Antitrust® Chronicle

MARCH · WINTER 2023 · VOLUME 3(2)

Year of the Rabbit: Antitrust in China

CPI COMPETITION POLICY® INTERNATIONAL

TABLE OF CONTENTS

04 Letter from the Editor

05 Summaries

07 What's Next? Announcements

08 CPI TALKS Q&A
By with Qing Li

11 HIGHLIGHTS AND ISSUES CONCERNING THE AMENDMENT OF CHINA'S ANTIMONOPOLY LAW
By Xiaoye Wang

18 IN PRAISE OF SAMR's BEHAVIORAL REMEDIES: PREVENTING OVER-DETERRENCE IN GLOBAL MERGER CONTROL
By Andrew Foster & Cindy Lau

28 MERGER REMEDIES IN CHINA IN 2022 AND THE PREVALENCE OF "CONTINUE TO SUPPLY UNDER FRAND PRINCIPLES" AS THE REMEDIES
By John Yong Ren, Christine Zhang & Schiffer Shi

36 WHAT TO EXPECT OF CHINESE MERGER CONTROL REVIEWS OF GLOBAL SEMICONDUCTOR DEALS FOLLOWING AMENDMENTS TO THE ANTI-MONOPOLY LAW
By Hazel Yin, Haoyang Zhuo & Laurent Bougard

43 A REFLECTION ON CHINA'S AML ENFORCEMENT RE CONCENTRATIONS OF UNDERTAKINGS IN THE INTERNET INDUSTRY
By Roger Xin Zhang

51 THE NOT-SO-SILK ROAD: THE PROLIFERATING REGULATORY OBSTACLES TO CHINESE INVESTMENT IN THE U.S.
By David Pearl & Bella Solórzano

61 THE INTERACTION OF IPRs AND ANTITRUST: FROM THE PERSPECTIVE OF CHINESE PRIVATE ANTITRUST LITIGATIONS
By Hao Zhan, Ying Song & Ruichen Liu

Editorial Team

Chairman & Founder
David S. Evans

Senior Managing Director
Elisa Ramundo

Editor in Chief
Samuel Sadden

Senior Editor
Nancy Hoch

Latin America Editor
Jan Roth

Associate Editor
Andrew Leyden

Junior Editor
Jeff Boyd

Editorial Advisory Board

Editorial Board Chairman
Richard Schmalensee - *MIT Sloan School of Management*

Joaquín Almunia - *Sciences Po Paris*

Kent Bernard - *Fordham School of Law*

Rachel Brandenburger - *Oxford University*

Dennis W. Carlton - *Booth School of Business*

Susan Creighton - *Wilson Sonsini*

Adrian Emch - *Hogan Lovells*

Allan Fels AO - *University of Melbourne*

Kyriakos Fountoukakos - *Herbert Smith*

Jay Himes - *Labaton Sucharow*

James Killick - *White & Case*

Stephen Kinsella - *Sidley Austin*

Ioannis Lianos - *University College London*

Diana Moss - *American Antitrust Institute*

Robert O'Donoghue - *Brick Court Chambers*

Maureen Ohlhausen - *Baker Botts*

Aaron Panner - *Kellogg, Hansen, Todd, Figel & Frederick*

Scan to Stay Connected!
Scan or click here to sign up for CPI's **FREE** daily newsletter.

LETTER FROM THE EDITOR*

Dear Readers,

We are delighted to release our CPI Antitrust Chronicle for March 2023, *Year of the Rabbit: Antitrust in China*. This collection of eight excellent articles is contributed by distinguished authors, including a former deputy director general at China's anti-monopoly agencies, a distinguished scholar who is a pioneer of Competition Law in China, and several top practitioners in leading antitrust law firms and law schools. This Chronicle covers a wide range of hot topics such as the amendment to China's Anti-Monopoly Law ("AML"), merger remedies, the role of national security review on cross-border M&A transactions, as well as various important sectors including semiconductors, digital platforms, just to name a few.

The following is a snapshot of the articles:

The Chronicle opens with an interview with **Qing Li**, a Vice President of China's Society of Economic Reform and a former deputy director general at China's SAMR and NDRC. It covers several topics, including the amendment of China's AML, the fair competition review system, the application of economic analysis to antitrust practice in China, and an outlook on the development of competition policy in China.

The second article is contributed by **Professor Xiaoye Wang**, a prestigious professor who witnessed the birth of China's AML. It provides an in-depth review of the amendment of the AML in June 2022.

The next several articles discuss the important developments on China's merger reviews. The article by **Andrew Foster and Cindy Lau** discusses continued willingness and flexibility of SAMR to accept behavioral remedies, and then compares SAMR with its U.S. and EU counterparts.

The article by **John Yong Ren, Christine Zhang, and Schiffer Shi** summarizes key procedural developments and competitive concerns in transactions with the conditional approvals in China's merger review in 2022.The article by Hazel Yin, Haoyang Zhuo and Laurent Bougard assesses what global semiconductor players and investors should expect under the amendment of AML regarding semiconductor transactions.

China's AML enforcement in the digital economy in the past three years has attracted attention worldwide. The article by **Roger Xin Zhang**, a researcher at Center for Competition Policy Studies of Shandong University, summarizes the characteristics of the AML enforcement on the concentration of digital platform operators in China.

The article by **David Pearl & Bella Solórzano** reviews past CFIUS actions that have affected companies with ties to China and details recent and potential future legislation and executive action that may further affect Chinese M&A activity in the United States (and vice versa).

Last but not least, the article by **Hao Zhan, Ying Song, and Ruichen Liu** analyzes two recent litigations in China, the Transformer Charger and the Hitachi Metals, to provide a better understanding of Chinese courts' attitudes towards the interaction between antitrust law and intellectual property law.

We would like to thank our contributors for their efforts and dedication to our March 2023 CPI Antitrust Chronicle, and hope you enjoy reading this special China issue.

Sincerely,

Elizabeth Xiaoru Wang, Ph.D.
Kun Huang, Ph.D.
Zhou Zhong, Ph.D.

*CPI thanks Compass Lexecon for their sponsorship of this issue of the Antitrust Chronicle. Sponsoring an issue of the Chronicle entails the suggestion of a specific topic or theme for discussion in a given publication. CPI determines whether the suggestion merits a dedicated conversation, as is the case with the current issue of the Chronicle. As always, CPI takes steps to ensure that the viewpoints relevant to a balanced debate are invited to participate and that the quality of our content maintains our high standards.

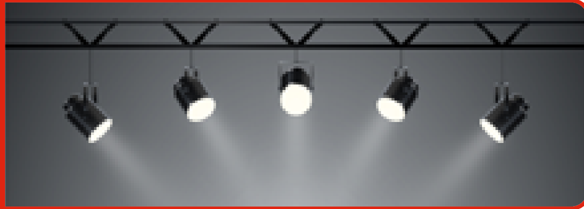
SUMMARIES

08

CPI TALKS Q&A
with Qing Li

In this edition of CPI Talks we have the pleasure of speaking with Qing Li, Vice President of the China Society of Economic Reform and former Deputy Director General at China's SAMR and NDRC.

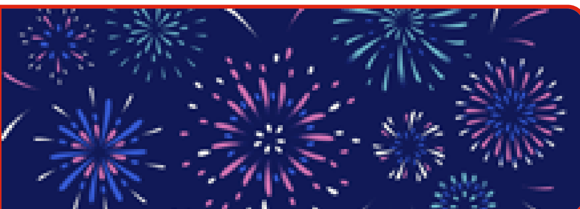
11



HIGHLIGHTS AND ISSUES CONCERNING THE AMENDMENT OF CHINA'S ANTIMONOPOLY LAW
By Xiaoye Wang

The first amendment to the *Anti-Monopoly Law of the PRC* came into effect in August 2022 since it was promulgated in 2007. From a macro perspective, this amendment emphasizes the fundamental status of competition policy in the various national economic policies and introduces fair competition review system; while in terms of micro aspects, it strengthens anti-monopoly enforcement in the digital economy, introduces 'safe harbor' rule for some vertical agreements, and enhances legal deterrence for anticompetitive violations. Nevertheless, the revised AML contains some issues worth further discussion and improvement, in particular it should not only recruit new contents, but also scrap some outdated provisions with theoretical or practical defects.

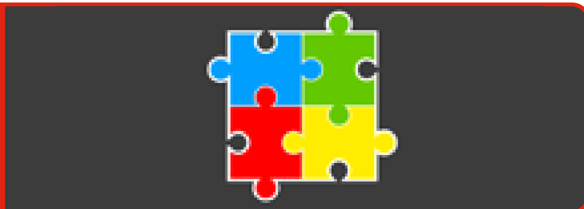
18



IN PRAISE OF SAMR's BEHAVIORAL REMEDIES: PREVENTING OVER-DETERRENCE IN GLOBAL MERGER CONTROL
By Andrew Foster & Cindy Lau

This article examines the use of behavioral remedies in merger control in China, and contrasts it with the stance opposing conduct remedies in the U.S., UK, and other jurisdictions including Australia and Germany. It argues that acknowledgement of the benefits offered by behavioral remedies can eliminate a serious risk of over-enforcement, avoiding a chilling effect on even pro-competitive mergers and acquisitions ("M&As"). The nearly fifteen years' experience of implementing behavioral remedies in China demonstrates that many common complaints about behavioral remedies may be overstated, including monitoring difficulties and ineffectiveness at remedying vertical or conglomerate concerns. As many agencies and regulators move away from the traditional "consumer welfare" standard to consider the impact of a transaction more holistically, China's experience shows that behavioral remedies can be an important and useful tool for regulators to achieve a balance between protecting market competition and incentivizing, or at least not over-deterring, legitimate M&A activities.

28

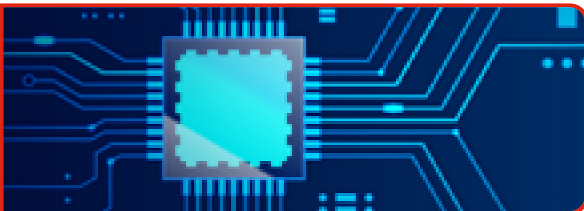


MERGER REMEDIES IN CHINA IN 2022 AND THE PREVALENCE OF "CONTINUE TO SUPPLY UNDER FRAND PRINCIPLES" AS THE REMEDIES
By John Yong Ren, Christine Zhang & Schiffer Shi

This Article examines the remedy imposed on the conditional approvals in China's merger review in 2022. The five cases of conditional approvals in 2022 are summarised from both procedural and substantive perspectives with the behavioural remedy of "continue to supply under FRAND principles" highlighted. This article studies the prevalence of the remedy of "continue to supply under FRAND principles" in the recent years and analyses SAMR's reasoning behind. The prevalence of "continue to supply under FRAND principles" can resulted from the need to provide extra protection for contract performance and may also serve as an option to address both competition concerns and industry concerns in light of the AML's multi-dimensional goals. In addition, the reference of such remedy can also provide both the transaction parties and SAMR the foreseeability and predictability to a large extent. As such, we believe such remedy is likely to continue to be frequently imposed in the future.

SUMMARIES

36



WHAT TO EXPECT OF CHINESE MERGER CONTROL REVIEWS OF GLOBAL SEMICONDUCTOR DEALS FOLLOWING AMENDMENTS TO THE ANTI-MONOPOLY LAW

By Hazel Yin, Haoyang Zhuo & Laurent Bougard

The long list of semiconductor transactions around the globe in the past few years underlines China's continuing role as one of the key jurisdictions for global semiconductor transactions and their clearance prospects under applicable merger control laws. On June 24, 2022, China's top legislature formally published the amended Anti-Monopoly Law, with sweeping changes in force from August 2022. While it does not specifically target the semiconductor industry, it may impact the merger control review practices applicable to semiconductor deals, particularly considering that the semiconductor industry is one of the most heavily scrutinized sectors in China. This article assesses what global semiconductor players and investors should expect when pursuing a clearance in this new antitrust era in China.

43

A REFLECTION ON CHINA'S AML ENFORCEMENT RE CONCENTRATIONS OF UNDERTAKINGS IN THE INTERNET INDUSTRY

By Roger Xin Zhang

China's application of competition law in the digital economy in the past three years has attracted attention worldwide. One significant reason is because of the regulation of VIE-structured transactions. For more than 10 years after the implementation of the Anti-Monopoly Law, seldom VIE-structured transactions have been reviewed by the competition authority, which means, almost the whole internet industry hasn't made notifications of concentrations and there were no investigations for a decade. The whole thing has been turned around by end of 2020, when the State Administration of Market Regulation released the Guidelines for Anti-monopoly in the Field of Platform Economy (Draft for Solicitation of Comments) in November and specifically stated that VIE-structured transactions should be notified with SAMR if the thresholds are satisfied. Ever since then, SAMR has officially kicked off the review of the concentration of Internet undertakings, many historical transaction issues have surfaced, and new investments have been imposed with the notification obligation. This article attempts to summarize the characteristics of anti-monopoly law enforcement concerning Internet industry operators in China by reviewing the law enforcement in the past three years and conduct a summary analysis of some of the problems.

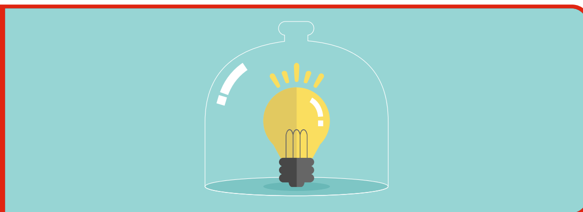
51

THE NOT-SO-SILK ROAD: THE PROLIFERATING REGULATORY OBSTACLES TO CHINESE INVESTMENT IN THE U.S.

By David Pearl & Bella Solórzano

All companies engaged in M&A activity in the United States must plan for enhanced scrutiny from an increasingly aggressive DOJ and FTC, but non-U.S. companies, particularly Chinese companies, must also reckon with another U.S. regulatory regime with the power to scuttle their deals: the Committee on Foreign Investment in the United States, or CFIUS. CFIUS is a U.S. interagency body that assesses the risk to national security of transactions involving non-U.S. acquirers. Coincident with the trade war between the U.S. and China begun during the Trump Administration, CFIUS gained a host of new powers that enable it to investigate more transactions, and, if it deems necessary, impose national security-related conditions to closing or block transactions altogether. And interest remains high in the U.S. Congress and Executive Branch to create additional vector to scrutinize Chinese investment even beyond CFIUS. As such, this paper seeks to demystify CFIUS and offer practical guidance for attorneys and their non-U.S. clients on how to think about parallel DOJ/FTC and CFIUS review of a transaction.

61



THE INTERACTION OF IPRs AND ANTITRUST: FROM THE PERSPECTIVE OF CHINESE PRIVATE ANTITRUST LITIGATIONS

By Hao Zhan, Ying Song & Ruichen Liu

In recent years, the complicated relationship between intellectual property rights and antitrust have drawn increasing attention of Chinese courts in private antitrust litigations. China's Supreme People's Court has made great efforts trying to find a balancing approach when assessing antitrust behaviors in the form of exercise of intellectual property rights, by considering both the factors of market competition and innovation in the individual case. Two representative cases, the Transformer Charger Case and the Hitachi Metals Case, can provide some guidance to better understand Chinese courts' attitudes towards the interaction between antitrust law and intellectual property law, against the backdrop of patent settlement agreements and non-SEPS. This article summarizes the development of related legislation in China regarding the interaction between IPRs and antitrust law at first, then introduces in detail the recent judicial precedents reviewed by the Supreme People's Court, to highlight those fiercely disputed issues, the court findings, and various views thereon, with the hope to shed some light on the understanding of this topic.

WHAT'S NEXT?

For April 2023, we will feature an Antitrust Chronicle focused on issues related to (1) **Junk Fees** ; and (2) **Essential Facilities**.

ANNOUNCEMENTS

CPI wants to hear from our subscribers. In 2022, we will be reaching out to members of our community for your feedback and ideas. Let us know what you want (or don't want) to see, at: antitrustchronicle@competitionpolicyinternational.com.

CPI ANTITRUST CHRONICLES May 2023

For May 2022, we will feature an Antitrust Chronicle focused on issues related to (1) **Healthcare**; and (2) **Foreign Subsidies**.

Contributions to the Antitrust Chronicle are about 2,500 – 4,000 words long. They should be lightly cited and not be written as long law-review articles with many in-depth footnotes. As with all CPI publications, articles for the CPI Antitrust Chronicle should be written clearly and with the reader always in mind.

Interested authors should send their contributions to Sam Sadden (ssadden@competitionpolicyinternational.com) with the subject line "Antitrust Chronicle," a short bio and picture(s) of the author(s).

The CPI Editorial Team will evaluate all submissions and will publish the best papers. Authors can submit papers on any topic related to competition and regulation, however, priority will be given to articles addressing the abovementioned topics. Co-authors are always welcome.

CPI TALKS...

. . . with Qing Li

In this edition of CPI Talks we have the pleasure of speaking with Qing Li,Vice President of the China Society of Economic Reform and former Deputy Director General at China's SAMR and NDRC.

Thank you, Ms. Li, for taking this time to talk to CPI.

1. China amended its Anti-Monopoly Law in 2022, in your opinion, what are the important changes?

Since the implementation of the Anti-Monopoly Law in 2008, one of the most important laws in the market economy system, China's anti-monopoly enforcement and justice has been demonstrating its power and important role in economic governance with a relatively rapid development trend. The three anti-monopoly enforcement agencies merged in 2018, and the first amendment was made in 2022. According to the Decision of the Standing Committee of the National People's Congress of China on Amending the Anti-Monopoly Law of the People's Republic of China, this amendment involved 22 additions to the provisions, 14 amendments to the provisions, and several other provisions were repositioned accordingly.

In summary, there are five major changes: First, to clarify the fundamental status of competition policy and to establish a sound, fair competition review system. Second, to entitle the anti-monopoly enforcement agencies more functions, such as the interview system, the written reporting system, etc., and the corresponding increase in the obligations of the investigated entities and individuals to cooperate. Third, to increase the extent of administrative penalties, including a substantial increase in the upper limit of fines, the new fineable circumstances, the new provisions for individuals, etc.; Fourth, to increase the provisions for the platform economy sector. Finally, to improve the anti-monopoly rules, such as the safe harbor system, the "stop the clock" system for the review period of the concentration of operators, and the specific circumstances of abuse of administrative power to exclude and restrict competition. In these amendments, there is no doubt that the clarification of the fundamental status of competition policy is the greatest highlight of this amendment. The most important feature of this amendment is the trend of strengthening regulation, with higher expectation on the role of anti-monopoly law in the future. This amendment will play a significant role in strengthening the law enforcement of China's antitrust law.

Aside from the above-mentioned modifications, another aspect should also be concerned. Since the Anti-monopoly Law has been implemented in China for just over 10 years, some issues have undergone a lot of discussion during the revision process and a consensus has not yet been formed among various parties, which has not been resolved in this revision and is estimated to require several more years of judicial practice in enforcement to be gradually improved.

For example, competition damage resulting in welfare losses or illegal income had not become the main basis for determining the fine, but 1-10 percent of the operator of the previous year's sales, in addition to two to five times for particularly serious violations. Obviously, it emphasized the characteristics of enhanced supervision and increased deterrence, which also means that more accurate assessments of competition damages or the calculation of illegal income through economic analysis has not been given sufficient weight in determining fines.

A related problem is that, in the case of administrative penalties that reflect more deterrent features, the corresponding procedures are not sufficiently well designed to balance deterrence with the necessary rights of enterprises to defend themselves, and thus to guarantee a more accurate understanding and implementation of the antitrust law. Of course, procedural issues may be addressed in administrative regulations or departmental rules. For example, the existing provisions on the abuse of a dominant market position do not have a clear and complete theory

of harm, nor do they have abstract provisions based on specific abusive behavior, which is yet to be further studied and improved in terms of jurisprudence.

2. You are a key driver of China's fair competition review system, established from 2016 until 2022 when it is incorporated into the Anti-Monopoly Law, how do you see the development of this system in China?

The core element of China's fair competition review system is that policy-making organizations (administrative organizations) conduct self-review against set standards in the process of policy measure formulation to prevent policy measures from excluding and restricting competition.

This system has a special role for China to solve the problem of administrative power to exclude and restrict competition. China is an economic system that is gradually transforming from a highly centralized planned economy to a socialist market economy. Under a highly centralized planned economy, the role of administrative power in determining economic activities has a natural legitimacy, and administrative power determines all levels and aspects of economic operations from macro to micro. In the process of transition from a planned economy to a market economy, the relationship between the government and the market is gradually adjusted, and the decisive role of administrative power on economic activities begins to differentiate, part of it still has legitimacy, and part of it does not adapt to the relationship between the government and the market is regarded as "undue interference" in market competition.

Of course, this differentiation process is gradually evolving, which means that the correction of "undue interference" requires a longer period of time; at the same time, it also means that "undue interference" is of a certain scale, and cannot only rely on the ex post correction by the anti-monopoly enforcement agencies. It also means that "undue interference" is of a certain scale and cannot be corrected ex post by anti-monopoly enforcement agencies, and that self-adjustment by policy-making organs beforehand becomes necessary. This is where the need for a fair competition review system in China lies.

The relationship between the government and the market will change and adjust with the continuous improvement of the socialist market economy system. The more perfect the market economy system is, the more fair competition is needed, and the higher the demand for administrative power in competition is, and it is necessary to keep a clear understanding of this.

Therefore, the incorporation of the fair competition review system into the Anti-Monopoly Law in 2022 reflects a higher level of consensus, although there is still a need for further mutual adaptation of this system and the Anti-Monopoly Law in practice. We have reasons to believe that with the continuous improvement of China's socialist market economy system and the deepening of market-oriented reforms, and with the further understanding and respect of the concept of fair competition by policy-making authorities, the fair competition review system will play a broader role in preventing the exclusion of competition by administrative power, thus enhancing the quality of China's economic policies as a whole.

3. As a former senior enforcement official with a background in economics, can you briefly describe the application of economic analysis to antitrust practice in China?

