might make collusion or cooperation between the two firms more likely (*e.g.*, through the exchange of competitively sensitive information).[6]

The U.S. antitrust agencies provided their most direct guidance on how they analyze partial stock acquisitions with the release of the 2010 *Horizontal Merger Guidelines* ("*Merger Guidelines*").[7] In the *Merger Guidelines*, the agencies devoted an entire section to partial acquisitions and explained that "[t]he Agencies…review acquisitions of minority positions involving competing firms, even if such minority positions do not necessarily or completely eliminate competition between the parties to the transaction."[8] Following the prior enforcement actions, the *Merger Guidelines* identify three principal competitive concerns with partial acquisitions.[9]

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successful as it is not an incipiency statute like §7 of the Clayton Act that prohibits likely or probable future effects. Under §1 of the Sherman Act, a plaintiff challenging an acquisition bears the burden proving an existing anticompetitive effect. *See, Texasgulf, Inc. v. Canada Dev. Corp.*, 366 F. Supp. 374, 406 (S.D. Tex. 1973) (rejecting a §1 claim brought by a target of a tender offer for 35 percent of its stock because of a lack of present anticompetitive effect).

[5] §7 of the Clayton Action includes a "solely-for-investment" exemption but this exemption does not exempt or immunize partial stock acquisitions involving competitors. *See*, *United States v. Tracinda Inv. Corp.*, 477 F. Supp. 1093, 1098 (C.D. Cal. 1979) (test for "solely-for-investment" exemption inherently no different than the analysis proscribed by §7 itself); *Anaconda Co. v. Crane Co.*, 411 F. Supp. 1210, 1219 (S.D.N.Y. 1975) (same); *see also*, AREEDA & HOVENKAMP, ANTITRUST LAW ¶1204(b) ("The investment exception is better seen as serving the much more limited function of reassuring investors, particularly institutional investors, that the Clayton Act was not designed to interfere with general investment….") ("Areeda").

[6] *Memorandum in Opposition to Defendant Northwest Airlines' Motion for Summary Judgment* (July 28, 2000), *available at* http://www.justice.gov/atr/cases/f6100/6161.htm.

[7] *Available at* http://www.justice.gov/atr/public/guidelines/hmg-2010.html.

[8] *Id*. at ¶13.

[9] Shortly after the 2010 Merger Guidelines, the U.S. antitrust agencies required through the new HSR form more detailed information to identify potentially anticompetitive partial ownerships. The HSR form now requires

First, a partial acquisition can lessen competition by enabling the acquiring firm to influence the competitive conduct of the target firm. Although not an exhaustive list, such influence can be derived either from a voting interest in the target firm or specific governance rights (i.e. right to appoint members to the board of directors). This influence has the ability to lessen competition as the acquiring firm can use its leverage to induce the target firm to compete less aggressively or to coordinate the conduct between the target and acquiring firm.

Second, a partial acquisition can reduce the incentive of the acquiring firm to compete. For example, if the acquiring firm increases its competition with the target firm, then the target firm could, for example, suffer economic losses from lost sales. But in causing the target to suffer economic loss, the acquiring firm would now also incur losses through its percentage of ownership in the target firm. Therefore, in order to protect its investment in the target firm, the acquiring firm would no longer have the same incentive to compete aggressively with the target firm. The *Merger Guidelines* note that this effect of reduced competitive incentive can arise even if the acquiring firm is unable to influence or control the conduct of the target.

Third, a partial acquisition can enable the acquiring firm to gain access to non-public competitively sensitive information from the target firm. Even if the acquiring firm has no ability to influence the conduct of the target firm, access to competitively sensitive information makes adverse unilateral or coordinated effects possible.

C. Recent Partial Acquisition Enforcement Actions

While it is easy to articulate theories of competitive harm in partial acquisition situations, applying these theories in practice is often a difficult exercise. Indeed, the agencies state "[p]artial acquisitions…vary greatly in their potential anticompetitive effects…the specific facts of each case must be examined to assess the likelihood of harm to competition."[10] Consistent with this guidance, the enforcement actions over the years show no discernible pattern in the percentage of ownership that might trigger concerns or how the agencies attempt to remedy those concerns.

Despite the lack of clear rules or guidance, the enforcement actions by the agencies fit into three general buckets:

1. The Acquiring Firm is the Direct Competitor of the Target Firm or the Target Firm's Partial Ownership Interest

The range of the percent of ownership that has drawn the scrutiny of the agencies in this bucket has been anywhere between just under 30 percent to as low as 7.5 percent.[11] With this

information about "associates" that requires the acquiring entity to provide information on entities that are under common investment or operation management with itself.

[10] 2010 Horizontal Merger Guidelines at ¶13.