In my opinion, the core value of economic analysis in antitrust practice is to judge and seek the competitive order, market structure, and business model that maximizes the overall welfare of the society from the perspective of efficiency, to present the objective facts for the relevant parties in the whole process of antitrust law implementation, and to provide a reference for judging the legality of business behavior on this basis. Therefore, economic analysis has a wide range of applications in antitrust practice, such as identifying relevant markets, market dominance, analyzing market structure and concentration, assessing the effect of promoting or restricting competition, calculating competition damages or illegal income, etc. Over the past 10 years since the implementation of China's anti-monopoly law, economic analysis has played a very important role in several administrative enforcement and judicial cases. In the merger review of ZF/Wabco by SAMR, Vertical Arithmetic was employed to examine the Parties' incentive of input foreclosure. In the antitrust litigation of Rainbow v. Johnson & Johnson by Shanghai Higher People's Court, economic analysis was conducted to assess the anti-competitive effect of J&J's resale price maintenance ("RPM") agreement.

Since the implementation of China's antitrust law is only more than ten years old, the application of economics analysis in antitrust practice can only be said to be in its infancy. Compared with the level of economics analysis and the role played by analysis in the implementation of antitrust laws in Europe and the United States, there is still much room for development. First, with the revision of the antitrust law and the increase in the strength of antitrust enforcement agencies, the number of cases of antitrust administrative enforcement in China will increase significantly, as well as the number of civil antitrust lawsuits, putting forward a greater demand for economic analysis. Second, some

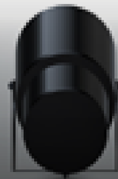
complex cases, especially antitrust cases involving data and algorithms, technology, platform rules, and intellectual property rights, will require a higher level of economic analysis. In this regard, China's economic analysis can learn from international experience, improve its own level and quality, gain greater development, and have room to make "China" contributions. Third, economic analysis can provide more professional support for anti-monopoly enforcement agencies. For example, the assessment of the competition landscape after the rectification of monopoly behavior. This includes both the restoration of competition in the relevant market and the adjustment of the business model of the enterprise after the monopoly violation of the enterprise is corrected, and the adjustment of the relevant policies, the condition of the industry, the restoration of competition in the relevant market, etc. after the abuse of administrative power to exclude and restrict competition is corrected. My personal observation is that if economic analysis can play a greater role in these points, it will certainly help the antitrust law to play a stronger and broader role in market regulation.

4. Can you give us an outlook on the development of competition policy in China in the next five to ten years?

In 2022, the Antimonopoly Law was amended to explicitly "strengthen the fundamental status of competition policy." If measured by the criteria of priority of value, universal application and independent authority, the basic status of competition policy has not yet been established in China. From a historical perspective, the construction and development of China's socialist market economy system should be used as the background for the observation of competition policy in China. Taking industrial policy as an example, China introduced the concept of industrial policy in 1986, while the first appearance of competition policy was in the Anti-Monopoly Law enacted in 2007, and the proposal that competition policy has a fundamental status was made in 2015, more than 20 years and nearly 30 years later, respectively. This time difference aptly reflects the stage of development of China's socialist market economy. It took decades of reform and opening up to reach the consensus that competition policy has a fundamental status, but it does take longer to truly realize the fundamental status of competition policy. The next five to ten years will be a critical period for China to "accelerate the construction of a new development pattern, focus on promoting high-quality development" and "build a high-level socialist market economy system" as proposed by the 20th Party Congress, which is also a critical period for competition policy to establish its fundamental status and position.

I personally hold positive expectations for the development of China's competition policy in the next five to ten years, although it may face many challenges and difficulties. First, the additional anti-monopoly enforcement agencies will have more enforcement resources to correct the abuse of administrative power to exclude and restrict competition; second, the policy-making authorities can achieve better self-regulation under the constraints of the fair competition review system; third, competition policy and other economic policies, especially industrial policies, will gradually form a suitable interaction to achieve the goals of industrial policies while reducing the damage to competition; fourth, the development of competition policy will promote China's market-oriented reforms, especially the reform of market allocation of factors and the construction of a unified national market, in which competitors are required to play their unique role. Among them, the fourth aspect is the most important contribution of competition policy to China's economic development.

HIGHLIGHTS AND ISSUES CONCERNING THE AMENDMENT OF CHINA'S ANTIMONOPOLY LAW



BY XIAOYE WANG[1]

1 Distinguished Professor at Shenzhen University and Law Professor at the Chinese Academy of Social Sciences.

I. INTRODUCTION

On June 24, 2022, the 35th meeting of the Standing Committee of the 13th National People's Congress adopted the Draft Anti-Monopoly Law (Amendment), which came into effect in August 2022. The new Anti-Monopoly Law has 70 articles in 8 chapters, with 13 new articles added and 23 articles modified from the past. Parts I to IV of this paper review the highlights of this amendment, Part V discusses several important issues that should have been considered during the amendment, and the conclusion comes at the end of this paper.

II. STRENGTHEN THE BASIC POSITION OF COMPETITION POLICY

The biggest highlight of the amendment of the Antimonopoly Law is the addition of the expression "the State shall strengthen the basic position of competition policy" in Article 4. This indicates that the basic way of allocating resources and regulating supply and demand in other economic fields is the market-based competition mechanism, except for the industries in which the state-owned economy is in control and which are related to the lifeline of the national economy and national security, as well as the industries franchised and monopolized according to the law, as stated in Article 8.

Another important aspect of strengthening the basic position of competition policy is the introduction of a fair competition review system. Article 5 provides that "the State shall establish and improve a fair competition review system. Administrative organs and organizations authorized by laws and regulations with the function of managing public affairs shall conduct a fair competition review when formulating regulations involving economic activities of market players." The 2016 Opinions of the State Council on Establishing a Fair Competition Review System in the Construction of the Market System states, "In order to regulate relevant government behavior, prevent the introduction of policies and measures that exclude or restrict competition, and gradually clean up and abolish regulations and practices that hinder the national unified market and fair competition, China needs to establish a fair competition review system in the construction of the market system."

Five ministries and commissions, including the General Administration of Market Regulation, the National Development and Reform Commission, and the Ministry of Finance, also jointly issued the "Rules for the Implementation of the Fair Competition Review System" in June 2021, which proposed 18 criteria for fair competition review in four areas, including market access and exit, free flow of goods and factors, impacts on production and business costs, and impacts on production and business practices. According to these criteria, unless for considerations of national economic security, overall economic interests and social public interests, enterprises operating in the market, whether state-owned or private, and whether Chinese or foreign, should be able to compete fairly in the market and receive equal legal protection. Like the prohibition of administrative monopoly in the Antimonopoly Law, the fair competition review also restrains the government's behavior. The difference between the two is that the fair competition review is a prior prevention of administrative monopoly behavior, i.e., the government's abuse of administrative power to exclude or restrict competition is nipped in the bud. With the entry of fair competition review into the Antimonopoly Law as a legal procedure that must be carried out by government agencies to introduce rules and regulations involving the business activities of market players, this further puts government behavior into the cage of the system and helps to solve the problem of unreasonable and excessive government intervention in the market.

As the anti-monopoly law strengthens the basic status of competition policy, it is necessary to briefly discuss the purpose of anti-monopoly legislation here. Article 1 only proposes to protect fair competition without mentioning the protection of free competition, which is incomplete. The anti-monopoly law prohibits monopoly agreements, over-sized M&A, and abusive behaviors by dominant market players to safeguard the competitive market, and it also prohibits the abuse of administrative power to restrict competition. Although these provisions are intended to uphold fair competition, their main value is to safeguard economic democracy and protect the free rights of enterprises to participate in market competition.

Therefore, as the purpose of anti-monopoly legislation, Article 1 should emphasize more on maintaining free competition in the market. Article 1 of the revised Antimonopoly Law also adds "encourage innovation." Some people think this is a significant development of the Antimonopoly Law, but I think this is a problem in theory. Since the top idea of the Anti-monopoly Law is to oppose monopolies and protect competition, and if "encouraging innovation" is juxtaposed as the purpose of anti-monopoly legislation, the question of which purpose should take priority in some cases inevitable. On the other hand, "encouraging innovation" becomes the purpose of antitrust legislation, which requires the state to take relevant measures to enhance the innovation of enterprises. For example, in order to support innovation, the government may adopt industrial policies, especially fiscal subsidies, and the bulk of which usually go to state-owned enterprises. Since improving innovation and encouraging innovation are different issues, "encouraging innovation" and "protecting competition" should not be deemed as equal in the Anti-monopoly Law.

III. STRENGTHEN THE DIGITAL ECONOMY ANTI-MONOPOLY

Article 9 of the General Provisions of the revised Antimonopoly Law provides that "operators shall not take advantage of data and algorithms, technology, capital and platform rules to engage in monopolistic acts prohibited by this Law." Given that the general provisions relate to the purpose of the legislation, the scope of adjustment, the basic principles, and other elements that are of guiding significance to the entire law, this provision is an important guide for law enforcement authorities dealing with monopoly agreements, abuse of dominant market position and merger control involving the digital economy.

A. Prohibiting Algorithmic Complicity

While the Antimonopoly Law does not clarify the "algorithmic conspiracy," the Antimonopoly Committee of the State Council's "Antimonopoly Guidelines on the Platform Economy" does refer to the issue of price conspiracy through algorithms and Hub-and-Spoke collusions. For example, algorithmic conspiracy may occur when companies in the same industry use the same algorithm and set the prices of their products based on the output and demand of the industry. Manufacturers selling products through e-commerce platforms can use algorithms or technology to track retailers' prices for the purpose of unified resale price maintenance (RPM). As price conspiracy or resale price maintenance can raise prices to harm consumers, even if the algorithms or technical means used here are neutral, these actions should still be subject to antitrust laws.

B. Prohibition of Abuse of Dominant Market Position

In addition to General Article 9, Article 22(2) of the Anti-Monopoly Law provides that "an operator with a dominant market position shall not use data and algorithms, technology, and platform rules to engage in the abuse of a dominant market position specified in the preceding articles." Here, this includes unfair overpricing practices as well as unfair low-cost sales, refusal to deal, forced transactions, tied sales, and differential treatment committed by large platform companies. Abuses in the platform economy generally involve data transactions, especially data transactions with SMEs. For example, the administrative penalty decision issued by the General Administration of Market Regulation against Alibaba for "two-for-one" conduct in the e-commerce sector states that "since 2015, the party concerned has abused its dominant position in the market of e-tailing platform services in China to prohibit operators on the platform from opening stores or participating in promotional activities on other competing platforms, which has excluded and restricted competition in the market, ... constituting an abuse of dominant market position prohibited by the Anti-Monopoly Law."[2] This indicates that data transactions between large platform companies and third-party companies are allowed for data open on fair, reasonable and non-discriminatory terms.

C. Control of business Operator Concentration

Article 9 of the Anti-monopoly Law prohibits enterprises from engaging in monopolistic acts prohibited by the Anti-monopoly Law through "capital advantage," which includes the concentration of business operators with the effect of excluding or restricting competition. Article 26(2) also provides that "if the concentration of operators does not meet the declaration standards set by the State Council, but there is evidence that the concentration of operators has or may have the effect of excluding or restricting competition, the anti-monopoly enforcement agency of the State Council may require the operators to declare it." This indicates that the Anti-monopoly Law shall strengthen the control of operator concentration even if that does not meet the notification standard but may have effect of excluding or restricting competition, in order to avoid and reduce the situation where the market sales of the enterprises involved are not large, but the M&A transaction has a large impact on market competition. The Anti-Monopoly Guidelines for Platform Economy states that "law enforcement agencies should pay high attention to operator concentrations in the platform economy where one of the operators involved in the concentration is a start-up or an emerging platform, where the operator involved in the concentration has a low turnover due to the adoption of a free or low-price model, where the relevant market concentration is high, and where the number of competitors involved is small. For the operator does not meet the notification standards but has or may have the effect of excluding or restricting competition, the anti-monopoly enforcement agency of the State Council will investigate and deal with it according to law."

It is necessary to point out here that even though the Antimonopoly Law strengthens the regulation of M&A activities of Internet companies, it should not prohibit all M&A activities of Internet companies in a "one-size-fits-all" manner. In other words, economic analysis of M&A in the Internet sector should still be conducted, taking into account not only the impact of M&A on competition, but also the motives of M&A, and not only the motives of the acquirer, but also the motives of the acquired party, such as preventing bankruptcy or achieving complementary advantages. The voice of the China Central Leading Group on Financial and Economic Affairs in August 2021 was that "strengthening the regu-

2 Decision on Administrative Punishment by the State Administration for Market Regulation - State Administration of Municipal Supervision [2021] No. 28.

lation of large technology enterprises such as Internet platforms to prevent monopoly and disorderly expansion of capital is a worldwide problem for which all countries are exploring solutions. We insist on both regulation and development simultaneously and equivalently."[3]

IV. INTRODUCTION OF THE "SAFE HARBOR" RULE

Article 18(3) of the Anti-monopoly Law provides that "if an operator can prove that its market share in the relevant market is lower than the standard set by the anti-monopoly enforcement agency of the State Council and meets other conditions set by the anti-monopoly enforcement agency of the State Council, it shall not be prohibited." Because the market share is used as a criterion for exempting monopoly agreements here is clearly a reference to the "safe harbor" system of the EU competition law.

The De Minimis Notices published by the European Commission in 1970 established the 'safe harbor'. If it can be judged that the competitive damage of an anticompetitive agreement is not significant according to the market position of the parties to the agreement, the agreement may not be prohibited by Article 101 (1) TFEU. That is to say, 'safe harbor' is established for agreements between undertakings whose market shares fall below certain threshold.[4] In accordance with the current *De Minimis Notice*, an agreement falls under 'safe harbor' if (1) the aggregated market shares of competitors are no more than 10 per cent; (2) the market shares of neither non-competitive parties (be them are from upstream and downstream markets; or from adjacent markets) are more than 15 per cent.[5]

Another important aspect of the "safe harbor" rule of EU competition law is that it emphasizes that agreements within the "safe harbor" must not substantially restrict competition, and therefore the *De Minimis* Notice specifies that the "safe harbor" rule shall not apply to agreements whose object is to prevent, restrict or distort competition in the internal market[6], in particular not to "hard-core cartels" and "hard-core restrictions" introduced by the European Commission in its series of block exemption regulations.[7] For example, the European Commission's Guidelines on Vertical Restraints explicitly state that "agreements fixing resale prices or limiting minimum resale prices, directly or indirectly, alone or in combination with other factors, are 'hardcore restraints' and cannot be subject to the Block Exemption Regulation because they not only violate Article 101(1) of the Treaty, but also make it difficult to meet the conditions for exemption under Article 101(3)."[8] These prerequisites suggest that the "safe harbor" of EU competition law is a rule that satisfies certain conditions and thereby precludes them from being competitively harmful or can be found lawful without assessing specific market circumstances.

The "safe harbor" of China's Anti-monopoly Law is placed in Article 18, which deals with vertical agreements. Paragraph 1 of this article prohibits an operator and its counterparty from entering into (1) a fixed price for reselling goods to a third party; (2) a limited minimum price for reselling goods to a third party; or (3) other monopoly agreements as determined by the anti-monopoly enforcement agency of the State Council. For the preceding paragraph (1) and (2), Paragraph 2 states that if the operator can prove that it does not have the effect of excluding or restricting competition, it is not prohibited. Paragraph 3 introduces the "safe harbor" rule mentioned above. The introduction of the "safe harbor" in the Antimonopoly Law is intended to improve enforcement transparency and save enforcement resources. However, the "safe harbor" rule introduced by the Antimonopoly Law has not been very successful because of the following problems.

The first problem is that the agreement in the "safe harbor" is not safe. Obviously, the "safe harbor" rule should be based on the enforcement experience, i.e. a "safe harbor" can be established if one is confident that a certain range of conduct is unlikely to produce serious competitive harm. However, if a agreement in "safe harbor" may still be found to be illegal, the "safe harbor" is not sufficiently transparent and cannot effectively help businesses avoid the risks of violating anti-monopoly law. According to Article 18(3) of the Antimonopoly Law, in addition to the market share standard, the "safe harbor" rule must "meet other conditions set by the antimonopoly enforcement agency of the State Council." Article 18(2) also provides that the business operator "shall be able to prove that it does not have the effect of excluding competition," and this "safe harbor" rule is unlikely to greatly improve the efficiency of antitrust enforcement because the agreement in "safe harbor" is not safe.

3 China Central Finance Office, 'Common Prosperity is Not "killing the Rich to Help the Poor, Rectifying the Internet Platform is Definitely not Targeting Private Enterprises' (*sohu*, 26 August 2021) <https://www.sohu.com/a/485866356_313745> accessed 26 January 2023

4 European Commission Notice on agreements of minor importance which do not appreciably restrict competition under Article 101(1) of the Treaty on the Functioning of the European Union (De Minimis Notice) (2014/OJ C 291/01).

5 ibid, §§ 8, 9.

6 See § 2, De Minimis Notice (2014/OJ C 291.

7 See § 13, De Minimis Notice, 2014/OJ C 291.

8 COMMISSION Guidelines on Vertical Restraints, Section 2.10.

The second issue is the placement of the "safe harbor" rule in Article 18, which deals with vertical agreements, which suggests that it does not apply to horizontal agreements between competitors. Although horizontal agreements may restrict competition to a greater extent than vertical agreements, it cannot be said that there is no "safe harbor" for cooperation between competitors. In fact, according to Article 20 of the Antimonopoly Law many kind of horizontal agreements may be exempted provided that "the business operator shall prove that the agreement reached does not substantially restrict competition in the relevant market and enables consumers to share in the benefits arising therefrom." In order to improve the efficiency of enforcement and the predictability of the parties, the Antimonopoly Law should, for the long run, also establish a "safe harbor" system for certain agreements between competitors, such as specialization agreements and R&D agreements as proposed in Article 20.

The third issue is the application of the "safe harbor" for RPM in China's Antimonopoly Law. There are two different philosophies of RPM for administrative enforcement and justice in China: administrative enforcement generally considers them illegal, while courts generally consider them legal based on “rule of reason”.[9] I advocate that RPM is illegal in principle, but the parties have the right to defend themselves. RPM, in principle, should be prohibited in China because, on the one hand, RPM seriously damages price competition among sellers and objectively raises prices to hurt the interest of consumers as a result; on the other hand, because China enacted the Anti-Monopoly Law relatively late, the business community generally lacks anti-monopoly awareness and competition culture, RPM is common among manufacturing enterprises. For example, the infant milk powder case handled by the NDRC in 2013 involved almost all brands in the industry.[10] The two cases of Gree and Haier air conditioners in 2016 show that the highly concentrated industry also has a serious RPM problem, i.e. almost every household air conditioner in the market contains a high retail fee.[11] The 2019 Beijing Market Supervision Bureau's investigation suspension on Lenovo indicates the largest producer in the Chinese PC market has long used the RPM model for its various products, including spare parts sales and repair services,[12] which can tell the severity of RPM in the Chinese market. Therefore, the "safe harbor" rule according to the AML should not be applied to RPM because it can very often seriously harm market competition in China.

V. INCREASE PENALTIES FOR VIOLATIONS

The Antimonopoly Law increases the penalties for violations, as shown in the following areas:

A. Increase the Penalty for Illegal Operator Concentration

Before the amendment, the Antimonopoly Law provided that an operator concentration implemented in violation of the law may be subject to a fine of up to RMB 500,000 in addition to stopping the implementation of the concentration and taking necessary measures to restore it to its pre-concentration state. In view of the fact that the operator concentration that should have been notified cannot be restored to the pre-concentration state by splitting, an administrative fine of 500,000 yuan for the illegally implemented concentration is insignificant and not a deterrent to large enterprises, Article 58 of the amended Anti-Monopoly Law provides that "an operator who implements a concentration in violation of the provisions of this Law... shall be fined up to ten percent of the previous year's sales; if it does not have the effect of excluding or restricting competition, a fine of not more than 5 million yuan shall be imposed.”

B. Introduce Personal Responsibility

Article 56, which deals with monopoly agreements, provides that "the legal representative, the principal person in charge and the person directly responsible for the operator who is personally liable for entering into a monopoly agreement may be fined up to one million yuan." The personal liability here should be for the hard-core cartel which is illegal. Since the direct purpose of the hard-core cartel is to exclude and restrict competition, it is reasonable to impose personal liability on the leaders or senior employees of the enterprise responsible for organizing or participating in the hard-core cartel, considering that the imposition of personal liability can further increase the deterrent effect on illegal conduct.

9 See "A Critique of the Application of the "Rule of Reason" to the Resale Price Maintenance according to China's AML," Legal and Commercial Research, Vol. 1, No. 2021, p. 43 by Wang Xiaoye.

10 See "Dometic Wyeth and other milk powder under antitrust investigation," http://finance.sina.com.cn/focus/nfqyztc/, 2020-5-1.

11 See "A Critique of the Application of the "Reasonable Principle" to the Antitrust Regulation of Resale Price Maintenance," Legal and Commercial Research, Vol. 1, No. 2021, p. 43, written by Wang Xiaoye.

12 See "Antitrust Investigation Discontinued Due to Lenovo's Aggressive Cooperation? , https://finance.sina.com.cn/stock/relnews/hk/2019-11-19/doc-iihnzhfz0353432.shtml, 2020-5-1.

C. Add a Special Deterrent Clause

Article 63 of the Antimonopoly Law provides that " For violations of the provisions of this Law with particularly serious circumstances, bad impacts and serious consequences, the State Council anti-monopoly enforcement agencies can determine the specific fines between two times and five times of the prescribed amountat least two times or five times the number specified in ...... this Law. " Considering the stability and predictability of the law and the lack of transparency of the determination of " particularly serious circumstances, bad impacts and serious consequences " in practice due to the discretion of law enforcement agencies, I suggest that law enforcement agencies should make detailed explanations or adopt guiding cases to explain. For example, the EU Fines Guidelines provide that "if the European Commission or a member state competition enforcement agency determines that an enterprise has violated Article 101 or 102 of The Treaty of Operations of the European Union, it may increase the base fine for the determined violation by 100% if the enterprise is found to have continued or repeated the same or similar violations. "[13]

D. Increase Criminal Liability

Article 67 of the Antimonopoly Law provides that "if a crime is committed, criminal liability shall be investigated in accordance with law." The introduction of criminal liability helps to increase the deterrent effect of the Law, but here criminal investigations, prosecutions and criminal imprisonment of corporate executives entail costs. Given the great uncertainty of antimonopoly cases, cases imposing criminal liability should be limited to hardcore cartels that are illegal.

E. The Entire Sales of the Offending Enterprise as the Basis for Administrative Fines

The Antimonopoly Law provides that the offending enterprise may be fined "one to ten percent of the previous year's sales ," but how to calculate the "sales" is not clearly defined. The Antimonopoly Bureau of the State Administration for Market Regulation has made the following statement on "sales": "After consulting with the Legal Affairs Commission of the National People's Congress, in principle, in the enforcement of monopoly cases, all sales of the operator are used as the basis for calculating the fine."[14] For Alibaba's e-commerce platform "either or choice " behavior, the State Administration for Market Regulation 2021 imposed a fine of 4 percent of its 2019 sales within China of RMB 455.712 billion, totaling RMB 18.228 billion.[15] The Supreme People's Court also recently endorsed the Hainan Administration for Market Regulation's 2020 administrative fine against Shenghua, which was based on Shenghua's entire 2018 sales, but only less than 1 percent of all sales involved in the violation.[16]

The purpose of using the entire market sales of the offending enterprise as the base for fines is to increase antimonopoly deterrence. However, even if the deterrent effect is increased, there should be a reasonable range of fines for illegal acts. In antimonopoly cases, this should refer to the relevant markets, including the relevant commodity markets and the relevant geographical markets.[17] If, instead of considering which products or which services are in violation of the law, sales are calculated according to the entire business of the enterprise, this may result in fines for legitimate business activities. Such a penalty is not only unreasonable but also unlawful, because even if the enforcement authorities question the existence of other business activities of the enterprise, they have to be regarded as lawful before they can make a penalty decision based on evidence, while lawful business activities should not be subject to administrative penalties. The antimonopoly enforcement authorities should seriously consider this issue, which not only involves the significant interests of enterprises, but also concerns the scientific and rational nature of anti-monopoly enforcement.

VI. REMAINING ISSUES FOR THE AMENDMENT

In my opinion, the amendment of the Antimonopoly Law should not only add provisions that are urgently needed in law enforcement but also delete provisions that are impossible to apply.

13 Guidelines on the Method of Setting Fines Imposed Pursuant to Article 23(2) (a) of Regulation No 1/2003, O.J. [2006] C 210/2, para 28.

14 By the Anti-Monopoly Bureau of the State Administration for Market Regulation, China Anti-Monopoly Legislation and Enforcement Practice, China Industry and Commerce Press, 1st edition, June 2020, p. 349.

15 Decision on Administrative Punishment by the State Administration for Market Regulation - State Administration of Municipal Supervision [2021] No. 28.

16 Administrative Judgment of the Supreme People's Court, (2021) Supreme Intellectual Property Final No. 880.

17 See Article 15 of the China's AML.

A. Export Cartel Exemption

Article 20(6) of the Antimonopoly Law provides that the prohibition of monopoly agreements may not be applied "in order to safeguard legitimate interests in foreign trade and foreign economic cooperation." However, considering that antimonopoly laws around the world have the same effect of extraterritorial application as China's Antitrust Law,[18] the exemption of export cartels from the Antimonopoly Law would not be of substantial help to Chinese exporters because they could be considered as violating foreign anti-monopoly laws in the country of export even if they do not violate the Chinese Antimonopoly Law. For example, in 2005, four Chinese pharmaceutical companies exporting vitamins were subject to antitrust litigation in the United States. Therefore, the Antimonopoly Law should repeal this provision.

B. Exemption From the Exercise of Intellectual Property Rights

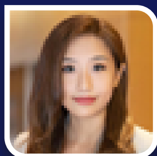
Article 68 of the Antimonopoly Law provides that "the exercise of intellectual property rights by an operator in accordance with the laws and administrative regulations relating to intellectual property rights shall not be subject to this Law." This provision is, on the one hand, in conflict with legal practice, as cases in which the exercise of intellectual property rights has been found to be in violation of the antitrust law are common at home and abroad. On the other hand, this provision is also inconsistent with the basic antitrust principles governing the exercise of intellectual property rights in countries around the world. For example, the Guidelines on Technology Transfer Agreements issued by the European Commission clearly states two basic principles of the relationship between intellectual property law and competition law: first, exclusive rights to intellectual property rights do not mean that intellectual property rights can be exempted from competition law; and second, there is no inherent conflict between intellectual property law and EU competition law, because their purposes are both to promote consumer welfare and efficient allocation of resources.[19] With today's highly developed information technology, various standards, both de jure and de facto, can easily lead to the dominance of rights holders in certain technology markets. While the state should protect IPRs on the one hand, it should also prevent monopolistic rent-seeking activities of rights holders, and therefore IPR protection cannot exclude the application of competition law.

18 See Article 2 of the China's AML.

19 EU Guidelines on the application of Article 101 of the Treaty on the Functioning of the European Union to technology transfer agreements, 2014/OJ C 8, para. 7.

IN PRAISE OF SAMR's BEHAVIORAL REMEDIES: PREVENTING OVER-DETERRENCE IN GLOBAL MERGER CONTROL

BY ANDREW FOSTER & CINDY LAU[1]



1 By Andrew Foster, partner at Skadden, Arps, and Cindy Lau, associate at Skadden Arps.

In recent years, agencies and regulators responsible for merger control in the U.S., UK, and other jurisdictions (including Australia and Germany) have taken an increasingly hardline stance opposing the implementation of behavioral remedies to rectify competition concerns, even in cases without obvious anticompetitive red flags. While classic ideological considerations support the use of behavioral remedies in transactions with vertical or neighboring relationships, the U.S. and UK have gone further in their recent practice, effectively precluding the use of behavioral remedies in most cases. By contrast, China's State Administration for Market Regulation ("SAMR") has been willing to use behavioral remedies as a solution for concerns under the Anti-Monopoly Law ("AML"), and has indeed allowed conduct commitments in the majority of its conditional clearances over the past fifteen years, while the European Commission continues to consider behavioral remedies as potentially useful in some vertical and conglomerate assessments.

A failure to acknowledge the potential benefits offered by behavioral remedies brings a serious risk of over-enforcement, potentially leading to a chilling effect on even pro-competitive mergers and acquisitions as a whole. Indeed, it has been recognized that behavioral remedies could at times generate greater efficiencies than structural commitments. A governmental aversion to behavioral remedies can lead to prohibitions of efficiency-creating mergers with only limited potential competitive issues – an arbitrary result at best, and intentionally chilling at worst.[2] This happens where complex, headline-grabbing M&A transactions in dynamic and innovative industries such as digital platforms or semiconductors encounter agencies and regulators willing to speculate on novel and untested theories of competitive harm. Many of those same agencies and regulators will then refuse to engage on solutions for such speculative theories, instead flatly rejecting an approach to craft tailored remedies, absent a problematic horizontal overlap with a clear structural fix. The nearly fifteen years' of experience of SAMR and its predecessor[3] in implementing and enforcing behavioral remedies, however, belies many of the most common complaints about behavioral remedies – for example, that they are difficult to implement or monitor, or ineffective at remedying vertical or conglomerate concerns in dynamic markets.

SAMR's continued willingness and flexibility to accept behavioral remedies is to some degree driven by its unique mandate under the AML to consider not only competition concerns but also the impact of a transaction on China's national economy.[4] This means that SAMR has long experience considering a deal's effects outside the traditional "consumer welfare" standard previously embraced by most competition practitioners. Now, as many agencies and regulators move away from that traditionally accepted standard to consider the impact of a transaction more holistically, SAMR's experience has become all the more important. SAMR's preference to avoid prohibitions in favor of tailored solutions achieves a balance between protecting market competition and incentivizing (or at least not deterring) legitimate M&A activities. This is all the more important when the impact of over-enforcement in merger control leads inevitably to the death of a proposed transaction, while the dangers of under-enforcement can subsequently be remedied by a vigilant enforcer using its dominance or monopolization toolbox. Seen in this light, although China has a well-earned reputation for being one of the most difficult jurisdictions with respect to regulatory approvals for complex M&A, its use of behavioral remedies balances its ability to conduct a holistic review and entertain multiple theories of harm while avoiding the unjustified and overly broad deterrent of flat prohibitions for largely pro-competitive transactions.

I. STRUCTURAL REMEDIES PREFERRED OVER BEHAVIORAL REMEDIES IN U.S. AND UK

Structural remedies seek to directly influence the competitive structure of the relevant market(s) in order to maintain or improve the conditions for competition.[5] The classic structural remedy is a divestiture of a business. Behavioral remedies seek to address the identified competition concerns through commitments by the undertakings concerned to behave or not to behave in a certain manner. Examples include supply obligations, licensing key technology, providing access to key infrastructure, firewall provisions, and refraining from raising prices above a certain level. The classic approach to remedies attached to conditional clearances of merger transactions identifies structural remedies as superior to behavioral remedies. Structural remedies directly and permanently resolve competitive issues, ensuring lasting conditions preserving dynamic competition.[6] Behavioral remedies have traditionally been considered less effective in addressing competitive harm and less desirable where they result from activist governmental intervention that nevertheless fails ultimately to address the underlying structural flaws in the market itself. Behavioral remedies are also said to be more burdensome, as they require monitoring post-transaction, and to be more difficult to implement. In the U.S. and UK, the agencies and regulators have cited these reasons for refusing to accept behavioral remedies, and overall there has been a lower proportion of cases that end up with behavioral remedies as conditions to clearances, compared to China.

2 Ezrachi, *Under (and Over) Prescribing of Behavioral Remedies*, The University of Oxford Centre for Competition Law and Policy Working Paper (L) 13/05.

3 SAMR was officially established in 2018. From 2008 until 2018, the Anti-Monopoly Bureau of the Ministry of Commerce ("MOFCOM") administered merger control reviews under the AML. For the purposes of this article, references to SAMR should be taken to include its predecessor at MOFCOM where time appropriate.

4 Art. 33(5) AML.

5 Maier-Rigaud and Loertscher, *Structural vs. Behavioral Remedies,* CPI Antitrust Chronicle (April 2020).

6 See Ezrachi, *supra* note 2.

In the U.S., there is a strong preference for structural remedies, such as divestitures, over behavioral remedies. Former U.S. Assistant Attorney General Makan Delrahim commented that, *"behavioral remedies often fail to let the competitive process play out, [requiring] centralized decisions instead of free market process"*.[7] Moreover, in the U.S., conduct remedies are seen as ineffectual in addressing competitive harm, because of perceived administrative difficulties of enforcing and monitoring compliance.[8] The U.S. Department of Justice ("DOJ")'s Merger Remedies Manual states that remedies should not create ongoing government regulation of the market, therefore stand-alone conduct relief is appropriate only when the parties prove that: (1) a transaction generates significant efficiencies that cannot be achieved without the merger; (2) a structural remedy is not possible; (3) the conduct remedy will completely cure the anticompetitive harm, and (4) the remedy can be enforced effectively.

Similarly, the UK Competition and Markets Authority ("CMA") prefers structural remedies to behavioral remedies, because behavioral remedies are unlikely to be as comprehensive or lasting as a structural fix in resolving a substantial lessening of competition and its adverse effects.[9] In its 2019 Merger Remedy Evaluations, the CMA expressed its belief in the superiority of structural remedies, in terms of their effectiveness, risk profile and durability, but still acknowledged some limited circumstances in which behavioral remedies might be effective (for example, where a merger takes place in a technologically mature sector with an established and well-resourced regulatory regime and where there is clear evidence that the remedies will only be required for a limited period).[10]

In recent years, however, the CMA's stance on behavioral remedies has hardened significantly, consistent with its highly interventionist approach to merger control in general. As reported in 2020, the CMA was *"the most active antitrust enforcer"* and it frustrated the highest share of deals worldwide.[11] Indeed, in 2021, the CMA issued a joint statement with the Australian Competition and Consumer Commission ("ACCC") and Germany's Bundeskartellamt, ("FCO")[12] highlighting the importance of rigorous and effective merger enforcement and discrediting *any* potential pro-competitive effects of behavioral remedies:

> *It is widely acknowledged that complex behavioral remedies that create continuing economic links and dependencies are unlikely to recreate the pre-merger competitive intensity of the market, can raise significant circumvention risks, and can quickly become outdated as market conditions change … Structural remedies – whether prohibition or divestment of a standalone business – are more likely to preserve competition and lead to an optimal solution for stakeholders and are therefore in the best interests of consumers. Importantly, the threshold of proof required to prohibit a merger is not higher when no divestment would be effective in restoring the lost competition; indeed, protecting competition and consumer welfare can sometimes only be achieved by blocking a merger outright.*[13]

Traditionally it has been accepted that some competitive harm may be better dealt with by a behavioral remedy than a structural one,[14] such as where a merger involves vertical elements and may limit access to infrastructure and result in foreclosure, or when a behavioral remedy of non-discriminatory open access may be sufficient to address the competitive harm while preserving the efficiencies associated with a transaction.[15] Additionally, the flexibility and reversibility of behavioral remedies make them superior tools for dealing with changing market realities, e.g. in technology markets, and addressing limited market effects, e.g. where the competitive harm is confined to one market, in which case imposing a global divestiture would amount to over-fixing. [16]

7 Keynote Address at American Bar Association's Antitrust Fall Forum, Washington D.C. (Nov. 16, 2017).

8 U.S. DOJ Antitrust Division, *Merger Remedies Manual* (Sep. 2020), p. 16.

9 CMA, *Merger Remedies* (Dec. 13, 2021), p. 6.

10 CMA, *Merger Remedy Evaluations – Report on Case Study Research* (Jun. 18, 2019), p. 3.

11 Javier Espinoza and others, *UK competition watchdog is most active antitrust enforcer* (Financial Times, Mar. 2, 2020).

12 Under German merger control rules, behavioral remedies are said to be "sometimes, in appropriate cases, also an effective measure … [i]n some cases, it may be sufficient to enable third companies to enter the market or to lower entry barriers to facilitate market entry." See p. 41 of FCO's Guidance on Remedies in Merger Control (May 2017). That said, behavioral commitments that require continued control of the merged entity's market conduct (e.g. Chinese walls) are not considered effective and are not accepted by the FCO in its remedies practice, which is somewhat unusual by international standards. See e.g. Wilson, *Merger remedies – is it time to go more behavioral?* (Kluwer Competition Law Blog, Feb. 21, 2020).

13 CMA, ACCC and Bundeskartellamt, *Joint statement on merger control enforcement* (Apr. 20, 2021) (emphasis added).

14 See Ezrachi, *supra* note 2.

15 See Ezrachi, *supra* note 2.

16 See Ezrachi, *supra* note 2.

While classic ideological considerations support behavioral remedies in certain types of vertical or conglomerate transactions, the CMA goes much further to preclude behavioral remedies in most cases, except for instance, in regulated infrastructure markets, where the CMA considers that behavioral remedies may be appropriate. The CMA has been clear that the bar to show that behavioral remedies can address competition concerns is high.[17] In a recent speech by the Chief Executive of the CMA, Sarah Cardell explained that behavioral remedies typically involve arrangements that the parties would not enter into under normal circumstances, and once the remedy expires, the underlying causes of the competition concerns may remain. Moreover, the CMA sees many practical challenges to designing an effective behavioral remedy.[18] As will be discussed below, the CMA's approach is in stark contrast to SAMR's policy of promoting economic development and consensus-based approach of balancing competing interests, which entails a consideration of the effects on M&A incentives.

II. A MORE MEASURED APPROACH FROM THE EUROPEAN COMMISSION

The European Commission ("EC") has notably continued to take a more measured stance with respect to behavioral remedies – while expressing some skepticism regarding their effectiveness, it is still willing to consider them in certain circumstances.[19] In recent years, there have been voices calling for a more open approach towards behavioral remedies in Europe,[20] and EC cases and speeches by EC officials have shown some receptiveness to these views.

Commissioner for Competition Margrethe Vestager said in July 2019 that she was open to behavioral remedies in digital mergers, noting that in digital markets the merging parties are not always straightforward competitors and the issue is not necessarily the removal of a competitor, but how markets interact and whether there are important input services such as access to technology.[21] An example is *Qualcomm/NXP* (2018),[22] which was cleared by the EC, subject to behavioral commitments. A key concern in that case centered around NXP's MIFARE, a technology for contactless payments in transport and other domains that was licensed by NXP to third parties. One of the competition concerns was the merged entity's incentives to license MIFARE, once it could offer its own bundles with baseband chipsets and secure elements. Among other commitments, the parties undertook to offer licenses to NXP's MIFARE technology and trademarks on terms that are at least as advantageous as those available then, and to ensure the interoperability of the merged entity's products with those of rivals.

More recently, the EC cleared *Google/Fitbit* (2020)[23] and *Meta/Kustomer* (2022)[24] imposing behavioral commitments in both cases. Google committed, for example, to not use users' health and wellness data collected from Fitbit devices in its Google Ads business, and also committed to store relevant Fitbit user data in a "data silo" separate from any other Google data used for advertising. Notably, the ACCC refused to accept similar behavioral undertakings, reasoning that long term behavioral undertaking of this type in such a complex and dynamic industry could not be effectively monitored and enforced in Australia, instead opting to open an investigation into the transaction.[25] The EC also cleared the acquisition by Meta (formerly Facebook) of customer relationship management software maker Kustomer, subject to a set of 10-year commitments that would guarantee access to the social network's publicly available application programming interfaces ("APIs").

17 See CMA, *Merger Remedy Evaluations, supra* note 9, p. 2 ("*The need to put addressing likely consumer harm from problematic mergers at the forefront of decisions about merger remedies – where the CMA accepts a risk that a remedy may not be fully effective in doing so, this risk is ultimately borne by consumers*").

18 CMA, *A speech delivered by Sarah Cardell, Chief Executive of the CMA to the UK Competition Law Conference 2023* (Feb. 27, 2023).

19 EC, *Commission Notice on remedies acceptable under Council Regulation (EC) No 139/2004 and under Commission Regulation (EC) No 802/2004*, p. 6.

20 See e.g. Wilson, *Merger remedies – is it time to go more behavioral?* (Kluwer Competition Law Blog, Feb. 21, 2020)

21 *Speech by Margrethe Vestager on dealing with mergers in a digital age* (Practical Law Competition, Jun. 19, 2019).

22 EC Case M.8306 - *Qualcomm/NXP Semiconductors* (Jan. 18, 2018).

23 EC Case M.9660 – *Google/Fitbit* (Dec. 17, 2020).

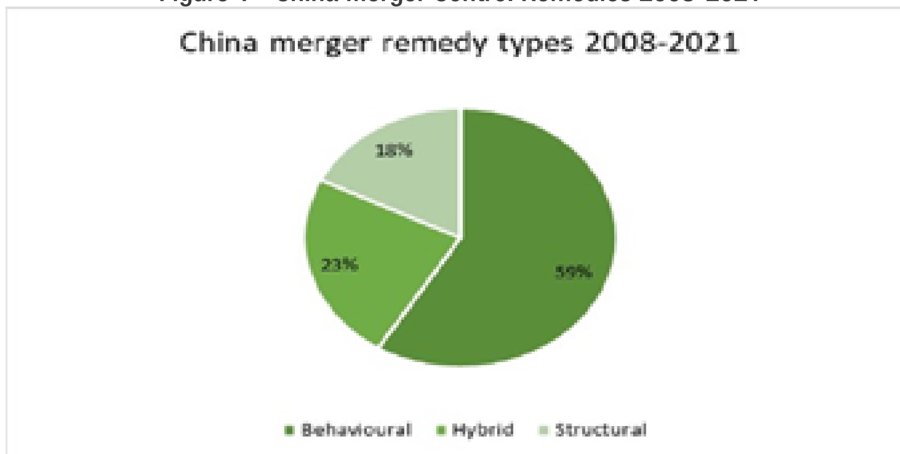
24 EC Case M. 10262 – *Meta (formerly Facebook)/Kustomer* (Jan. 27, 2022).

25 ACCC, *ACCC rejects Google behavioral undertakings for Fitbit acquisition* (Dec. 22, 2020).

III. CONTINUED WILLINGNESS AND FLEXIBILITY OF SAMR TO ACCEPT BEHAVIORAL REMEDIES

Compared to regulators in the U.S. and UK, SAMR has traditionally been more willing and flexible to accept behavioral remedies; classic structural remedies, such as divestitures, have also been less common in SAMR remedy cases than behavioral remedies.[26] In a 2021 survey of all SAMR remedy cases, it was found that those involving non-structural remedies represent a materially larger portion than the cases reviewed by the U.S. DOJ.[27] Around 82 percent of all conditional clearances from 2008 to 2021 involved behavioral remedies, and only 18 percent had purely structural remedies; as a comparison, the U.S. DOJ required divestitures in 95 percent of its conditional merger approvals from 2010 to 2021.[28]

Figure 1 - China Merger Control Remedies 2008-2021



Source: PaRR.[29]

Over time, SAMR has developed an effective, and innovative, toolbox of behavioral remedies to address concerns arising from Chinese stakeholders, particularly, customer concerns about input foreclosure and interoperability, and industrial policy concerns presented by industry associations. In cases involving strategically key industries (e.g. semiconductors, information and communications technology, healthcare, and agriculture) that receive heightened scrutiny in China, "creative" behavioral remedies can address China-specific concerns, whether or not competition-related, without irretrievably damaging the value of the underlying deal. Common behavioral remedies imposed in China include: continuous commitments to supply products on existing terms as to price, quality, quantity, *etc.*; fair, reasonable, and non-discriminatory ("FRAND") sales commitments, particularly to enable local players' access to input and IP; pricing commitments; prohibitions against bundling or the imposition of other unreasonable commercial terms; interoperability commitments for third-party products, seen particularly in semiconductor cases; firewall provisions to protect third-party competitively sensitive information; and commitments to continue to invest in R&D activities to address concerns of stifling innovation.