[11] *See e.g.*, (1) Clear Channel Communications Inc.'s purchase of AMFM, Inc. which had a 28.6 percent equity interest in a direct competitor of Clear Channel; (2) AT&T's purchase of TCI, which had a 23.5 percent equity interest in one of AT&T's direct competitor in wireless phone operations; (3) U.S. West's purchase of Continental Cablevision, which had a 20 percent equity interest in a direct competitor of U.S. West; (4) Northwest Airlines' purchase of 15 percent of its direct competitor's equity, Continental Airlines; (5) American Airlines' purchase of 8.5 percent of its direct competitor's equity, Aerolineas; (6) TCI's direct purchase of 7.5 percent of Time Warner's equity, which was its direct competitor, with an option to purchase another 7.5 percent interest; and (7) Lockheed Martin's purchase of the defense-related business of Loral Corp. that included a 20 percent interest in Loral Space & Communications, which owned a 33 percent interest in Space Systems/Loral, which was a direct competitor of Lockheed.

wide range of ownership interests, the agencies have required various remedies to alleviate their competitive concerns. For example, in the Clear Channel/AMFM, the AT&T/TCI, and the US West/Continental Cablevision transactions, the agencies required full divestment of the partial stock ownership in the competitor to the acquiring firm.

The consistent fact across these three transactions that required full divestment is that they involved partial ownership interests that exceeded 20 percent ownership. Alternatively, in the Northwest-Continental matter, the agencies did not require Northwest Airlines to divest its entire 15 percent ownership of Continental Airlines but instead required it to divest its interest to no more than 5 percent, and American Airlines was allowed to retain its entire 8.5 percent equity interest in Aerolineas by converting its interest into a passive ownership interest. With respect to TCI's ownership stake in Time Warner, the FTC permitted TCI to choose to either divest its 7.5 percent interest in Time Warner entirely or accept a non-voting interest capped at 7.5 percent.

2. The Acquiring Firm Has a Controlling Interest in the Direct Competitor of the Target Firm or an Investment of the Target Firm

Within this second bucket are transactions where the acquiring firm owns a controlling interest in another firm, and it is this ownership interest that competes directly either with the target firm or an ownership interest of the target firm.[12] As seen in the fist bucket, the transactions in the second bucket each encountered different requirements to appease the agencies. After some litigation and before a second trial could commence, DFA fully divested its 50 percent interest in one of the competing dairies it owned; in order to acquire MediaOne, AT&T had to fully divest MediaOne's 34 percent interest in RoadRunner; and, finally, in order to acquire partial ownership in Kinder Morgan, the investment funds Carlyle and Riverstone had to make its 50 percent ownership in Magellan completely passive and put into place numerous competitive firewalls to ensure competitive information did not get exchanged regarding Kinder Morgan and Magellan.

3. The Acquiring Firm Has a Non-Controlling Interest in the Direct Competitor of the Target Firm

In the final bucket are transactions where the partial equity interest at issue is a non-controlling interest in a firm owned by the acquiring firm that competes directly with the target firm.[13] With all of the transactions in this non-controlling interest bucket, the agencies have

[12] *See e.g.*, (1) Carlyle & Riverstone jointly owned a fund that had a 50 percent interest in another fund that was the controlling partner of Magellan Midstream Partners, who was a direct competitor of Kinder Morgan, which was being bought out by a conglomerate of equity funds that included an 11.3 percent interest by Carlyle and another 11.3 percent interest from a fund jointly owned by Carlyle and Riverstone; (2) Dairy Farmers of America ("DFA") owned a 50 percent interest in a Flav-O-Rich dairy that competed directly in Kentucky and Tennessee with a proposed 50 percent acquisition of a dairy owned by Southern Belle by DFA; and (3) AT&T proposed to buy MediaOne and both companies had ownership interests of competitors in the residential broadband market—AT&T owned 26 percent of Excite@HomeCorp, while MediaOne had a 34 percent equity interest in the company that operated RoadRunner.

[13] *See e.g.*, (1) prior to attempting to acquire Hispanic Broadcasting Corporation ("HBC"), Univision held a 30 percent interest in Entravision, which was a direct competitor to HBC; (2) Lockheed Martin had a 34 percent interest in L-3 Communications, L-3 Communications proposed to acquire the Ocean Systems business unit from AlliedSignal, where Ocean Systems was a direct competitor of Lockheed Martin for towed sonar arrays; and (3) Medtronic had a 10 percent equity interest in Survivalink, which competed directly with Medtronic's acquisition target Physio-Control.

primarily relied on behavioral remedies instead of divestment of all or part of the equity interest. For example, in order for Univision to complete its acquisition of HBC, Univision had to: (1) reduce its investment in Entravision from 30 percent to 15 percent within the first three years and then down to 10 percent within the first six years of the deal closing; (2) convert the equity interest into a passive ownership interest; and (3) establish firewalls to protect against the exchange of competitively sensitive information between the parties. Medtronic, with its acquisition of Physio-Control, was able to complete its transaction by converting its 10 percent interest in Survivalink to a passive investment. Finally, L-3 Communications was permitted to acquire from AlliedSignal the Ocean Systems business unit by: (1) establishing firewalls to ensure that any business decisions made by L-3 concerning towed arrays would be made without sharing or receiving non-public information from Lockheed Martin; and (2) that L-3 and Lockheed Martin would compete separately for Department of Defense towed array contracts.