In 2021, SAMR imposed remedies in four cases, of which three used behavioral remedies *(Cisco/Acacia; ITW/MTS; SK hynix/Intel)* and one used structural remedies *(Danfoss/Eaton)*. In 2022, all five of the conditional approvals granted by SAMR involved behavioral remedies, although two involved hybrid remedies (that is, including both structural and behavioral remedies). Table 1 below summarizes recent conditional cases with behavioral remedies in China.

26 In the rare cases where structural remedies were imposed by SAMR, e.g. *Novelis/Aleris (2019), Danaher/GE Healthcare* (2020) and *Danfoss/Eaton* (2021), overseas competition regulators also imposed structural remedies.

27 Zhou, Peng and Eichlin, *Non-Structural Remedies* (GCR, Nov. 8, 2021).

28 Klein and Fan*, 71% of Chinese divestment remedies same as other regulators* (PaRR Analytics, Dec. 8, 2021).

29 *Ibid.*

Table 1 - Notable Transactions Reviewed by SAMR in China with Behavioral Remedies (2021-2022)

Case	Competition Concerns	Behavioral Remedies in China	Outcome in U.S., EU, and UK (if filed)
***Shanghai Airport / Eastern Air Logistics JV* (2022)**	· **Horizontal** overlap in airport cargo terminal services · **Vertical** relationship between airport cargo terminal services (upstream) and international and domestic air cargo services (downstream)	· Continuous execution of customer contracts on cargo terminal services at Pudong Airport and renewal of such contracts upon customer request (with a shorter duration of 5 years) · Provision of cargo terminal services at Pudong Airport on FRAND terms · Duration: 8 years; termination upon application and approval	N/A
***Korean Air / Asiana Airlines* (2022)**	· **Horizontal** overlap in scheduled air passenger transport services and air cargo transport services	· Commitment to return a certain number of flight slots and to return part of the traffic rights for specific routes, upon the request of new entrants · Commitment that the annual supply of specific routes shall remain at a certain level · Commitment to renew interline, special prorate and code-sharing agreements with Chinese airline companies upon request · Commitment to provide air passenger transport ground services at Korean airports to Chinese entrants for specific routes on FRAND terms · Duration: 10 years; lifted automatically	· Cleared in U.S. · EU: Phase I decision to be issued · UK: Phase I decision found that the proposed transaction could result in higher prices and harm competition. Undertakings were offered, which the CMA proposed to accept, subject to public comments. CMA extended the period to consider the undertakings until Mar. 23, 2023.
***AMD / Xilinx* (2022)**	· Neighboring relationship, giving rise to **conglomerate** concerns, between AMD's CPUs and GPU accelerators and Xilinx' FGPAs. The merged entity would have strong market power in FGPA as Xilinx had a 50-55 percent share in the global and Chinese markets, and the merged entity would be the only manufacturer in the world able to simultaneously supply all three products.	· Continuous supply on FRAND terms of CPUs, GPU accelerators and FGPAs in China · Prohibition against bundling · Guaranteed interoperability with third-party products · Protection of third party information · Duration: 6 years; termination upon application and approval	Cleared in U.S., EU, and UK
***II-VI / Coherent* (2022)**	· **Horizontal** overlaps in seven markets: laser gain crystals; non-linear optical crystals; laser diodes; laser diode modules; beam delivery components; diode lasers; and diode pumped solid-state lasers. · 22 **vertical** relationships in 16 relevant markets	· Continued execution of supply contracts, and continued supply, of CO_2 laser optics on FRAND terms · Commitment to adopt multiple supply channels for procurement of glass-based laser optics · Protection of third-party information · Duration: 5 years; lifted automatically	Cleared in U.S.

Case	Competition Concerns	Behavioral Remedies in China	Outcome in U.S., EU, and UK (if filed)
***SK hynix / Intel* (2021)**	· **Horizontal** overlaps in four markets: PCI enterprise-class SSDs (with a combined share of 40-45 percent globally and 50-55 percent in China), SATA enterprise-class SSDs (with a combined share of 30-35 percent globally and 55-60 percent in China), customer-class SSDs and NAND flash memory · Two **vertical** relationships: (1) between DRAM (upstream) and SSDs (downstream); and (2) between NAND flash memory (upstream) and SSDs (downstream)	· Pricing commitment: not to increase prices for PCIe enterprise-class SSDs and SATA enterprise-class SSDs above a certain level in the Chinese market · Commitment to expand production of PCIe and SATA enterprise-class SSDs · Commitment to supply all products of the merged entity in China on FRAND terms · Prohibition against exclusive dealing and bundling · Commitment to assist third party market entry · Commitment not to collude with competitors in China on price, sales, and production volumes · Duration: 5 years; termination upon applicant and approval	Cleared in U.S., EU, and UK
***ITW / MTS* (2021)**	· **Horizontal** overlaps in four markets: ground vehicle durability testing equipment, static material testing equipment, electric mechanical material testing equipment, and high-end electro-hydraulic servo material testing equipment	· Continued fulfilment of existing contracts with Chinese customers · Commitment not to raise relevant product prices above a certain level · Prohibition against unreasonable trading terms, or degrading product or service quality or technical level, in relation to Chinese customers · Duration: 5 years; termination upon application and approval	N/A
***Cisco / Acacia* (2021)**	· **Vertical** relationship, giving rise to input foreclosure concerns. Acacia is active in the upstream coherent Digital Signal Processors ("DSP") market, with a 45-50 percent global share and a 40-45 percent China share. Cisco operates in the downstream optical transmission systems market. SAMR found that the merged entity will have the ability and motive to block material supplies, through refusal to deal and raising coherent DSP prices. · Neighboring relationship, giving rise to **conglomerate** concerns, in optical transceiver modules and routers.	· Continuous execution of existing customer contracts · Continuous supply on FRAND terms of coherent DSPs to Chinese customers · Prohibition against bundling · Training for management staff and employees · Duration: 5 years; lifted automatically	Cleared in U.S.

IV. CHINA'S RECEPTIVENESS TO BEHAVIORAL REMEDIES

China's receptiveness and recourse to behavioral remedies can be explained on a few possible grounds. As noted above, industrial policy considerations pertaining to the national economy play an influential part in SAMR's decision-making. The Anti-Monopoly Law of China ("AML") expressly authorizes and mandates SAMR to consider, among other factors, the impact on national economic development in reviewing any concentration of undertakings.[30] This means that SAMR must consider and try to reconcile viewpoints from many different stakeholders in China with respect to the clearance of a transaction – not only customers, but trade associations, competitors, and other government ministries and agencies. As a result, SAMR has never had the luxury of trying to defend a single ideological standard (such as the traditional consumer welfare standard) and instead must find a way to satisfy the sometimes conflicting views of many while not over-deterring foreign investment or global transactions more generally.

Thus, while SAMR has an ostensibly broader mandate than its Western counterparts to consider extra-competition concerns, it has been careful still not to over-reach in prohibiting transactions. Indeed, since the establishment of the AML in 2008 to date, only three transactions have been blocked in China.[31] In this way, SAMR seeks to address and resolve issues raised by specific transactions, rather than relying on over-deterrence that could discourage foreign investment in China or business activities more generally.

In this way, as SAMR solicits and considers input from a wide range of Chinese stakeholders, which can in many cases be conflicting, it engages with stakeholders with a view to reconciling competing interests and achieving a consensus on the terms of a clearance. Often "threading the needle" to resolve complaints without arbitrarily blocking deals requires the flexibility of behavioral commitments. Indeed, SAMR uses behavioral remedies to preserve flexibility while giving regulators visibility and some degree of control over competitive dynamics in the market. A senior Chinese antitrust official has explained that *"behavioral remedies can be tweaked and adapted over time to reflect shifts in the market."*[32] Implicit in this statement is the fact that ideological differences as to theories of harm should not hinder China from pursuing what might otherwise be an effective remedies solution.

Importantly, with respect to the purported administrative difficulties and burdens of monitoring, SAMR has proven more willing than its counterparts to bear the regulatory burden of negotiating remedies and monitoring compliance, and has developed a sophisticated enforcement regime. Generally, the parties will submit a commitment proposal (before which there can already be multiple rounds of communications with SAMR), and SAMR will evaluate the proposal by consulting with stakeholders and conducting market tests. The parties will then go through a monitoring trustee selection process with SAMR, and will submit a detailed implementation plan ("DIP") for SAMR's approval. The monitoring trustee will produce its own DIP on how to monitor implementation, and can take actions including on-site examination, requests for information, meeting with the parties and contacting stakeholders.

Notably, the burden of drawing up a behavioral remedy proposal falls to a large extent to the parties (not the government), and costs associated with on-going compliance are also borne largely by the parties. As can be seen from Table 1 above, a proportion of behavioral commitments in China automatically expire, while others are lifted upon application, showing the benefits of flexibility offered by these remedies. For instance, in April 2020, SAMR lifted the remedies imposed in 2014 in respect of the establishment of a joint venture by Corun, Toyota, Primearth EV Energy and Sinogy upon the parties' application, on the ground that there have been material changes in the competitive dynamics of the market, including the changes in the applicable policies in the automotive industry, the advancement of technology and the parties' decreasing market share.

SAMR's approach then raises the question as to whether the administrative difficulties of monitoring compliance are indeed so insurmountable as perceived in other jurisdictions. Public records show that non-compliance with behavioral remedies is not a common occurrence in China. Indeed, there have only been two instances in which administrative sanctions have been imposed for non-compliance: *Western Digital/Hitachi* (2012) and *Thermo Fisher/Life Technologies* (2014).

- *Western Digital/Hitachi* (2012): A fine of approximately USD 97,369 (RMB 600,000) was imposed on Western Digital for its failure to comply with the hold separate remedy attached to the conditional clearance of Western Digital's acquisition of Hitachi's hard disc drive unit. According to the hold separate condition, Viviti Technologies (previously named Hitachi Global Storage Technology) would continue to operate as an independent competitor and maintain independent business operations for two years after the transaction closed. It was

30 Article 33(5), AML.

31 The three prohibited transactions in China are: *Coca-Cola/Huiyuan Juice* (2009); *Maersk-Mediterranean Shipping-CMA CGM (P3 Network)* (2014); and *Huya/DouYu* (2021).

32 McConnell, *Top Chinese official defends use of behavioral remedies* (GCR, Jul. 7, 2021).

found that Western Digital had violated this condition, by consolidating two of Viviti's business units into Western Digital and transferring employees thereunder to Western Digital.

- *Thermo Fisher/Life Technologies* (2014): Thermo Fisher was fined approximately USD 23,824 (RMB 150,000) for its failure to comply with one of the behavioral conditions imposed for its acquisition of Life Technologies – to provide the requisite level of discounts to Chinese customers. It was found that the failure was due to an unintentional error and it occurred only for a small percentage of the relevant products. Moreover, Thermo Fisher took immediate measures to remedy its wrongdoing. These mitigating circumstances were taken into account in the total penalty imposed.

Based on these experiences in China, it would appear that the costs and uncertainties of successful implementation traditionally associated with behavioral remedies may be over-stated.

It is noteworthy that the AML, as amended since Aug. 1, 2022, now imposes much heavier fines for remedy breaches than the AML of 2008. Under the current, amended AML, the maximum fines for merger control violations, including breach of remedies or prohibitions, failure to notify, and gun-jumping, are significantly increased to 10 percent of the revenues in the preceding year, for concentrations that eliminate or restrict competition; or approximately USD 750,000 (RMB 5 million) for concentrations that do not lead to competition concerns.[33] Before the amendment, the maximum penalties were only approximately USD 75,000 (RMB 500,000).[34] Another amendment to the AML was the introduction of an aggregated penalties provision, allowing violations with "particularly serious circumstances, egregious impact, and serious repercussions" to be punished by two to five times the base amount.[35] With these amendments, the current AML is expected to be able to better deter non-compliance with behavioral remedies.

V. POLICY IMPLICATIONS

From a policy perspective, SAMR's willingness to accept behavioral remedies to avoid unnecessarily blocking generally pro-competitive transactions has the benefit of encouraging parties to pursue creative and flexible solutions. The contrasting approach in the U.S. and UK may be leading to over-enforcement and have a chilling effect on M&A activities, as it disincentivizes complex transactions,[36] especially vertical deals that could have achieved procompetitive efficiency benefits through improving synergy. Based on recent statistics from the U.S., this seems plausible.

In the U.S. in 2022, 60 percent of significant merger investigations resulted in a complaint or abandoned transaction, marking a significant increase from 37 percent in 2021, which was already a record high since 2016; 2022 also witnessed the highest number of litigation complaints filed to block transactions since 2011.[37] This was perhaps not surprising, given DOJ Assistant Attorney-General Jonathan Kanter's remark in Nov. 2021 that investigations resolved with merger remedies should be the exception, not the rule. Only two significant investigations concluded in the fourth quarter of 2022, which is a record low for what is normally the most active quarter of the year, suggesting that there could have been a drop in overall activity in the U.S.

Although the EU is less hawkish compared to the U.S. and UK, deal statistics suggest that the regulatory challenges in the EU also might have dampened the incentives for M&A transactions. In 2022, six deals were abandoned or blocked following a Phase II investigation, the highest number ever recorded since 2011 and nearly 200 percent above the average between 2011 and 2021. Regulatory challenges were explicitly cited as the reason for abandoning the transactions in *Nvidia/Arm, Kronospan/Pfleiderer Polska* and *Kingspan Group/Trimo.*

33 Article 58, AML (current version).

34 Article 48, AML (2008 version).

35 Article 63, AML (current version).

36 SAMR's policy of encouraging M&A activities can also be observed from cases that received unconditional clearances in China, but were blocked by other regulators. For instance, *AoN/Willis Towers Watson* (2021) was unconditionally cleared in China, but blocked in the U.S. and subjected to structural remedies (divestment) in the EU. *Konecranes/Cargotec* (2021) was unconditionally cleared in China but blocked in the U.S. and UK.

37 DAMITT 2022 Annual Report: Timing and Remedy Risks Grow for Transactions Hit with Significant Investigations.

VI. TAKEAWAYS AND THE WAY FORWARD

Ideological considerations aside, China has shown that behavioral remedies can successfully be implemented and monitored, and administrative costs and burdens on the government may have been overstated. This is so considering the fact that many behavioral commitments in China automatically expire, and others can be lifted by SAMR upon application by the parties to reflect changing circumstances. The flexible manner in which behavioral remedies can be employed and adapted over time undercuts the argument of administrative burden.

It remains to be seen whether the U.S. and UK can soften their stance against behavioral remedies to avoid disincentivizing transactions that could otherwise be beneficial to the economy. In the UK, with the establishment of the new Digital Markets Unit ("DMU") within the CMA to operationalize the regulatory regime for digital markets with the resources and express authority to *"implement pro-competition interventions including interoperability and access to data,"*[38] there is, theoretically speaking, a potential path forward for the CMA to be more receptive to behavioral remedies. Indeed, CMA official Colin Raftery indicated in a speech in Feb. 2023 that behavioral remedies could theoretically be used in regulated markets or to address very short-term concerns, but speculated again that they are difficult to employ in fast-moving markets.[39]

On a more positive note, recent developments in the EU signal that behavioral remedies will continue to be a viable solution in cases where foreclosure or conglomerate concerns are the issues. In a Dec. 2022 speech, Olivier Guersent, the Director-General of the Directorate General for Competition, commented that behavioral remedies are well-suited for deals in which the merging parties are active in neighboring markets, such as digital ones. He cited the data silo remedy that the EC accepted in its clearance of Google's acquisition of Fitbit, the access remedy accepted in Meta's acquisition of Kustomer and the interoperability remedy used in the LinkedIn/Microsoft transaction. Mr. Guersent acknowledged that monitoring should not be difficult, and breaches should be quickly and easily identifiable.[40]

The experience in China shows that behavioral remedies can be an important and useful tool for competition regulators to achieve a balance between, on one hand, protecting and preserving market competition, and on the other hand, avoiding the chilling effects of over-enforcement on M&A transactions. The "politicization of antitrust" has been observed by some as a common trend across jurisdictions.[41] As regulators move away from the traditional "consumer welfare standard" to consider the impact of a transaction more holistically, deal parties face increasingly strong regulatory headwinds and greater uncertainties in regulatory outcomes. If SAMR's lessons in behavioral remedies could be of reference value to other regulators, that could be positive news to transactional parties.

38 *CMA's Digital Markets Unit: exciting opportunities to influence the regulation of big tech* (CMA Blog, Jan. 7, 2022).

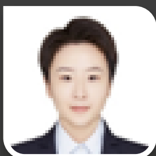
39 Madge-Wyld, *DMU could steer rethink on behavioral remedies in digital mergers, CMA official says* (GCR, Feb. 2, 2023).

40 *EC Official Endorses Behavioral Remedies in Digital Markets Merger Cases* (PaRR, Dec. 14, 2022).

41 See, e.g. Pasquale & Green, *Two Politicizations of U.S. Antitrust Law*, Symposium: Consumer Welfare, Market Structure, and Political Power (2019); Zhang, *Chinese Antitrust Exceptionalism, How the Rise of China Challenges Global Regulation* (Oxford University Press, 2021); and Ezrachi, *Sponge*, Journal of Antitrust Enforcement (2016) 1-26.

MERGER REMEDIES IN CHINA IN 2022 AND THE PREVALENCE OF "CONTINUE TO SUPPLY UNDER FRAND PRINCIPLES" AS THE REMEDIES

BY JOHN YONG REN, CHRISTINE ZHANG & SCHIFFER SHI[1]



1 Dr. John Yong REN is the Managing Partner of T&D Associates. Christine Fengyi Zhang is the Partner and Dr. Schiffer Mengmeng Shi is the senior associate of T&D Associates. We would like to thank Mengyao Yu for her contribution to this article.

I. INTRODUCTION

2022 was the 14th anniversary since China's Anti-Monopoly Law ("AML") came into force in 2008. 2022 witnessed the first amendment[2] made to the AML that not only reflected Chinese competition authority's experience accumulated during the past decade's enforcement, but also reflected the evolving expectations attached to the AML.

Examples for the former include the introduction of "stop the clock" mechanism[3] in the merger review procedures which one may perceive by referring to the EU Merger Regulation. The new AML's the explicit prohibitions on undertakings' anti-monopolistic conducts in the areas of data, algorithm, technology, and capital advantages, etc., as well as the inclusion of "encouraging innovation" in the General Chapter of the AML can be regarded as the evolving expectations and multi-dimensional aims of the AML.

Against the background of the AML amendments, this article will discuss the topic in relation to the merger control mechanism in China – the remedy imposed on the conditional approvals.

In 2022, as the central competition authority in China, the State Administration for Market Regulation ("SAMR") approved 5 cases conditionally, which was summarized as follows.

Table 1 | Conditional Approvals in 2022

Case	Relevant Market	Types of Remedies	Main Remedies
Global Wafers' acquisition of Siltronic	8-inch zone-melt wafer	Hybrid	• Divestment • **Continue to supply wafers under FRAND[4] principles** • No refusal of customers' request for contract renewal after expirations • Training for relevant personnel
AMD's acquisition of Xilinx	GPU, CPU, FPGA	Behavioral	• No tying / imposing unreasonable trading conditions • **Continue to provide products/service under FRAND principles** • Ensure the flexibility and programmability of Xilinx FPGAs • Maintain interoperability • Protection of confidential information from third parties
II-VI's acquisition of Coherent	Laser and laser optics	Behavioral	• Fulfil existing contracts and terms • **Continue to supply CO2 laser optics under FRAND principles** • **Continue to multisource and conduct procurement under non-discriminatory term** • Protection of competitively sensitive information
Joint venture ("JV") between Shanghai Airport and Eastern Airlines Logistics ("EAL")	Airport cargo terminal services and air cargo services	Behavioral	• Hold-separate of the parties' cargo terminal business • Keep competition between the parties and the JV • No exchange of competitively sensitive information among the parties and the JV • Fulfil existing contracts and no refusal of customers' request for contract renewal after expirations • **Shanghai Airport, EAL and the JV continue to provide service under FRAND principles**
Korean Air' acquisition of Asiana Airlines	Air passenger and air cargo services	Behavioral	• Return of slots at airport • Return of traffic rights • **Continue to supply certain air routes** • Renewal of air passenger service agreement • **Provide air passenger auxiliary services under FRAND principles**

2 The amended AML was effective as of 1 August 2022.

3 According to Article 32 of the new AML, the competition authority may decide to suspend the calculation of the review period of a merger review: (1) undertakings fail to submit the documents and materials in accordance with the provisions, resulting in that the review cannot be conducted; (2) the emergence of new circumstances and new facts that have a significant impact on the review of the concentration of undertaking, and the review process cannot be proceeded if they are not verified; (3) the restrictive conditions to be attached to the concentration of undertakings need to be further evaluated, and the undertakings raise a request for suspension.

4 FRAND refers to Fair, Reasonable and Non-Discriminatory.

As can be observed from Table 1, all conditional approvals were subject to the so-called "continue to supply under FRAND principles." Therefore, against the background of the AML amendment, it can be natural to ask: why such remedies, which was originated from Standard Essential Patents of the intellectual property field, were so prevalent in China's merger review? What can we learn from SAMR's such practice (if not preference)? what can be expect in the future cases?

To answer these questions and to present the readers the general picture of the conditional approvals in 2022, this article will be structured as follows. Section II will recap the conditional approvals in 2022 from both procedural and substantive perspectives to give the readers an overview of SAMR practice of merger control in 2022. Section III will discuss and explore the possible considerations and reasons behind the mentioned prevalence of continue to supply under FRAND principles. Conclusions and observations will be presented in Section IV.