As this summary of the U.S. antitrust agencies' actions shows, there is no obvious ownership threshold that can be used to predict, with confidence, when a partial ownership will trigger an agency's concerns. But, when the agency does identify concerns, the likely remedy (or remedies) is less difficult to predict. For example, an acquiring firm can expect to divest either in whole, or at least in part down to a passive investment, the partial equity interest when that interest competes directly with the acquiring firm's activities.[14] But behavioral remedies, like converting a voting equity interest into a passive interest or implementation of firewalls for competitively sensitive information, are more likely to be acceptable when the acquiring firm owns a non-controlling interest in an entity that competes directly with the target firm of a transaction.[15]

III. EMERGENCE OF CHINA'S ANTITRUST JURISPRUDENCE REGARDING PARTIAL STOCK ACQUISITIONS

While China's AML has only been in effect since August 1, 2008, the same underlying anticompetitive concerns with partial stock acquisitions seen in the United States are now being expressed in China. But while the underlying theories of harm are the same, a recent MOFCOM action suggests that it might be less tolerant of partial acquisitions than the U.S. courts and enforcement agencies. Time will tell whether MOFCOM's most recent action is a sign of heightened enforcement and a divergence from U.S. substantive standards, or an anomaly due to the particular facts and circumstances in that case.

A. Relevant Chinese Law

The AML prohibits transactions that have or may have the effect of excluding or restricting competition in the relevant geographic and product market. Mergers or acquisitions with the above effects may be illegal under the AML when an operator acquires: (i) the right of control over another operator by means of asset or equity acquisitions or contractual

[14] *See e.g.,* Clear Channel's divestment of AMFM's entire 28.6 percent interest in Clear Channel's competitor Lamar Advertising; Northwest Airlines reduction of ownership of Continental Airlines from 15 percent down to no more than 5 percent; and American Airlines requirement of converting its 8.5 percent equity interest in Aerolineas into a passive investment.

[15] *See e.g.*, L-3 Communications acquisition of Ocean Systems that required firewalls to be implemented to eliminate sharing of competitively sensitive information between Lockheed Martin, who had a 34 percent interest in L-3, and its competitor Ocean Systems; and Medtronic's acquisition of Physio-Control that required Medtronic to convert its 10 percent voting stock interest in Survivalink, a competitor of Physio-Control, into a passive investment.

arrangements, and (ii) the capability of exerting decisive influence over another operator. As in the United States, the acquisition of "any part" of another operator could trigger the antitrust review process if the transaction reaches the filing threshold under the *Provisions of the State Council on the Standards for Filing of Concentration of Business Operators*.[16] The AML authorizes MOFCOM, one of the AML enforcement agencies, to impose restrictive conditions on a concentration deal for the purpose of lessening the adverse effect of the transaction on competition. One possible restrictive condition is a requirement that the parties divest certain assets or interests.

B. Relevant Chinese Cases

Unlike in the United States, where the enforcement agencies have a history of challenging partial acquisitions and requiring divestments of equity interests, MOFCOM has only imposed divestment obligations as conditions for approving two minority shareholding deals since China launched its M&A review system: the SANYO Electric Co., Ltd. ("Sanyo")-Panasonic Corporation ("Panasonic") transaction in 2009 ("Panasonic Deal") and the proposed acquisitions of Savio Machine Tessilli SpA ("Savio"), an Italian manufacturer of yarn-clearing machinery, by Alpha Private Equity Fund V ("Alpha V") in 2011 ("Alpha V Deal").

As a condition for its approval of the Panasonic Deal, MOFCOM required Panasonic to reduce its ownership stake in PEVE, a joint venture between Panasonic and Toyota Motor Corporation, from 40 percent to 19.5 percent within six months after the consummation of the deal. MOFCOM's concerns in this matter resulted from the fact that PEVE, Panasonic, and Sanyo were the only competitors in the market for "vehicle Ni - MH batteries," with PEVE holding 77 percent of the market. Thus, not only would the transaction reduce the number of players from three to two, the parties to the transaction would own 40 percent of the only other player (the dominant firm) in the market. Given this market structure and Panasonic's interest in the PEVE joint venture, MOFCOM expressed concerns that the merger of Sanyo into Panasonic would reduce the number of competitors and allow Panasonic to take advantage of its influence over PEVE to lessen competition.