II. AN ANALYSIS ON SAMR'S CONDITIONAL APPROVALS IN 2022

A. Procedural Perspectives

1. Timing

As mentioned, the year 2022 saw five conditionally approved merger cases in China, including, for the first time ever, one case that only concerned domestic enterprises. The timing for the merger review of these cases was summarized in Table 2.

Table 2 | Reviewing Time for Conditional Approvals in 2022

Case Name	Timing		Total Months
Globalwafers/Siltronic AG	2020.12.25	Submission of the Notification	Approx. 13 months
	2021.3.29	Initiation	
	2021.9.24	Withdrawal	
	2021.9.29	Refile	
	2022.1.20	Conditional approved	
AMD/Xilinx	2021.1.19	Submission of the Notification	Approx. 12 months
	2021.4.7	Initiation	
	2021.9.30	Withdrawal	
	2021.9.30	Refile	
	2022.1.21	Conditional approved	
II-VI/Coherent	2021.6.22	Submission of the Notification	Approx. 12 months
	2021.9.18	Initiation	
	2022.3.14	Withdrawal	
	2022.3.15	Refile	
	2022.6.28	Conditional approved	
Shanghai Airport Authority/Eastern Air Logistics (both were domestic enterprises)	2021.10.21	Submission of the Notification	Approx. 11 months
	2021.11.8	Initiation	
	2022.4.29	Withdrawal	
	2022.4.29	Refile	
	2022.9.13	Conditional approved	

Korean Air/Asiana Airlines	2021.1.15	Submission of the Notification	Approx. 23 months
	2021.3.23	Initiation	
	2021.9.18	Withdrawal	
	2021.10.8	First refile	
	2022.4.2	Withdrawal again	
	2022.4.7	Second refile	
	2022.4.26	Initiation again	
	2022.12.26	Conditional approved	

The average reviewing time for these conditional approvals in 2022 accounting from the submission of notifications till approvals was around 14.2 months, with all cases being withdrawn and refiled. Comparatively, the average reviewing time for conditional approvals in 2020 and 2021 was, respectively, 9.75 months and 11.5 months. Of the 4 conditional approvals in 2020, 2 cases were withdrawn and refiled, while all cases in 2021 were withdrawn and refiled. In particular, *Cisco/Acacia* (2021) was refiled twice, like *Korean Air/Asiana Airlines* in 2022. Therefore, it seems to be fair to conclude that in 2022, it took longer time for SAMR to review these conditional approvals which were featured as complexity and the percentage of "withdrawal and refiling" was 100 percent for 2021 and 2022, and 50 percent for 2020.

Accordingly, it is natural to perceive that the introduction of "stop the clock" mechanism in the amended AML can be a solution to help the competition authority to get out of the dilemma where they need more time to review the notified transactions while they run out of the time under the timeline in the old AML (i.e. 180 calendar days in total from case initiation till the expiration of the extension of Phase II), which was featured as "non-stop."

2. Acceptance and approval of the remedy proposal

The following table summarizes the dates for acceptance and approvals of the remedy proposals.

Table 3 | Date for Accepting Remedy Proposal and Final Approvals

Case Name	Date for SAMR Accepting the Final Version of the Remedy Proposal	Approval date	Time In-between
Globalwafers/Siltronic AG	2022.1.18	2022.1.20	2 days
AMD/Xilinx	2022.1.13	2022.1.21	8 days
II-VI/Coherent	2022.4.1	2022.6.28	Around 3 months
Shanghai Airport Authority/Eastern Air Logistics	2022.7.18	2022.9.13	Around 2 months
Korean Air/Asiana Airlines	2022.12.2	2022.12.26	24 days

It can be observed that the time between the acceptance of the final draft remedy proposal and the approval of the case varied greatly. According to the authors' experience, such difference can be resulted from which draft that SAMR rested on when conducting market tests.

Like the EC's practice, SAMR consults with relevant stakeholders as part of its assessment on the sufficiency and suitability of a remedy proposal. It believes that if a remedy proposal was submitted to SAMR before it disclosed its competition concerns, or SAMR's market test was conducted based on a near-to-final version of remedy proposal, suggesting SAMR's assessment and the market test happened simultaneously, then it is likely that the time gap between the final draft remedy proposal and the case approvals can be short.

By contrast, if SAMR conducted its market test based on the very near-to-final version of a remedy proposal, meaning SAMR assessed the remedy proposal first followed by a market test, then likely, there would be a long gap between the submission of the final draft and the case's approval because it takes time for the stakeholders to respond to SAMR's consultation.

B. Substantial Perspective

1. Industry Concerned

As Table 4 demonstrates, the conditionally approved transactions in 2022 concerned sensitive industries such as semiconductors.

Table 4 | Industry Concerned in the Conditional Approvals in 2022

Case Name	Industry Concerned
Globalwafers/Siltronic AG	Semiconductors (wafers)
AMD/Xilinx	Semiconductors (GPU/CPU/FPGA)
II-VI/Coherent	Semiconductors (lasers/laser optics)
Shanghai Airport Authority/Eastern Air Logistics	Airport cargo terminal services/Air cargo service
Korean Air/Asiana Airlines	Air cargo service/Air passenger service

There is high sensitiveness around those semiconductor-related cases, which may stoke SAMR's extra concerns about industry development in addition to its competition concerns. Consideration of industry development is actually in line with the multi-dimensional goals of the AML, which include to promote the healthy development of socialist market economy. Such sensitiveness was likely to result in SAMR's scrutiny on these cases.

2. Competition Concerns and Remedies

Based on Table 1 supra, Table 5 below further summarized the types of competition concerns and the imposed remedies of these conditional approvals in 2022.

Table 5 | Competition Concerns and Remedies of Conditional Approvals in 2022

Case Name	Horizontal Overlap	Vertical Relationship	Conglomerate Relationship	Types of Remedies
Globalwafers/Siltronic AG	√			Hybrid
AMD/Xilinx			√	Behavioral
II-VI/Coherent		√		Behavioral
Shanghai Airport Authority/Eastern Air Logistics	√	√		Behavioral
Korean Air/Asiana Airlines	√			Hybrid

As can be observed from Table 1 and Table 5, consistent with practice of the EC, structural remedies were adopted by SAMR to address horizontal concerns, while Behavioral remedies were used to address non-horizontal concerns.

Further, as mentioned above, FRAND terms are commonly imposed by SAMR and in 2022, all conditional approvals were subject to the so-called "continue to supply under FRAND principles," regardless of whether the transactions concerned horizontal concerns or not. The section below will explore the reasons behind the prevalence of such remedies.

III. EVOLUTION OF "CONTINUE TO SUPPLY UNDER FRAND PRINCIPLES" AND THE POSSIBLE REASONS BEHIND

A. Evolution of "Continue to Supply under FRAND Principles"

The remedy of "continue to supply under FRAND principles" did not form its shape in one move. Indeed, similar remedy was for the first time imposed on *General Motors/Delphi*, a case that was conditionally approved in 2009 – one year after the enactment of the AML in 2008. In this

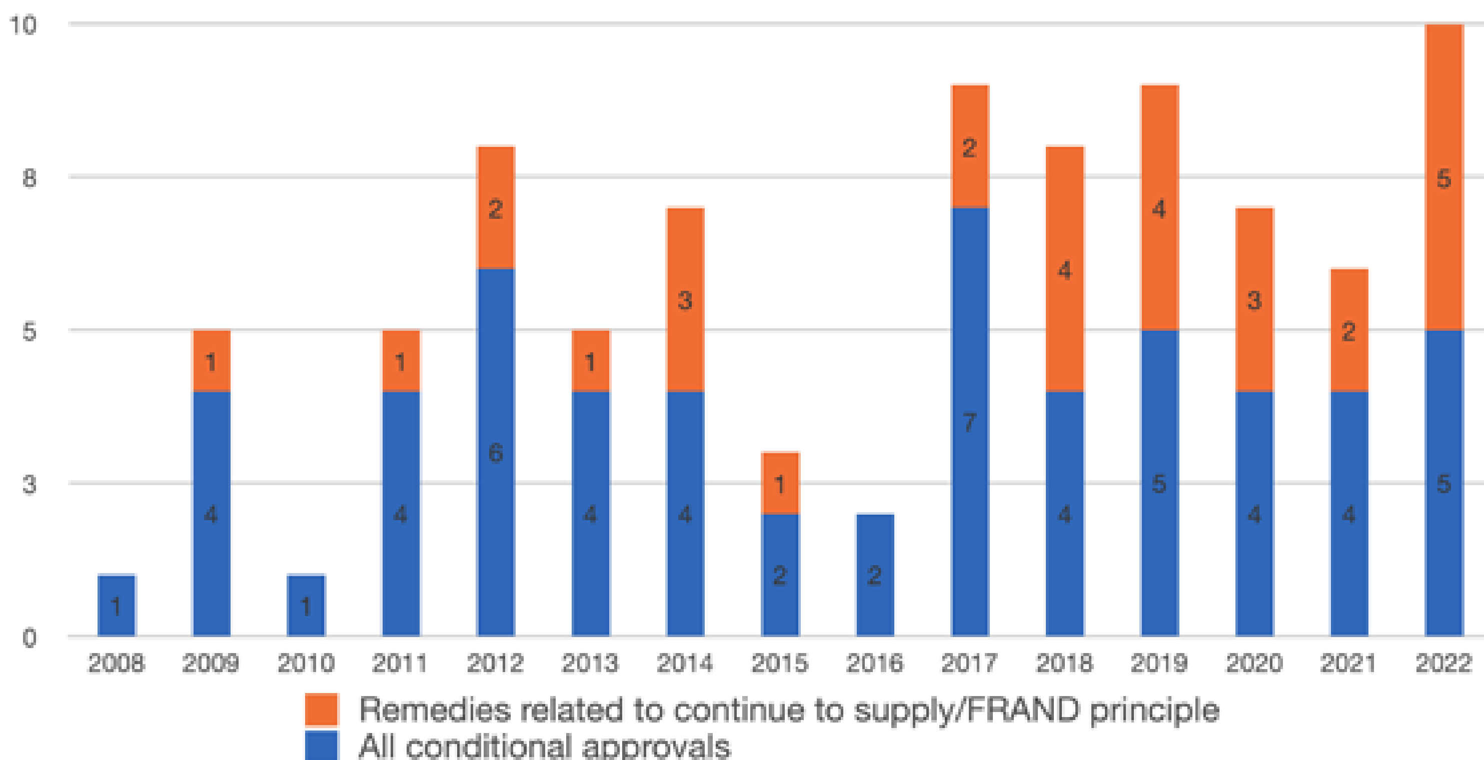
case, the parties were required to continue to supply "without discrimination." *Henkel/Tiande Chemical* (2013) was the first case on which a full array of "FRAND principles" were imposed, i.e. the parties were required to continue to supply ethyl cyanoacetate under fair, reasonable, and non-discriminatory principles.

When looking back at these precedents, one may notice that when the parties were required to continue to supply products/services, conditions of "Fair, Reasonable and Non-Discriminatory" may or may not be included, or one or more of such conditions can be included. Table 6 below provides a summary regarding how the language can be structured. Figure 1 further summarizes the use of such remedies since 2008.

Table 6 | Evolution of "Continue to Supply under FRAND Principles" in Conditional Approvals (selected)

Case	Relevant Remedies
General Motors/Delphi (2009)	*Supply its auto customers in China without discrimination*, and continue timely and reliably supply and to maintain the quality of its products…
Henkel/Tiande Chemical (2012)	Tiande Chemical shall provide ethyl cyanoacetate to *all downstream clients under the principle of fairness, reasonableness, and non-discrimination…*
Glencore/Xstrata (2013)	Glencore shall *continue to offer to supply* Chinese customers with zinc concentrate and lead concentrate …the offered terms (including price-related terms) *shall be fair and reasonable* …
KLA-Tencor/Orbotech (2019)	KLA-Tencor, Orbotech and the Combined Entity *shall continue to maintain stable supply* of semiconductor process control equipment and related services…on *fair, reasonable and non-discriminatory terms*.

Figure 1 | Conditional Approvals and Inclusion of "Continue to Supply on FRAND Principle" Remedies during 2008 to 2022



The average percentage of the use of "continue to supply under FRAND principles" in the recent five years (2018 – 2022) was 81.8 percent, nevertheless, such percentage for the years from 2008 to 2017 was only 31.4 percent, which clearly demonstrates the increasingly prevalence of such remedies in China.

B. Possible Reasons for the Prevalence

1. Extra Protection for Contract Performance

According to the authors' experience, once the competition authority disclosed its concerns on stable supply post-transaction, the parties were likely to argue that their customers were protected by legally binding contracts, and it would be unnecessary to make commitments like "continue to supply under FRAND principles." The parties can also provide supportive analyses to argue that they were lack of ability and incentives to stop their supply or supply in an unfair, unreasonable, and discriminatory way. However, the competition authority can quite persist to the inclusion of remedies of "continue to supply under FRAND principles."

In fact, "continue to supply (perform contract)" is a remedy which originated from the previous Contract Law and the current Article 577 of the China Civil Code, which regards "continue to perform" as a liability for the party that breach a contract. In practice, it may take long time and require significant cost for one party of a contract to claim its rights and require the other party that breaches the contract to continue to perform the contract, either through litigations or through mediations. In the context of merger filings, this may largely stoke SAMR's concerns for the effectiveness and timeliness of the protection of the parties' customers post-transaction in relation to contract performance.

From this perspective, the inclusion of remedies of "continue to supply under FRAND principles" may provide extra security of contract performance. Such a remedy provides customers with another approach to seek protection under the AML when the post-transaction entity breaches the supply contract.

2. A Solution to Address Both Competition Concerns and Industrial Concerns

The goals of the AML, including protecting the interests of consumers and the public, and promoting a healthy development of the socialist market economy (can be understood as promoting industry development), is featured as multi-dimensional. In the context of merger remedies, such a feature results in the fact that a remedy is expected to address not only competition concerns, but also industry concerns.

Like the EC practice, SAMR consults with stakeholders during its review of a notified transaction and such stakeholders always include relevant industrial associations whose feedbacks represent the voice of the relevant industry that a notified transaction concerned. It is possible that while a transaction may have limited competition concerns, it stokes industry concerns. Take cases concerning semiconductors as an example.

Semiconductor industry is of high strategically importance to China. For certain semiconductors, Chinese companies may largely rely on overseas suppliers for inputs. While a transaction in such relevant market can be a conglomerate one and according to theory of harm, such a merger is unlikely to result in anti-competitive effects, downstream Chinese companies can feel highly unsecure about the parties' post-transaction supply practice strategy. Due to their high reliance on the parties, any stop of supply (or even delay of supply) would result in significant loss, even endanger the future development of the relevant market. In such a situation, remedies of "continue to supply under FRAND principles" can be one of the optimal options to respond to these concerns.

While the semiconductor cases are only one example, it may to a large extent reveal one of the reasons behind the prevalence of "continue to supply under FRAND principles," i.e. to address not only competition concerns, but also industrial concerns.

3. Reference to Precedents During Remedy Negotiations

The remedy negotiation is a process of bargaining with the parties and their counsels on the one side and SAMR and its case team on the other side. While in some exceptional cases, same goal may not be shared by two sides – remedies negotiation might be used by SAMR as a way to drag a transaction to dead, and this can be particularly true when a transaction received strong industry complaints from stakeholders, but the possible competition concerns did not justify a straightforward prohibition from SAMR, which is the competition authority rather than an industrial regulator.

For those transactions in which both sides shared the same goal, i.e. clear the transactions, during the remedy negotiation, both sides refer to the precedents with similar competition concerns to persuade the other side and to reach a consensus on the remedies as soon as possible.

From the parties' and counsels' perspective, borrowing language from precedents provide with them the sense of security to the extent possible because, *inter alia*, they clearly know that there are predecessors that made similar commitments and SAMR accepted that. This can be particularly important when the parties are foreign enterprises that are unfamiliar with the AML and SAMR's practice and thus foreseeability and predictability are required when assessing the possible impact of a remedy. These precedents provide such insights perfectly.

This is also true from SAMR perspective. As the gatekeeper, SAMR needs to know whether and to what extent a remedy will address the competition concerns effectively. Precedents provides SAMR with such knowledge. SAMR can be in a better position to assess the sufficiency of a remedy proposal if such proposal refers to precedents. Also, this gives SAMR case team more comfort as the wordings used in precedents have already been reviewed and approved by other SAMR case teams and superior officials.

Accordingly, "continue to supply under FRAND principles" form its current shape through different cases referring to precedents and further being tailored to address SAMR's concerns on post-transaction stable supply.

IV. CONCLUSIVE REMARKS AND FUTURE TRENDS

The number of conditional approvals in 2022, 5 in total, was not surprising when comparing with such number in 2021 and 2020. Nevertheless, SAMR's average reviewing time for such cases reached approx. 14.2 months, which was longer than that in both 2021 (11.5 months) and 2020 (9.75 months) and all 5 cases experienced "pull and refile." Longer reviewing time may be relevant to the sensitiveness around the industry concerned in these cases – semiconductor. It expects that the introduction of "stop the clock" mechanism in the new AML may reduce the use of "pull and refile" given that it confers on the competition authority the rights to stop the reviewing clock when it needs necessary.

Like the EC and competition authorities in the US, structural remedies were used by SAMR to address concerns brought about by horizontal overlaps. As to the behavioral remedies, it is interesting to notice that "continue to supply under FRAND principles" were increasingly used. The percentage of such use was as high as 81.8 percent during 2018 to 2022, while such percentage for the years from 2008 to 2017 was only 31.4 percent.

The prevalence of "continue to supply under FRAND principles" can resulted from the need to provide extra protection for contract performance, given the possible long time and significant cost involved in solving contract breach through litigations or mediation. Such remedies may also serve as an option to address both competition concerns and industry concerns in light of the AML's multi-dimensional goals, which may to some extent result in the trade-off between different goals. The negotiation of merger remedies and the reference made by both the parties (and their counsels) and SAMR case team can also explain the prevalence of the mentioned remedies, which provides both sides the foreseeability and predictability to a large extent.

The mentioned percentage of 81.8 percent clearly demonstrates SAMR's high acceptance of the remedies "continue to supply under FRAND principles" to address concern about post-transaction stable supply of relevant products/services. Considering the effectiveness of such remedies to satisfy the requirements of providing extra protection of contract performance and addressing both competition and industry concerns, we believe these remedies are likely to be used and accepted by both the parties and SAMR.

WHAT TO EXPECT OF CHINESE MERGER CONTROL REVIEWS OF GLOBAL SEMICONDUCTOR DEALS FOLLOWING AMENDMENTS TO THE ANTI-MONOPOLY LAW

BY HAZEL YIN, HAOYANG ZHUO & LAURENT BOUGARD[1]

1 Hazel Yin is an antitrust partner at RuiMin Law Firm, China. Haoyang Zhuo is an associate with the Antitrust, Competition & Trade group at Freshfields Beijing office. Laurent Bougard is a senior associate with the Antitrust, Competition & Trade group at Freshfields Hong Kong office. The authors would like to thank Ethan Qu and Xiaopeng Lai at Freshfields Beijing office for their research assistance. The views expressed herein are those of the authors only and do not represent those of the entities that the authors are affiliated with.

I. INTRODUCTION

The numerous semiconductor transactions around the globe in the past few years have included transformative multi-billion deals with potentially far-reaching impact on the global semiconductor landscape, as well as many smaller deals (some statistics indicate that 80 percent of semiconductor deals were valued below $1bn in the last five years).[2]

Despite volatility in demand for semiconductor products and a projected modest decline in global semiconductor revenue in 2023,[3] robust demand remains in a few segments, shifting from consumer electronics to emerging areas like the internet of things ("IoT"), 5G connectivity and, most notably, the automotive industry, which has suffered from a chip shortage. This chip shortage has also spurred considerations of how to secure a stable access to these key inputs.

As industry consolidation continues, navigating regulatory challenges associated with competition authorities in different jurisdictions has become critical for successful deal-making. China is the top market for semiconductor products across different layers of the supply chain so a Chinese merger control filing is very often required. In 2021 alone, transactions reviewed by China's antitrust regulator, the State Administration of Market Regulation ("SAMR") for merger control in the semiconductor sector amounted to a total transaction value of RMB 736.1bn.[4]

In addition to geopolitical complexities, especially following China-U.S. trade tensions, August 2022 marked a new era for antitrust in China, with the amended Anti-Monopoly Law (the "New AML") coming into force. The New AML brought about sweeping changes, including potentially heightened scrutiny of mergers and acquisitions concerning critical areas such as the national economy and people's livelihood.[5] while it does not specifically target the semiconductor industry, it may impact the merger control review practices applicable to semiconductor deals, particularly considering that the semiconductor industry is one of the most heavily scrutinised sectors in China.

II. A GLANCE AT MERGER REVIEW STATISTICS FOR SEMICONDUCTOR DEALS IN CHINA

In 2021, SAMR completed reviews of 727 transactions, including 26 semiconductor transactions. While semiconductor deals only account for less than 4 percent of transaction volume, they contribute approximately 20 percent by value in all merger control reviews SAMR completed in 2021.

Chart 1 Completed merger review cases in 2021

2 See Accenture's report at https://www.accenture.com/_acnmedia/PDF-176/Accenture-Semi-MA-Value-Extraction-From-Smaller-Deals.pdf.

3 For example, Gartner projected a 3.6 percent decline in global semiconductor revenue in 2023. See Gartner's projection available at https://www.gartner.com/en/newsroom/press-releases/2022-11-28-gartner-forecasts-worldwide-semiconductor-revenue-growth-to-decline-3-6-percent-in-2023#:~:text=Global%20semiconductor%20revenue%20is%20forecast,billion%20(see%20Table%201).&text=Currently%2C%20the%20semiconductor%20market%20is,markets%20and%20enterprise%2D-driven%20markets.

4 See SAMR's Annual Report on Antitrust Enforcement in China (2021), available at https://www.samr.gov.cn/xw/zj/202206/t20220608_347582.html.

5 See Article 37 of the New AML, which calls for strengthening merger control of transactions in critical sectors impacting national economy and people's livelihood.

On the other hand, semiconductor-related filings have a much larger share in remedy cases – of the 57 conditionally approved transactions by end of 2022, 14 cases concerned semiconductor products or services, accounting for approximately 25 percent. When it comes to the applicable procedures (i.e. normal vs simplified procedure), of the 78 semiconductor deals SAMR reviewed from 2016 to 2020, more than 50 percent of transactions were reviewed under the normal procedure,[6] which typically results in a longer review timeframe of between three and six months. In 2021, the proportion was about 42 percent.[7] By contrast, as a reference, the ratios of filings under normal procedures for the digital sectors, chemicals, and the pharmaceuticals/medical industries are approximately 25 percent, 19 percent and 23 percent in 2021, respectively.[8]

III. POTENTIAL TRENDS AND CHALLENGES FOLLOWING THE NEW AML

A. Timetable Management: Will the New Stop-the-clock Mechanism Help Manage Review Timelines?

Managing regulatory timetables for global transactions is always challenging. In China, once the merger review process is formally initiated (through case acceptance), SAMR has up to 180 calendar days to review and conclude a case.

Before the new AML was adopted, there was no mechanism for SAMR to suspend its review process, even for valid reasons. However, for complicated transactions with competition concerns, it was often challenging to complete reviews within the statutory time limit given the complexity of products and markets concerned, and the time required to identify the concerns and to agree on the proper remedies to address these. Also worthy of note is that SAMR has been under-staffed for many years, with only a handful of case handlers, who concluded more than 700 merger filings in 2021, marking a 54 percent increase compared with 2020.[9]

In practice, if 180 days are not sufficient to complete the China merger review process, the parties would have had to pull and refile the transaction to buy more time. For instance, in 2022, all three conditionally approved transactions in the semiconductor industry, namely Siltronic/GlobalWafers, AMD/Xilinx, and II-VI/Coherent, went through a pull-and-refile process and took over a year to receive approval (see Table 1 below).

Table 1 Review timetable for conditionally approved semiconductor transactions in China

NO.	CASE NAME	TOTAL REVIEW PERIOD (DAYS)	DURATION OF CASE ACCEPTANCE (DAYS)	ANY PULL & REFILE	EXTRA DAYS USED AFTER THE FIRST ROUND OF REVIEW (DAYS)
1	MEDIATEK/MSTAR (2013)	417	60	YES (ONCE)	177
2	MERCK/AZ ELECTRONIC MATERIALS (2014)	106	14	NO	/
3	NXP/FREESCALE (2015)	237	42	YES (ONCE)	15
4	BROADCOM/BROCADE (2017)	222	52	NO	/
5	ASE/SPIL (2017)	457	111	YES (ONCE)	166
6	KLA/ORBOTECH (2019)	292	59	YES (ONCE)	53
7	II-VI/FINISAR (2019)	264	53	YES (ONCE)	31
8	INFINEON/CYPRESS (2020)	239	62	NO	/
9	NVIDIA/MELLANOX (2020)	359	113	YES (ONCE)	66
10	CISCO/ACACIA (2021)	451	59	YES (TWICE)	212

6 See SAMR's Annual Report on Antitrust Enforcement in China (2020), available at http://www.gov.cn/xinwen/2021-09/24/content_5639102.htm.

7 See SAMR's Annual Report on Antitrust Enforcement in China (2021), available at https://www.samr.gov.cn/xw/zj/202206/t20220608_347582.html.

8 The split between normal cases and simple cases is impacted by a series of factors, and most notably the approach to market definition. Under the Chinese merger control rules, if the parties' combined market share exceeds 15 percent for any horizontal overlap or each of the parties' market shares exceed 25 percent in any vertical relationships, the transaction will have to go through the normal procedure. In semiconductor deals, if the parties have a strong market position in a niche market or a potential segment, the authority may be more prudent about whether a broad market definition remains appropriate and may prefer to have a deep dive into any plausible narrower segments to rule out potential anti-competitive effects. This may also explain some of the semiconductor cases where the parties were required to switch their application under the simplified procedure to the normal procedure.

9 See SAMR's Annual Report on Antitrust Enforcement in China (2021), available at https://www.samr.gov.cn/xw/zj/202206/t20220608_347582.html; and SAMR's Annual Report on Antitrust Enforcement in China (2020), available at http://www.gov.cn/xinwen/2021-09/24/5639102/files/77006c5bccc04555aa05f30c9a296267.pdf.

11	SK HYNIX/INTEL (2021)	370	97	YES (ONCE)	93
12	SILTRONIC/GLOBALWAFERS (2022)	392	94	YES (ONCE)	118
13	AMD/XILINX (2022)	368	78	YES (ONCE)	110
14	II-VI/COHERENT (2022)	372	88	YES (ONCE)	104

In an effort to streamline the merger review process, the New AML has introduced a "stop-the-clock" mechanism, enabling SAMR to suspend its review period (with written notice) in any of the following circumstances: (1) the notifying party fails to submit requested information in a timely manner, preventing the review from progressing; (2) new facts emerge that materially impact the review and prevent the review from progressing without verifying the facts first; or (3) the notifying party applies to suspend the review to allow sufficient time for remedy discussions. It is anticipated that the "stop-the-clock" regime will replace the current practice of having to "pull and refile" a transaction in China.

In fact, it is not uncommon around the globe that both regulators and notifying parties are constantly under time pressure to resolve all concerns and complete the review process within the prescribed timeframe, especially when for a high-profile, transformational deal in strategic or sensitive segments. Competition authorities in other jurisdictions have been utilising the "stop-the-clock" mechanism to provide more flexibility and motivation for the parties to properly manage the regulatory timetable. For instance, under the EU merger control regime, the initially set deadline for the European Commission ("EC") to decide on a deal can be extended if the parties fail to provide complete information requested by the EC,[10] and the EC has become more willing to suspend their review clock during the past decade, usually with informal communications and negotiations with the parties for a mutually acceptable re-start date. This practice is limited to in-depth ("Phase II") investigations of transactions.

Failure to provide information required by SAMR in time will probably be the most likely triggering event for SAMR to proactively suspend the review clock. This is also consistent with the stop-the-clock mechanism of the EU, which ties the suspension of review clock with scenarios where the parties have not responded to a formal information request or a part of an information request.

Semiconductor deals can often give rise to lengthy fact-finding processes, with multiple rounds of comprehensive enquiries for notifying parties before SAMR can conclude on a proper scope of market definition (especially in niche markets). These are the starting point for SAMR to establish any theory of harm. A wide scope of market testing and engagement with relevant third parties can also expand the scope of information required, in order to bottom out any potential concerns on defined markets.

The second triggering event for SAMR to proactively stop the clock relates to emergence of new facts that prevent SAMR from proceeding with the review. The amended AML does not provide guidance on what types of changes will qualify as "new facts" that will materially impact the review process. It also remains to be seen how such a suspension mechanism is distinguished from a withdrawal of notifications triggered by significant changes, which is an existing mechanism whereby notifying parties can withdraw their notification in the case of major changes to a transaction or the market competition landscape that warrants a new filing. Without further clarification on the nature of such "new facts," the decision seems largely at SAMR's discretion. The notifying parties in a semiconductor transaction may have to constantly monitor the competition and industry related changes that may impact the China market, to mitigate uncertainty or address potential issues as early as possible.

Despite these uncertainties, it is also expected that SAMR will apply the stop-the-clock mechanism very cautiously as part of the efforts to modernise its merger review process, on top of the efforts already made over the years to accelerate the review process. Above all, the vast majority of the transactions cleared by SAMR have benefited from the simplified procedure, where SAMR will be unlikely resort to suspension of the review clock.

SAMR has also been trying to provide extra comfort and confidence to notifying parties in the application of the new mechanism. For instance, pursuant to the Draft Provisions on the Examination of Concentration of Undertakings (Draft Implementing Rules) published by SAMR alongside the new AML, failure to provide required information would not automatically lead to suspension of the review clock, and the parties can request an additional extension before SAMR eventually decides to stop the clock.[11]

Existing EU practices may shed light on how such a mechanism could work. Similarly, the EU has no ultimate limit on for how long and how many times the review clock can be stopped. But in practice, the EC is usually open to negotiate the submission deadline for pending information requests and the duration of the suspension of review clock. Although such communications are informal and do not legally restrict the EC from extending the suspension, these informal contacts and the agreement on a mutually acceptable re-start date help set forth clearer

10 See Article 10 (Time limits for initiating proceedings and for decisions) and Article 11 (Requests for information) of Council Regulation (EC) No 139/2004 of 20 January 2004 on the control of concentrations between undertakings (the EC Merger Regulation) (*EUMR*).

11 Article 23 of Draft Provisions on the Examination of Concentration of Undertakings for public consultation (2022), available at https://www.samr.gov.cn/jzxts/tzgg/zqyj/202206/t20220624_348145.html.

expectations for next steps and work plans, providing clarity to notifying parties. Such suspensions are observed in the context of requests for a significant volume of internal documents during in-depth investigations – the EC imposes a deadline which cannot be realistically achieved, in turn triggering the informally discussed (if not agreed) suspension of the timeline.

B. Ex Officio Power: Would SAMR Call in a Semiconductor Transaction Below the Turnover Thresholds?

Another highlight of the New AML is the codification of SAMR's power to "call in" a transaction that falls below the filing thresholds and to require the parties to notify if the transaction is likely to eliminate or restrict competition. The call-in power is not new in China: prior to the new AML, the implementing rules of the AML already make it clear that SAMR could call in a transaction for review if evidence indicated that it was likely to be anticompetitive. That said, SAMR has rarely, if ever, exercised its call-in power in the past decade. In fact, there are no procedural rules to follow, even if SAMR intends to call in a transaction.

More proactive enforcement may now become a reality with the Draft Implementing Rules providing for such procedural rules. Pursuant to the Draft Implementing Rules, SAMR has the power to call in a transaction either before or after a transaction has closed (without any time limit).[12] It is also expected that SAMR will explore facts first, during which time the parties may have the opportunity to explain and argue why no Chinese filing is triggered or necessary before SAMR formally determines to call in the transaction and initiate the merger review. Being formally called in can lead to immediate implications on the timeframe of a pending transaction – as Chinese merger control review is suspensory the parties cannot close the deal before receiving SAMR clearance.[13] In the case of a closed transaction, SAMR also has the power to suspend implementation of the transaction until a clearance is granted.[14]

SAMR's call-in power is believed to be aimed at tackling so-called "killer acquisitions," which is a trend that had already been picked up by competition authorities in many jurisdictions. Killer acquisitions refer to transactions where, to avoid future competition, a large incumbent acquires a start-up in order to shut down the latter's products, pipelines or projects before it can grow into a viable competitive threat.[15] Killer acquisitions have become a particular concern in the digital and life science sectors, where the target company may already have substantial market value and growth potential and yet insufficient turnover to trigger a filing requirement. Although SAMR's call-in power can capture killer acquisitions, it enables the authority to review a broader range of potentially problematic transactions such as where the target company is already a well-established player globally and yet has not had significant China presence.

Such flexibility seems particularly relevant to the semiconductor industry – the geographic market of semiconductor products is very often global. This is because modern microchips have billions of components and are ubiquitous, and these hugely complicated products have resulted in an equally complex supply chain composing of thousands of specialised companies across the world.[16] Even if a party or parties do not currently have sufficient turnover or a strong market position in China, the global nature of the market might draw concerns as to whether the market power of the parties outside of China may be easily translated into a similar position in China down the line. Similarly, a semiconductor deal that focuses on niche products, while not a stereotype killer-type acquisition, may still be captured by the call-in power. With the proposed increase of Chinese merger control filing thresholds, where China turnover threshold will double from RMB 400mn to RMB 800mn;[17] more transactions will likely fall below the new thresholds, and may open the door for potential call-in.

This may be particularly relevant to high-profile transactions undergoing close scrutiny in other jurisdictions, which heightens the risk of Chinese stakeholders to spot the transaction and voice their concerns to the Chinese regulators. Vocal third-party complainants knowing the in's and outs of Chinese merger control may be a particular threat to overseas semiconductor transactions. Their complaints can be driven by genuine competition concerns, or industry-related concerns, but also commercial considerations. These can all be raised with SAMR, who would then verify the evidence and take a view on whether a call-in is warranted.

12 See Article 26 of the New AML.

13 See Article 26 of the New AML and Article 7 of Draft Implementing Rules.

14 See Article 7 of Draft Implementing Rules.

15 See OECD report Start-ups, Killer Acquisitions and Merger Control, available at https://www.oecd.org/daf/competition/start-ups-killer-acquisitions-and-merger-control-2020.pdf.

16 See The Economist's briefing, The semiconductor industry and the power of globalization, available at https://www.economist.com/briefing/2018/12/01/the-semiconductor-industry-and-the-power-of-globalisation.

17 See Article 3 of Draft Provisions of the State Council on the Notification Thresholds for Concentration of Undertakings for public consultation (2022), available at https://www.samr.gov.cn/jzxts/tzgg/zqyj/202206/t20220625_348150.html.

This call-in risk serves as a reminder on the importance of managing regulatory uncertainties and identifying China-specific (competition or non-competition) issues upfront – regardless of notifiability – especially in light of the suspensory effect once a transaction is called in.

C. Substantive Negotiation: Will there be Additional Complexity on Remedy Design?

The new AML also imposed additional uncertainty when it comes to discussions on remedies. As mentioned above, the review clock can be stopped if the notifying party applies to suspend the review to allow sufficient time for remedy discussions. Ultimately the notifying parties must bear the timing risk, as SAMR can eventually resort to blocking the deal if remedy proposals are found ineffective or insufficient.

On the other hand, designing effective remedies for a global semiconductor deal looks to become increasingly challenging. Globally, there is a trend of renewed focus on non-horizontal mergers by competition authorities, such as in the U.S. and EU.[18] In China, the authority's attention to such concerns can be traced back to the early era of AML enforcement.[19] Since SAMR's establishment in 2018, approximately 60 percent of SAMR remedy cases involved vertical or conglomerate concerns (sometimes together with horizontal concerns), and SAMR has been largely resorting to behavioural remedies to resolve potential vertical foreclosure or conglomerate concerns in China. Behavioural remedies can also be employed to solve China-specific concerns in addition to cross-jurisdiction divestitures.[20]

Remedies adopted in recent decisions typically include a combination of: (i) commitment of continued supply to Chinese customers on FRAND terms and maintaining the quality of product/aftersales support; (ii) commitments to ensure interoperability with third-party products; (iii) commitment to not engage in tying/bundling practices; and (iv) commitment to continue R&D investments (in China). While one may argue the effectiveness of behavioural remedies in general, during the past few years, these remedies have been frequently used to mitigate a range of competition concerns and industry issues that are commonly seen in the semiconductor sector.

However, whether such behavioural commitments will continue to work has come more in doubt against the backdrop of tightened export control restrictions, especially the U.S.' upgraded chip bans on China. The upgraded U.S. export control rules released in 2022 cover a wider range of restrictions that limit China's access to advanced computing chips, its ability to develop and maintain supercomputers, and to manufacture advanced semiconductors. It not only covers the chips as well as relevant technology and software, but also includes manufacturing equipment.

It remains unclear whether transacting parties can simultaneously satisfy their supply commitments to SAMR and the U.S. export control requirements, which may be in tension, or even contradiction with each other. Going forward, companies in a similar situation may also have to show that they have the willingness and, most importantly, ability to navigate conflicting regimes to receive the go ahead for their transaction.

IV. CONCLUSION

As the world's largest consumer of semiconductor products, China will inevitably play a key role in the global regulatory processes, and merger control processes in particular. While there is at this time no clear empirical evidence that SAMR's attitudes towards semiconductor or other transactions are changing, uncertainty both in terms of procedure and substance can be expected to increase in light of the New AML.

Semiconductor players or investors should ensure they understand how to manage uncertain review timelines in China, which are likely to manifest in case of complaints or substantive issues. Concerns unrelated to competition also need to be carefully mapped out upfront, particularly those involving any critical inputs, sectors or stakeholders in China, and/or threatening supply to China market in the context of U.S. export controls. These can lead to additional layers of complexity when determining whether a transaction would be notifiable in China, or be deemed problematic by SAMR, in which case the question shifts to whether a commercially acceptable remedy may be found to address China-specific concerns, on top of a globally coordinated remedy package.

---

18 Both the DOJ and FTC had tried to block vertical mergers in 2022 (e.g. the DOJ unsuccessfully attempted to block *UnitedHealth/Change Healthcare* and FTC failed in challenging *Illumina/Grail*, both involving vertical transactions). Both agencies are also reviewing the Vertical Merger Guidelines over the concern that the old guidelines (2020 Vertical Merger Guidelines) overstate the potential efficiencies of vertical mergers. The EC has recently also stepped up its scrutiny of vertical mergers by prohibiting *Illumina/Grail*.

19 China's first prohibition decision against *Coca-Cola/Huiyuan* (2009) identified conglomerate concerns where Coca-Cola was found to have the ability to leverage its market power in the carbonated soft drinks market to enhance its presence in the neighboring juice beverages market.

20 The conditional approval of *Dow/DuPont* (2017) in China is such an example. In addition to the global divesture, the parties also committed to keep supplying certain crop protection products to willing Chinese customers and not to enter exclusive arrangements with Chinese distributors.

A REFLECTION ON CHINA'S AML ENFORCEMENT RE CONCENTRATIONS OF UNDERTAKINGS IN THE INTERNET INDUSTRY

BY ROGER XIN ZHANG[1]

1 Roger Xin Zhang is a researcher of Center for Competition Policy Studies (CCPS), Shandong University. The views expressed herein are the views and opinions solely of the authors and do not reflect or represent the views of CCPS, or any of the organizations with which the author is affiliated.

China's application of competition law in the digital economy in the past three years has attracted attention worldwide. One significant reason is because of the regulation of VIE-structured transactions. For more than 10 years after the implementation of the Anti-Monopoly Law ("AML"), seldom VIE-structured transactions have been reviewed by the competition authority, which means, almost the whole internet industry hasn't made notifications of concentrations and there were no investigations for a decade. The whole thing has been turned around by end of 2020, when the State Administration of Market Regulation ("SAMR") released the Guidelines for Anti-monopoly in the Field of Platform Economy (Draft for Solicitation of Comments)[2] in November and specifically stated that VIE-structured transactions should be notified with SAMR if the thresholds are satisfied[3]. Ever since then, SAMR has officially kicked off the review of the concentration of Internet undertakings, many historical transaction issues have surfaced, and new investments have been imposed with the notification obligation. This article attempts to summarize the characteristics of anti-monopoly law enforcement concerning Internet industry operators in China by reviewing the law enforcement in the past three years and conduct a summary analysis of some of the problems.

China's merger control enforcement under AML in the internet industry faces a lot of challenges. The most obvious obstacle may be the number of historical transactions that need to be dealt with in this sector besides the legal uncertainty of VIE structure. However, the investigation of the historical deals has to some extent helped agencies accumulate experiences with new deals. With the reflection on this topic, more lights could be shed on how to appropriately set "traffic lights"[4] for investments in the future.

I. THE INVESTIGATIONS OF HISTORICAL TRANSACTIONS IN THE INTERNET INDUSTRY

A. Overview of the Investigations

Due to the VIE arrangements and other reasons, a huge number of historical concentrations of undertakings in the internet industry which satisfied the notification thresholds have been implemented without notification with the competition authority. The failure of notification is not an isolated phenomenon, but a common phenomenon in the whole internet industry. Till now, the SAMR has publicized 128 decisions[5] of illegal implementation of concentrations of undertakings in the internet industry since the central government requested to strengthen anti-monopoly law enforcement and prevent the disorderly expansion of capital.[6] Among the 128 decisions, 127 of which are collectively publicized in 7 batches during the past 3 years,[7] while the Tencent Holdings Ltd.'s Acquisition of shares of China Music Corporation case (the CMC case) were announced separately.[8] The 5th batch contains the highest number of decisions so far, which amounts to 43.[9]

2 See https://www.samr.gov.cn/hd/zjdc/202011/t20201109_323234.html (last visited February 8, 2023).

3 See Art 18 of the Guidelines, "The concentration of undertakings involving agreement control (VIE) structure falls within the scope of the anti-monopoly review of the concentration of undertakings. Where the concentration of business operators meets the declaration standards stipulated by the State Council, the business operators shall report to the anti-monopoly law enforcement agency of the State Council in advance, and shall not implement the concentration without declaration."

4 "traffic lights" is a metaphorical term introduced by Central Economic Work Conference 2021 that direct the regulation on investments and financial activities. See http://www.news.cn/politics/2021-12/13/c_1128159713.htm (last visited February 8, 2023).

5 See "Administrative Penalty Cases" Colum on the official website of the 2nd Bureau of Antimonopoly Enforcement of SAMR, https://www.samr.gov.cn/fldes/tzgg/xzcf (last visited February 8, 2023).