To remedy these concerns, in addition to requiring Panasonic to reduce its position in PEVE from 40 percent to 19.5 percent, MOFCOM required Panasonic to waive: (i) its voting rights at PEVE's shareholders meeting, (ii) its right to designate directors to PEVE's board, and (iii) its veto power with respect to PEVE's vehicle Ni - MH battery business.

The more recent, and potentially more troubling, matter involved Alpha V's proposed acquisition of Savio. The acquiring entity in that matter, Apef Management Company 5 Limited ("Apef 5"), had previously made investments through Alpha V in various related and non-related industries to Savio's business, including a minority shareholding (27.9 percent) in Uster Technologies AG ("Uster"), a competitor to Savio's Loepfe Brothers Ltd ("Loepfe") business. According to MOFCOM, Uster and Loepfe controlled 100 percent of the global and Chinese markets for automatic yarn-clearing machinery. Given Alpha V's minority shareholding in Uster,

[16] A transaction will be subject to the antitrust review if: (1) the total turnover on a global basis for the last accounting year of the transaction parties exceeds RMB 10 billion (approximately US$ 1.46 billion), and at least two parties have turnover in China for the last accounting year exceeding RMB 400 million (approximately US$ 58.57 million) each; or (2) the total turnover in China for the last accounting year of the transaction parties exceeds RMB 2 billion (approximately US$ 292.83 million), and at least two parties have turnover in China for the last accounting year exceeding RMB 400 million each.

MOFCOM explored whether or not Alpha V participated in or had sufficient control over the operations of Uster to raise competitive concerns.

For this purpose, MOFCOM investigated, among other issues, the state of competition, supply and demand factors, procurement processes, and barriers to entry in the relevant markets, and obtained data from the parties, third parties, and industry experts. In addition to exploring the competitive dynamics in the relevant markets, in order to evaluate Alpha V's ability to use its minority shareholdings in Uster to exercise influence or control, MOFCOM reviewed Uster's equity structure, voting mechanisms at shareholder meetings, historical attendance records of such general meeting of shareholders, and the composition and voting mechanism of its board of directors. After this investigation MOFCOM raised competitive concerns with the transaction because the market was highly concentrated (Uster and Loepfe were the only meaningful players in China and on a worldwide basis) and barrier to entry was high.

MOFCOM's explanation and analysis of the competitive issues mirror what one would expect to see in the United States. MOFCOM's approach to the Alpha V partial ownership in Uster, however, was more notable, and is potentially controversial if it reflects how MOFCOM intends to pursue such matters in the future. While there is nothing particularly notable or controversial in MOFCOM expressing concerns about one competitor having the ability to exercise significant influence over another in a two-firm market, that was not the basis for MOFCOM's concerns. Rather, MOFCOM imposed conditions on Alpha V's acquisition of Savio on the basis that it could not rule out the possibility that Alpha V might participate in or influence the operations of Uster. While only a single case, the standard applied by MOFCOM in this matter opens the door for divergence with the U.S. approach.

Given MOFCOM's concerns, Apef 5 proposed, and MOFCOM accepted, the following conditions for the Alpha V Deal:

1. Apef 5 is required to divest Alpha V's minority shareholding in Uster to an independent third party within six months upon the issuance of MOFCOM's conditional approval of the deal;
2. Apef 5 is required to report to MOFCOM on details of the divestiture so that the divestiture will not create new competitive concerns;
3. Apef 5 must not participate in or exert any influence over the operations and management of Uster before the disposal of Alpha V's minority shareholding in Uster is completed; and
4. Apef 5 must appoint an independent trustee to supervise the disposal of Alpha V's minority interest in Uster.[17]

IV. CONCLUSIONS

While MOFCOM's two enforcement actions involving partial acquisitions involve the same substantive antitrust analysis that has been applied for decades in the United States, MOFCOM's recent decision in the Alpha V Deal is potentially troubling because of the evidentiary standard that MOFCOM seems to have applied. MOFCOM required Apef 5 to

[17] With respect to the divestiture itself, MOFCOM's decision is consistent with MOFCOM's 2010 *Provisional Measures on the Implementation of the Divestiture of Assets or Business Imposed on Concentration of Undertakings* and is also broadly consistent with other antitrust enforcers' approaches.

divest its indirect minority ownership interest in Uster not because MOFCOM **actually found** that Apef 5 (through Alpha V) would have control over both Uster and Loepfe (through Savio) post-transaction, or in U.S. terms, because there was an appreciable danger that Apef 5 would exercise such control. Instead MOFCOM imposed conditions on the basis that it **could not rule out the possibility** that Alpha V **might have** the possibility to control both businesses. If applied in future matters, a "cannot rule out the possibility" standard would likely result in additional enforcement activity in China and, perhaps more importantly, significant divergence with the standard required for finding a competitive harm in the United States