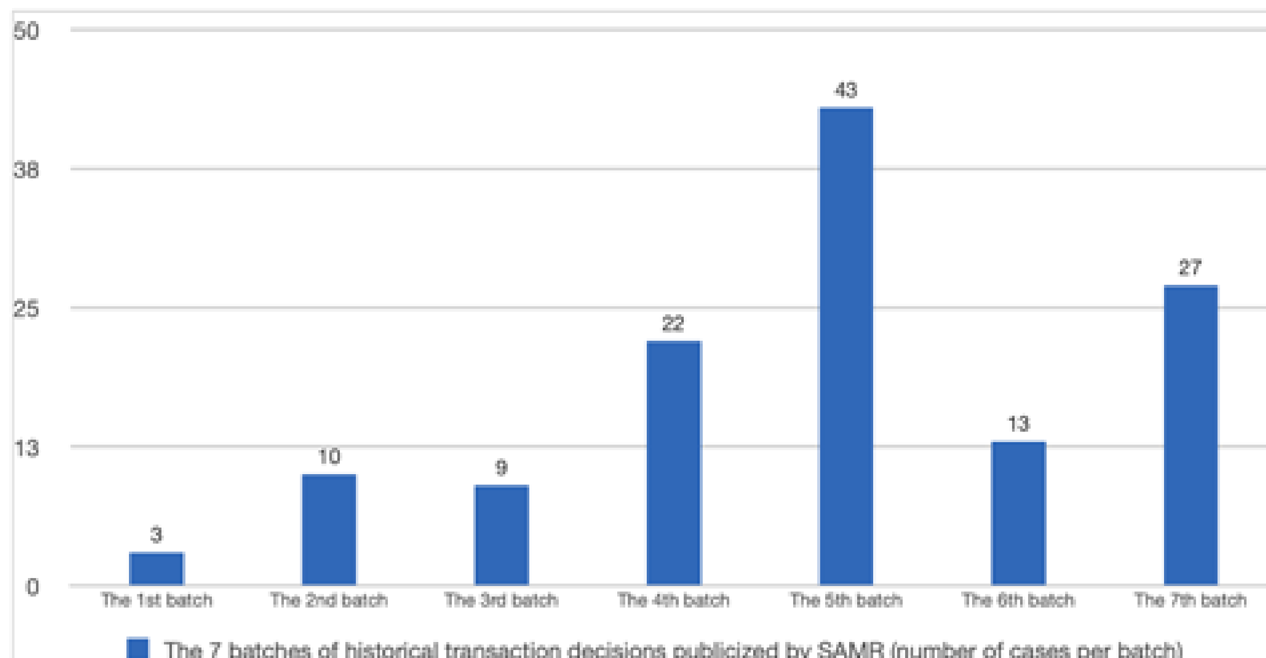
6 See "Interpreting the Spirit of the Central Economic Work Conference: Preventing Disorderly Expansion of Capital," on the Chinese government website, http://www.gov.cn/xinwen/2020-12/27/content_5573663.htm (last visited February 8, 2023).

7 See separately:
The 1st batch, the official website of SAMR, https://www.smar.gov.cn/xw/zj/202012/t20201214_324335.html (last visited February 8, 2023);
The 2nd batch, the official website of SAMR, https://www.samr.gov.cn/xw/zj/202103/t20210312_326737.html (last visited February 8, 2023);
The 3rd batch, the official website of SAMR, https://www.samr.gov.cn/xw/zj/202104/t20210430_328470.html (last visited February 8, 2023);
The 4th batch, the official website of SAMR, https://www.samr.gov.cn/xw/zj/202107/t202107_332396.html (last visited February 8, 2023);
The 5th batch, the official website of SAMR, https://www.samr.gov.cn/xw/zj/202111/t20211119_337049.html (last visited February 8, 2023);
The 6th batch, the official website of the 2nd Bureau of Antimonopoly Enforcement of SAMR, https://www.samr.gov.cn/fldes/tzgg/xzcf/ (last visited February 8, 2023);
The 7th batch, the official website of the 2nd Bureau of Antimonopoly Enforcement of SAMR, https://www.samr.gov.cn/fldes/tzgg/xzcf/202207/t20220710_348523.html (last visited February 8, 2023).

8 See the official website of the 2nd Bureau of Antimonopoly Enforcement of SAMR, https://www.samr.gov.cn/fldes/tzgg/xzcf/202204/t202204_341604.html (last visited February 8, 2023).

9 See the official website of SAMR, https://www.samr.gov.cn/xw/zj/202111/t20211119_337049.html (last visited February 8, 2023).

Figure1: The 7 batches of historical transaction decisions publicized by SAMR (number of cases per batch)



Most of the investigations show that the failures of notification of concentrations in the internet industry have no impact of restricting and eliminating competition. Among the 128 publicized cases, 127 of which were found of procedural violations of the AML and were imposed with the maximum fine of CNY 500, 000. If you compare the decisions on the failure of notification in other industries in the past, you may find that fines below CNY 500, 000 were imposed on many of the cases. The maximum fine to some extent emphasized the determination of the competition authority to solve the historical transaction issues in the internet industry. According to SAMR, these concentrations have no competition concern and the internet undertakings only gain joint control via minority shareholdings acquisitions for most of the times while the founding shareholders and others often still hold a large percentage of the shares and voting rights.

The merger control in the internet industry exposed the problem of insufficient law enforcement personnel of SAMR and to some extent may lead to the establishment of the National Antimonopoly Bureau ("NAB"). The 128 cases were just a small part of the work for SAMR since every single transaction that happened in the past 12 years in the whole sector has to be analyzed to see if there is a change of control and if the notification thresholds are met. That means tens of thousands of documents need to be run through by the agency. The workload is significant for SAMR to finish within no more than 3 years. Therefore, the enforcement of AML in the internet industry and the objective lack of enforcement capability may be one of the reasons for the expansion of the headcounts of the Anti-Monopoly Bureau afterward. It is partially true that the internet AML investigations have contributed to the establishment of NAB on Nov 18, 2021.[10] A division, particularly for review of concentration in the digital economy area, was founded in the 2nd Antimonopoly Enforcement Bureau.

The CMC case was the only conditional approved historical transaction, and SAMR initiated an administrative investigation procedure that lasted for 180 days.[11] This case is of special significance because no historical transactions were imposed with conditions before. The competition concern of the CMC case was the high market share possessed by the merging parties in China's online music-playing platform market post-transaction (the combined market share of the post-concentration entity exceeds 70 percent in terms of monthly user hours, sales amount, and the share of core music copyright resources), which contributes to a strong unilateral effect. SAMR believed that the unilateral effect was mainly because of the exclusive copyright licensing arrangements and the competition will be restored by breaking the exclusive licensing of upstream copyrights. Therefore, the transaction was imposed with conditions besides the monetary fine of CNY 500, 000. The internet industry is characterized by dynamic competition and cross-border competition, it is also possible that some short video platforms with a broad user base will become competitors in the relevant market with the merging parties in the future after obtaining sufficient music copyrights.

10 See "The National Anti-Monopoly Bureau Officially Launched," the official website of SAMR, https://www.samr.gov.cn/xw/zj/202111/t20211118_336974.html (last visited February 8, 2023).

11 SAMR opened the case for investigation on January 25, 2021 and publicized the decision on July 24, 2021. See https://www.samr.gov.cn/xw/zj/202107/t20210724_333016.html (last visited February 8, 2023).

B. The Legal Uncertainties of the Investigations

The reason for the huge number of failures of notifications of concentrations of historical transactions in the internet industry in the past decade is that the VIE structure involves multiple unclear policy issues of various regulatory areas, resulting in vague notification standards in practice. On the one hand, the VIE structure is suspected of bypassing the regulation of foreign investment and telecom value-added services which makes the legality of VIE structure questionable. When a transaction involving VIE structure is submitted to the competition authority, it is therefore difficult for the agency to clarify whether VIE structure-related transactions should be accepted under normal filing procedures. The objective challenges remained unsolved for a long time because different regulators hadn't reached a consensus. On the other hand, most undertakings in the internet industry chose not to make filings with the competition authority for transactions involving VIE structure based on their assessments of the regulatory environment and their own legal risks at the time of the transaction and the AML enforcement agencies didn't actively intervene in these transactions. Under law enforcement agencies' principle of prudential tolerance, undertakings in the internet industry have gradually formed a common concept that they will not notify investment transactions involving VIE structures with the competition authority. However, when the principle of prudential tolerance changed and the competition authority started to investigate the historical transactions involving VIE structures that were not notified in accordance with the law, many challenges followed. The most critical one is, how should law enforcement agencies deal with these long-standing and numerous historical transactions.

At least two legal concepts need further interpretations for solving historical transaction issues. The first one is the concept of "implementation." According to Article 26 of the AML (Art. 21 of the old law), "without notification, the concentration shall not be implemented,"[12] of which "implementation" has always been a vague concept and it needs to be considered with the second legal concept. The second one would be how to interpret the 2-year limitation of administrative enforcement for administrative penalties. Article 36 of China's Administrative Penalty Law states that" where an illegal act is not discovered within 2 years of its commission, administrative penalty shall no longer be imposed." and "if the act is of a continual or continuous nature, it shall be counted from the date the act is terminated."[13] Therefore, comes the question, for historical transactions, what should be considered to be the starting date for this calculation? The day the transaction was closed (such as the equity transfer settlement or registration and establishment of Joint Ventures) which means the close of the transaction is considered as the act of "implementation"? Or the day when the post-transaction entity (the company) ceases to exist, which means the operation of the company should be seen as a continuous act of "implementation"? If the completion of the transaction itself were to be taken as the point of time for the implementation of the concentration, many historical transactions should no longer be investigated by law enforcement agencies because their "violations" are not continuous acts that exceeded the 2-year time limit; If the post-transaction status is considered as the "continuous" state for implementation of the concentration, the continuing act of "violation" remains intact as long as the company has not deregistered or liquidated, which makes the vast majority of historical transactions subject to SAMR's retroactive investigations.

Due to the ambiguity of these two legal concepts, there is a lot of room for interpretation in practice. Therefore, it is reasonable to say that handling historical transaction issues could be at SAMR's discretion. Different approaches adopted by the agency may have totally different impacts on the market economy. To some extent, the competition authority is seeking a balance between regulating the concentration of undertakings and encouraging market investment by dealing with historical transactions in the internet industry. Anti-Monopoly Law provides a perspective to solve this problem. The purpose of the law is to prevent and restrain monopolistic conducts[14]. However, the monopolistic conducts listed in Article 3 only includes "concentration of undertakings that eliminates or restricts competition or might be eliminating or restricting competition"[15], which means concentrations without competition concerns could be excluded from the list. Therefore, for transactions that has no effect of eliminating or restricting competition, the competition authority could consider that the illegal act of "implementation" was

12 See Article 26 of Anti-Monopoly Law: "Any concentration that falls under the notification criteria issued by the State Council must be notified in advance with the State Council antimonopoly authorities. Without notification the concentration shall not be implemented. Where the concentration of undertakings does not meet the notification criteria but there is evidence showing that the concentration of undertakings has or may have the effect of eliminating or restricting competition, the State Council antimonopoly authorities can require the undertakings to notify. If the undertakings do not notify as prescribed by the preceding two paragraphs, the State Council antimonopoly authorities shall conduct an investigation according to law."

13 See Article 36 of Administrative Penalty Law: "Where an illegal act is not discovered within 2 years of its commission, administrative penalty shall no longer be imposed; If the lives, health, and financial security of citizens are involved and there are harmful consequences, the above-mentioned period shall be extended to 5 years. except as otherwise prescribed by law. The period of time prescribed in the preceding paragraph shall be counted from the date the illegal act is committed; if the act is of a continual or continuous nature, it shall be counted from the date the act is terminated."

14 See Article 1 of Anti-Monopoly Law: "This Law is enacted for the purposes of preventing and repressing monopolistic conduct, protecting fair market competition, encouraging innovation, enhancing economic efficiency, maintaining the interests of consumers and public interest, and promoting the sound development of socialist market economy."

15 See Article 3 of Anti-Monopoly Law:"For the purposes of this Law, "monopolistic conduct" includes:
(1) a monopoly agreement reached by undertakings;
(2) an undertaking's abuse of its dominant market position; and
(3) a concentration of undertakings that has or may have an effect of precluding or restricting competition."

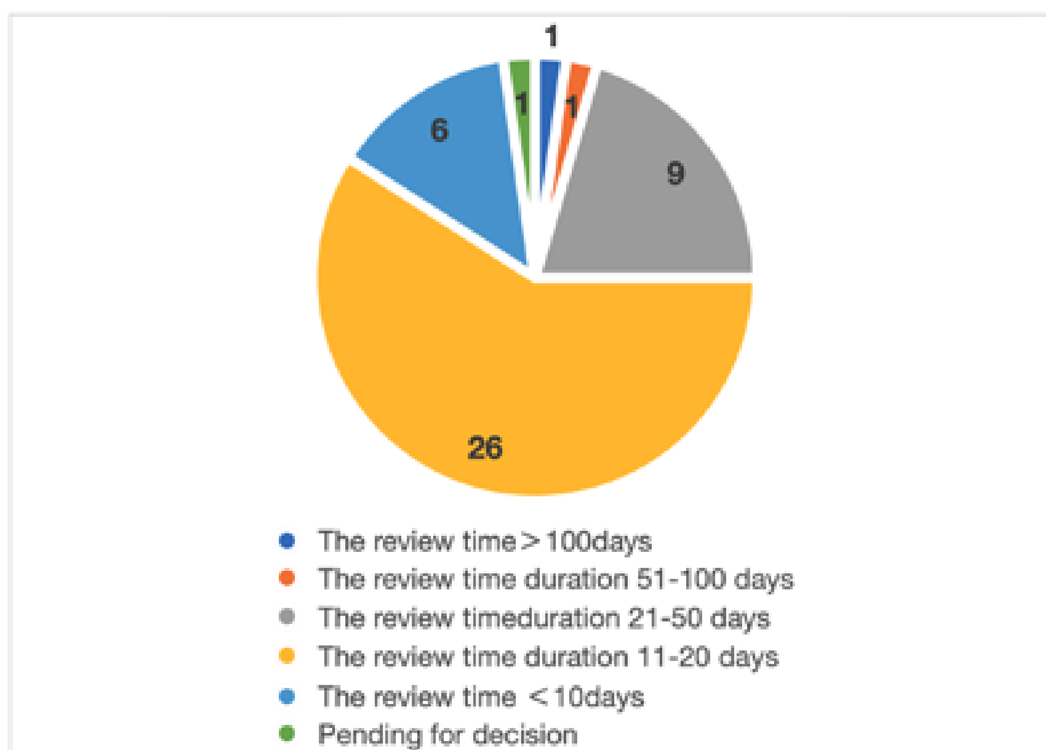
terminated when the transaction was closed; while for transactions that have the impact of exclusion or restriction of competition, the continuous state of "implementation" could be considered terminated when the negative impact on competition disappeared. As the Chinese old saying goes, "ingenuity in varying tactics depends on mother wit"[16], we have no doubt that the historical transactions will be properly handled by the joint endeavor of the regulator agencies and the market players.

II. THE REVIEW OF NEW INVESTMENTS IN THE INTERNET INDUSTRY

A. Overview of the new filings

With the clarification of notification obligation for transactions that satisfied the thresholds, undertakings in the internet industry have gradually strengthened their compliance and notified their new investments with SAMR in accordance with the law. According to statistics, for the new filings in the internet industry, there are only 8 transactions reviewed with standard procedure[17]; While more transactions were reviewed under the simplified procedure, the number of which amounts to 44.[18] It is fair to say that there is no difference between concentration of undertakings in the internet industry and the mergers in other sectors in terms of review. We have statistics on the review time of simple cases in new transactions which shows that the longest review time reaches 118 days, and the average review time is about 21 days.[19]

Figure 2: The review time for simplified cases in the internet industry



16 See The History of Song Dynasty · Biography of Yuefei: "Fight after formation is the art of war, ingenuity in varying tactics depends on mother wit."

17 See "the publicity of unconditional approval of concentrations of undertakings," the official website of the 2nd Bureau of Antimonopoly Enforcement of SAMR, https://www.samr.gov.cn/fldes/ajgs/wtjjz/ (last visited February 8, 2023); and "the announcement of Prohibiting the Anti-monopoly Review Decision on the Merger of Huya Company and Douyu International Holdings Co., Ltd. by SAMR," the official website of the 2nd Bureau of Antimonopoly Enforcement of SAMR, https://www.samr.gov.cn/fldes/tzgg/ftj/202204/t20220424_342158.html (last visited February 8, 2023).

18 See "the publicity of simplified cases," the official website of the 2nd Bureau of Antimonopoly Enforcement of SAMR, https://www.samr.gov.cn/fldes/ajgs/jyaj/ (last visited February 8, 2023).

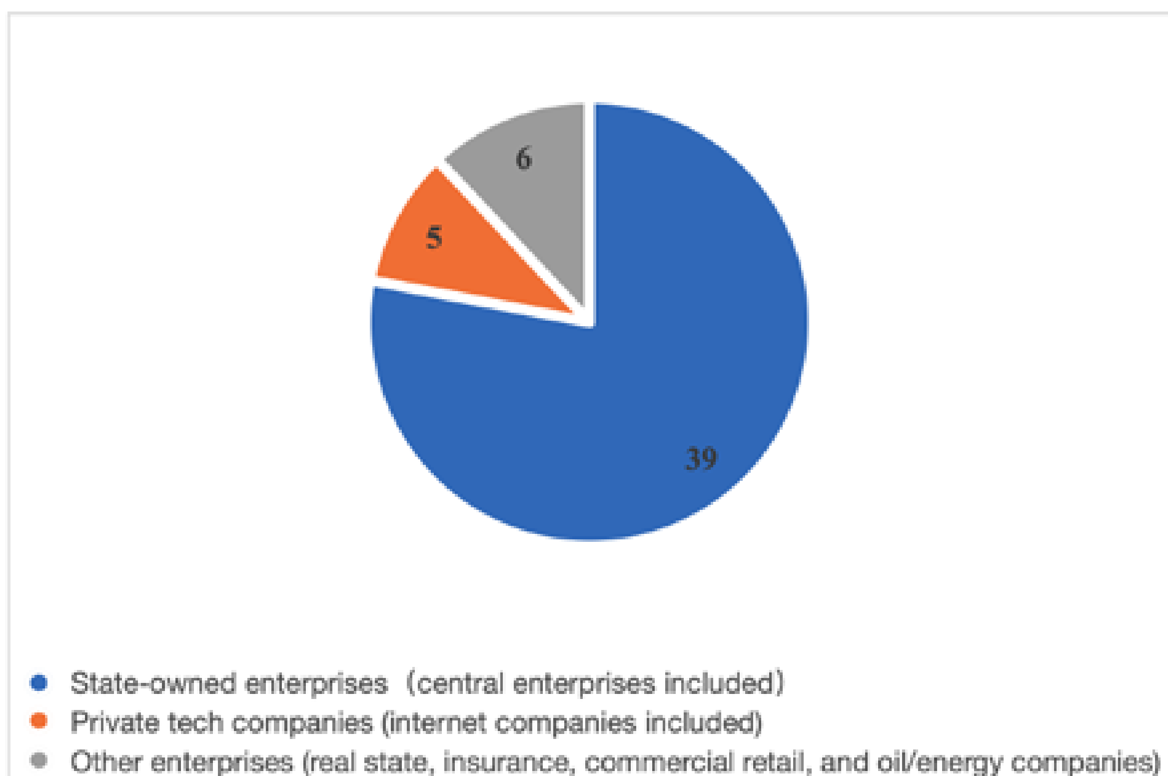
19 See "the publicity of simplified cases," the official website of the 2nd Bureau of Antimonopoly Enforcement of SAMR, https://www.samr.gov.cn/fldes/ajgs/jyaj/ (last visited February 8, 2023); and the publicity of unconditional approval of concentrations of undertakings," the official website of the 2nd Bureau of Antimonopoly Enforcement of SAMR, https://www.samr.gov.cn/fldes/ajgs/wtjjz/ (last visited February 8, 2023).

Although the review time of concentrations of undertakings in the internet industry is no longer than that of other sectors, due to the highly dynamic nature of the internet industry, there are still high expectations for the improvement of review efficiency. Excessive review time may delay investment transactions on Internet platforms, which is not conducive to stimulating market vitality and improving economic efficiency.

B. The Proposed Thresholds Based on Market Value or Valuation

Provisions of the State Council on Thresholds for Prior Notification of Concentrations of Undertakings (Draft form comments) released last year[20] has proposed to adopt market value or valuation as the notification threshold in addition to the annual revenue standard.[21] The newly introduced market value and valuation standards in the draft regulation lack a clear calculation standard and are vague, which may bring a large number of investments and mergers and acquisitions into the scope of notification, and are not conducive to encouraging investment innovation. According to statistics, most of the Chinese enterprises with an annual turnover of more than CNY 100 billion in 2021 are State-Owned Enterprises (including central SOEs), and among the qualified private enterprises, the proportion of technology enterprises (including Internet enterprises) is relatively high (see the following chart).[22] The new standards will inevitably encounter many uncertainties in the future implementation, including the calculation methodology, the calculation time period, and even the possibility of using other ways to evade this standard. We look forward to the final notification standards that can be refined and optimized with the enforcement practice to better meet market and investment needs.

Figure 3: The top 50 types of enterprises with a turnover of more than CNY 100 billion in 2021 SOE



20 See https://www.samr.gov.cn/jzxts/tzgg/zqyj/202206/t20220625_348150.html (last visited February 8, 2023).

21 See Article 4 of the State Council on Thresholds for Prior Notification of Concentrations of Undertakings (Draft form comments):
Undertakings that do not meet the notification thresholds specified in Article 3 of this Regulation but meet the following conditions shall, prior to implementation of concentration, notify with the Anti-Monopoly enforcement authority of the State Council:
(1) the turnover of one of the undertakings participating in the concentration in the last accounting year in China is more than CNY 100 billion;
(2) the market value (or valuation) of the other undertakings specified in Item (1) of Paragraph (1) or Items (2) and (3) of Paragraph (2) of Article 2 of this Regulation is not less than CNY 800 million, and the turnover of the undertaking in China in the last accounting year accounts for more than one-third of its turnover globally.

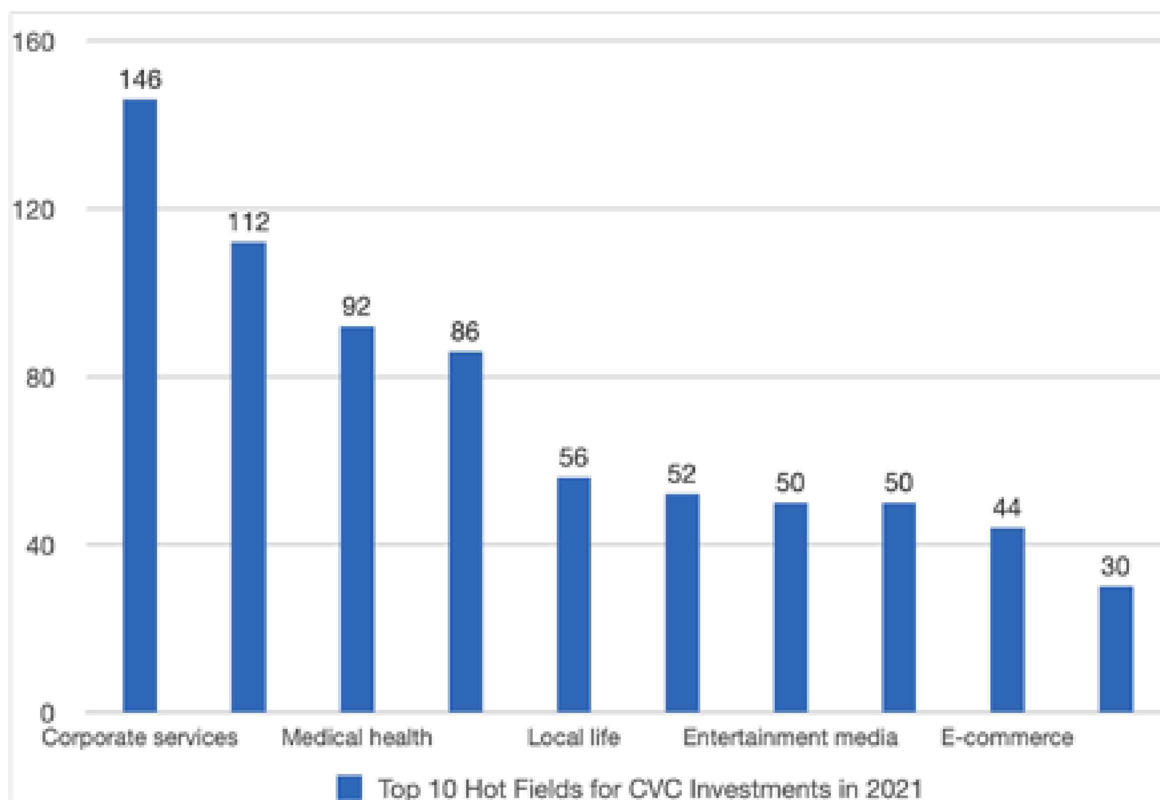
22 See "2021 Top 500 Chinese Enterprises," https://finance.sina.com.cn/china/2021-09-25/doc-iktzscyx6201643.shtml (last visited February 8, 2023).

C. On Optimizing the Regulation of Concentrations in the Internet Industry

The necessity of optimizing the AML merger review system for undertakings in the internet industry

General Secretary Xi Jinping pointed out that we need to continuously strengthen, optimize and expand our digital economy and set up "traffic lights" for capital. The AML merger review system is an important tool to play the role of the "traffic lights" to regulate and guide the healthy development of capital and promote the healthy and sustained development of the digital economy in accordance with the law. The Internet industry is characterized by strong dynamics and fleeting transaction opportunities, so its system of merger review also needs to cater to the industry characteristics to introduce a set of rapid and efficient mechanisms to promote investment and mergers and acquisitions ("M&A") and improve economic efficiency. Investment and M&A in the Internet industry are the main force of CVC (corporate venture investment) in China. According to itjuzi.com, as of August 31, 2021, the total number of investment events of Internet companies accounted for 58 percent of the total CVC investment in China.[23] Compared with PE/VE, CVC usually plays a more patient role in the target company, which means they can accompany enterprises to grow for a long time. This is of significant importance for startups to obtain financing support and sustainable development. In particular, it is worth noting that CVC investment is mostly related to industries with national strategic significance. According to itjuzi.com, the industry with the most CVC investment events in 2021 was corporate services (146 events), advanced manufacturing (112 events) and medical health (92 events) (details in the following chart).[24] This is of great significance for empowering the real economy, promoting digital transformation, strengthening technological innovation and tackling core technologies in key fields, and is conducive to the country's strategic experiments. Therefore, it is urgently necessary to further optimize the concentration regulation mode of the internet industry.

Figure 4: Top 10 Hot Fields for CVC Investments in 2021



D. The Principles for the Optimization

It is necessary to adhere to the principles of equal regulation, professional regulation and collaborative regulation in optimizing the management of Internet industry operators. Firstly, the principle of equal regulation should be adhered to, and the same level of supervision should be given to different industries without discrimination. Secondly, the principle of professional regulation should be adhered to. On the one hand, we should

23 See "2021 China CVC Investment and M&A Report," https://cdn.itjuzi.com/pdf/b3bdf9b55cac58721d39cee2f106e632.pdf (last visited February 8, 2023).

24 *Ibid.*

strengthen the professional training of anti-monopoly enforcement teams, and establish a mechanism for more antitrust experts to involve in the training sessions and even the enforcement of the law; On the other hand, we should actively recruit talents with the professional antitrust background to join the anti-monopoly enforcement agencies and expand the regulation team staffing appropriately. Thirdly, the principle of collaborative regulation should be adhered to, and an "anti-monopoly community" should be built to facilitate the exchange and cooperation mechanism between anti-monopoly enforcement agencies, judicial branches, corporate compliance departments, research institutions of universities and law firms, which can contribute to deepen consensus, cultivate competition culture. These are conducive to the harmony of administrative enforcement and litigation, the coordination of compliance and regulation, and the mutual promotion of theory study and practice.

Optimizing the regulation of the concentration of undertakings in the internet industry: Improving the categorization and classification review system

Article 37 of the revised Anti-Monopoly Law states: "The anti-monopoly enforcement agency of the State Council shall establish a categorization and classification system for concentration of undertakings, strengthen the review of concentration of undertakings in key fields that concern national economy and people's livelihood, and improve the quality and efficiency of the review."[25] The establishment of a categorization and classification review system for concentration of undertakings is conducive to setting the "traffic lights" for the investment and M&A of Internet platforms, which can provide more guidance for future investments.

Firstly, with reference to the negative list, it is necessary to clarify the "red light" areas and make it clear that all areas outside the "red light" areas can be invested. By dynamically updating the "Internet Market Access Prohibited License Catalog" and other laws and regulations, setting "red lights" for a few sensitive areas that may affect national security and stability, public opinion, and social mobilization capabilities, so that market players can clearly define the boundaries of prohibition. Outside the "red light" field, we should uphold the principle of "everything which is not forbidden is allowed" to improve the expectations of market players and boost development confidence.

Secondly, it is necessary to launch the "green light" cases as soon as possible and clarify the supporting measures to these cases to encourage investment. The report on the development of the digital economy made by Mr. He Lifeng, director of the National Development and Reform Commission, to the National People's Congress pointed out that it is necessary to support and guide the healthy and sustainable development of the platform economy, and to launch a batch of "green light" investment cases[26]. The key to launching "green light" cases lies in the timely introduction of incentives and support for this field of investment and M&A. In terms of concentration of undertakings, a fast review mechanism can be set up for the investment and M&A in the "green light" field to shorten the review time period, so as to enable these investments and M&As that are conducive to building new national competitive advantages to be implemented more quickly.

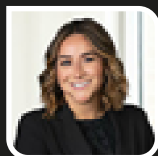
Finally, it is necessary to reduce the "gray area" between “red and green light” areas as much as possible to prevent the stagnation of investment and M&A. Under the situation of normalized supervision, enterprises may reduce investment and M&As in the "gray area" to avoid possible policy risks. If the scope of the "gray area" is too large, it may cause the scope of the enterprises' "fear of investing" to expand, which may lead to problems such as difficulty in financing for small and medium-sized enterprises, decline in market vitality, and reduction of economic efficiency.

25 See Article 37 of Anti-Monopoly Law.

26 See https://www.ndrc.gov.cn/fzggw/wld/hlf/lddt/202211/t20221116_1341446.html (last visited February 8, 2023).

THE NOT-SO-SILK ROAD: THE PROLIFERATING REGULATORY OBSTACLES TO CHINESE INVESTMENT IN THE U.S.

BY DAVID PEARL & BELLA SOLÓRZANO[1]



1 David is a Counsel in Axinn, Veltrop & Harkrider's Washington DC office and former Executive Secretary at the Department of the Treasury during the Obama Administration. Bella is an associate in Axinn's San Francisco office.

I. INTRODUCTION

Competition Policy International's audience is no doubt very familiar with the arduous path to closing long faced by deals that attract significant antitrust scrutiny. And competition authorities have gotten more aggressive of late, including in the United States, where both the Department of Justice ("DOJ") and the Federal Trade Commission ("FTC") have over the last several years employed a variety of tools that have the cumulative effect of making the U.S. merger review process even more onerous. The FTC has made a number of procedural changes, including suspending the granting of early termination of the Hart Scott Rodino ("HSR") waiting period for unproblematic deals, issuing "close at your own peril" letters to merging parties even after the expiration of the waiting period, and reviving a policy of including a provision in its settlements with merging parties that requires the parties to obtain prior FTC approval of future deals in the affected market for a ten-year period. The DOJ has enunciated a policy of deep skepticism of merger remedies, with Assistant Attorney General Jonathan Kanter expressing the view "that merger remedies short of blocking a transaction too often miss the mark."[2] And further changes are on the way, with the DOJ and FTC having jointly withdrawn the horizontal and vertical merger guidelines.

These changes at the DOJ and FTC have created additional speed bumps for all merging parties without regard to their national origin. But foreign acquirers, particularly Chinese acquirers, face yet another major, regulatory obstacle to getting deals done in the United States: the Committee on Foreign Investment in the United States, or CFIUS.

CFIUS is a U.S. interagency body that assesses the risk to national security of transactions involving non-U.S. acquirers. In so doing, CFIUS evaluates the ability and intention of the acquirer to harm national security (the threat), the degree to which the target U.S. business is susceptible to exploitation by the acquirer (the vulnerability), and the reasonably foreseeable impact on U.S. national security (the consequence).[3] If CFIUS finds that a given transaction poses a risk to national security, it can work with the parties to mitigate that risk or recommend to the President of the United States that the transaction be blocked. CFIUS has recently been granted an even more muscular set of powers and a broader jurisdiction that is bound to sweep in more transactions. And while CFIUS applies to all non-U.S. acquirers, acquirers with Chinese ties have drawn disproportionate interest, particularly as the United States and China have been fighting a slow burn trade war over the last several years.

This article first provides some basic background on CFIUS and takes a look at its recent enhancements. It then reviews past CFIUS actions that have affected companies with ties to China and details recent and potential future legislation and executive action that may further affect Chinese M&A activity in the United States (and vice versa). Finally, we offer some guidance for navigating the combined competition and national security merger review gauntlet.

II. A BRIEF HISTORY OF CFIUS

Though the United States generally has an "open door" policy toward foreign investment, CFIUS has seen its jurisdiction and powers to block foreign investment expand over time. In general, this has been in response to public concern about a particular country or countries obtaining influence over United States policy through ownership of U.S. assets.[4] CFIUS is chaired by the Secretary of the Treasury and was established by President Gerald Ford via executive order in 1975[5] in response to concerns about increased investment in the United States from OPEC nations.[6]

2 Assistant Attorney General Jonathan Kanter of the Antitrust Division Delivers Remarks to the New York State Bar Association Antitrust Section (Jan. 24, 2022), https://www.justice.gov/opa/speech/assistant-attorney-general-jonathan-kanter-antitrust-division-delivers-remarks-new-york. The DOJ has not entered into any settlements to resolve concerns about a merger since this speech. See *DAMITT 2022 Annual Report: Timing and Remedy Risks Grow for Transactions Hit with Significant Investigations,* Dechert (Jan. 23, 2023), https://www.dechert.com/knowledge/publication/2023/1/damitt-2022-annual-report--timing-and-remedy-risks-grow-for-tran.html.

3 31 C.F.R. § 800.102.

4 See generally Cathleen D. Cimino-Isaacs, The Committee on Foreign Investment in the United States (CFIUS), Congressional Research Service (Updated Feb. 14, 2020), https://crsreports.congress.gov/product/pdf/RL/RL33388.

5 Exec. Order No. 11858, 3 C.F.R. § 990, (1971-1975).

6 Testimony of C. Fred Bergsten, Assistant Secretary for International Affairs, U.S. Department of the Treasury, 96th Cong., Hearings: The Operations of Federal Agencies in Monitoring, Reporting on, and Analyzing Foreign Investments in the United States (July 30, 1979).

Initially, CFIUS did not have any authority to stop or alter an individual transaction. In fact, it faced accusations of not doing much of anything in its first several years of existence.[7] This changed in 1988. A trade dispute with Japan prompted Congressional concern about the acquisition of U.S. technology companies by Japanese companies.[8] Worried that such acquisitions could harm national security, Congress passed the "Exon-Florio" amendment to Section 721 of the Defense Production Act ("DPA"). This new law granted the President authority to "suspend or prohibit any acquisition, merger, or takeover," by a "foreign person" that the President determined was likely to "threaten to impair the national security."[9] It prescribed a timeline for the President's review — 30 days to assess whether an investigation is warranted, 45 days to complete that investigation, and 15 days for the President to review and announce a decision, for a maximum total of 90 days.[10] President Ronald Reagan delegated this new authority to CFIUS.[11]

The next major revision of CFIUS' authority came after it reviewed but decided not to block a high-profile transaction. In 2006, Dubai Ports World, a state-owned company based in the United Arab Emirates, proposed to acquire contracts to manage a number of major U.S. ports. Lingering post-911 anxiety about the security of U.S. ports sparked public and congressional outcry. The deal was not ultimately consummated, and Congress passed the Foreign Investment and National Security Act of 2007 ("FINSA").[12] FINSA made a number of changes that together served to elevate the attention paid to CFIUS both within the executive branch and from Congress. FINSA for the first time enshrined CFIUS in statute,[13] added additional Cabinet-level members,[14] required the designation of a lead agency for every transaction,[15] and mandated enhanced reporting to Congress.[16] In addition, FINSA added factors for the President to consider in evaluating transactions and standards to guide CFIUS when entering into agreements with parties to mitigate national security threats.[17]

During the 2016 U.S. Presidential campaign, Donald Trump made clear that he would take an aggressive stance against China.[18] After taking office, President Trump initiated a trade war with China in 2018. His administration undertook a number of actions, including imposing a litany of tariffs and pursuing dispute settlement in the World Trade Organization concerning China's "discriminatory licensing practices." President Trump also directed the Treasury Department to propose executive action to "address concerns about investment in the United States directed or facilitated by China in industries or technologies deemed important to the United States."[19] Congress had been working in parallel to update CFIUS' powers since late 2017. In August 2018, Congress passed the Foreign Investment Risk Review Modernization Act of 2018 ("FIRRMA").[20] FIRRMA, among other things, (i) expanded the jurisdiction of CFIUS to cover additional transaction types, (ii) introduced mandatory filing requirements, (iii) added a short-form expedited filing option, and (iv) substantially increased CFIUS' resources to enable enhanced monitoring.

7 See Testimony of William S. Barnes, PhD, Fletcher School of Law and Diplomacy, Tufts University, 96th Cong., Hearings The Operations of Federal Agencies in Monitoring, Reporting on, and Analyzing Foreign Investments in the United States (July 30, 1979).

8 David Sanger, *Japanese Purchase of Chip Maker Canceled After Objections in U.S.*, N.Y. Times (Mar. 17, 1987), https://www.nytimes.com/1987/03/17/business/japanese-purchase-of-chip-maker-canceled-after-objections-in-us.html.

9 Pub. L. 100-418, Title V, Section 5021, August 23, 1988, available at https://www.congress.gov/100/statute/STATUTE-102/STATUTE-102-Pg1107.pdf.

10 *Id.*

11 Exec Order 12661, s. 3-201, amending Exec. Order 11858, https://www.archives.gov/federal-register/codification/executive-order/12661.html.

12 Foreign Investment and National Security Act of 2007, 121 Stat. 246.

13 FINSA § 3.

14 *Id.*

15 *Id.*

16 *Id.* at § 7.

17 *Id.* at § 5.

18 See e.g. Nick Corasantini, *Donald Trump Vows to Rip Up Trade Deals and Confront China*, N.Y. Times (June 28, 2016), https://www.nytimes.com/2016/06/29/us/politics/donald-trump-trade-speech.html.

19 Memorandum on Actions by the United States Related to the Section 301 Investigation of China's Laws, Policies, Practices, or Actions Related to Technology Transfer, Intellectual Property, and Innovation (March 22, 2018), available at https://www.govinfo.gov/content/pkg/DCPD-201800180/pdf/DCPD-201800180.pdf. See also Chad P. Bown and Melina Kolb, *Trump's Trade War Timeline: An Up-to-Date Guide*, The Peterson Institute (Nov. 17, 2022), https://www.piie.com/sites/default/files/documents/trump-trade-war-timeline.pdf.

20 H.R. Con. Res. 5515-538.

III. HOW CFIUS REVIEW WORKS UNDER FIRRMA

A. Covered Transactions

FIRRMA and its implementing regulations grant CFIUS jurisdiction to review "any covered transaction,"[21] which includes a:

- "covered control transaction," which is a transaction that could result in foreign control of a U.S. business.[22]
- "covered investment," a non-controlling investment in certain U.S. businesses of special concern known as "TID" businesses.[23] TID refers to businesses that involve specified "critical Technologies" or "critical Infrastructure," or that collect or maintain "sensitive personal Data" of U.S. citizens.[24]
- any changes in rights that could result in a covered control transaction or a covered investment or any transactions designed to avoid CFIUS jurisdiction.[25]

CFIUS also has jurisdiction over "covered real estate transactions," which involve the acquisition of certain rights in property in close proximity to ports and military installations.[26]

In its latest Annual Report to Congress, CFIUS indicated that in 2021, it determined that 272 notices filed involved "covered transactions."[27] This is more than double the number from ten years ago and the highest number in the ten-year period examined in the report.[28] Of those, CFIUS investigated 130, or around 48 percent.[29]

B. Timing

The statutory timeline for CFIUS review was adjusted slightly by FIRRMA: the 30-day initial review period was extended to 45 days, but the time for an investigation (45 days) and for the President to decide whether to block a transaction (15 days) remain the same. There are a number of ways that CFIUS review can take longer than that basic 105-day timeline:

- Parties can choose to engage informally with CFIUS prior to filing, such as through presentations or submissions of draft versions of filings;
- CFIUS can reject the parties' filing for a variety of reasons, meaning that the initial review period does not commence until the parties cure whatever shortcoming led to the rejection;
- The parties may withdraw their filing and re-file at a later date, which re-starts the initial review period clock; or
- CFIUS can seek a one-time 15-day extension of the 45-day investigation period due to "extraordinary circumstances" such as a force majeure-level event;[30]

Parties have the option to file a short-form declaration that carries with it a 30-day review period instead of the 45-day review period for a formal notice.[31] In the case of a transaction that CFIUS is not likely to perceive as a national security threat, a declaration can be a quick route to obtaining certainty that CFIUS review will not hold up the closing. But CFIUS can also request that a party who filed a declaration file a subsequent

---

21 31 C.F.R. § 800.101.

22 *Id.* at § 800.210.

23 31 C.F.R. § 800.211.

24 *Id.* at § 800.248.

25 *Id.* at § 800.213.

26 Id. at § 802.101; 802.211; and 802.212.

27 CY 2021 CFIUS Annual Report. to Congress (Aug. 2022) at 15 ("2021 CFIUS Annual Report"), https://home.treasury.gov/system/files/206/CFIUS-Public-AnnualReporttoCongressCY2021.pdf.

28 *Id.*

29 *Id.*

30 31 C.F.R. § 800.508(e)-(f).

31 31 C.F.R. § 800.405.

notice, in which case the declaration serves only to prolong the review period. In 2021, this happened about 18 percent of the time.[32] As such, parties who believe a notice is likely to be required may prefer to go straight to the formal notice rather than filing a declaration.

C. Mandatory Filings and CFIUS' Call-in Powers

Most CFIUS filings are voluntary, but a filing is mandatory if a transaction would result in either: (i) a foreign government actor having a substantial interest in any type of TID business or (ii) foreign control of or a covered investment in a TID business that involves critical technologies subject to export control laws.[33] Of the 164 declarations filed in 2021, CFIUS concluded that 47 were mandatory filings.[34]

CFIUS also has the power to "call in" transactions for which parties did not submit a voluntary notice to CFIUS.[35] This power is not new, but FIRRMA gave CFIUS substantial additional resources to enable it to exercise this power with more frequency.[36] In 2021, CFIUS called in 135 transactions identified through this process and requested a filing from eight of them.[37]

D. National Security Concerns, Mitigation, and Penalties

Section 721(f) of the DPA articulates ten factors for CFIUS to consider and gives the President the authority to articulate others.[38] In September 2022, President Biden issued an executive order on CFIUS.[39] The executive order elaborated on two statutory factors: supply chain resilience 721(f)(3)) and U.S. "international technological leadership" (721(f)(5).[40] It also added three additional factors: "aggregate industry investment trends," cybersecurity risks, and sensitive data.[41] These five factors to some extent formalize CFIUS' existing practices, but their enumeration in an executive order is a strong signal that they will remain a focus of CFIUS going forward.

Where a transaction poses national security risk, Section 721(l) of the DPA grants CFIUS the authority to (i) temporarily prohibit the transaction from closing during the pendency of its review; (ii) make a recommendation to the President to permanently block the transaction; or (iii) negotiate mitigations that will resolve its national security concern.[42] CFIUS has broad discretion to determine what mitigations will sufficiently address the national security risk created by a transaction. Typical mitigations include limitations on access to systems or facilities to U.S. personnel; establishment of security protocols; special handling of contracts with the U.S. government, or carve-out of sensitive U.S. assets.[43]

Finally, CFIUS can impose penalties on parties in three circumstances: (i) failure to file a mandatory declaration or notice; (ii) failure to comply with mitigation agreements, conditions, or orders; and (iii) a material misstatement, omission, or false certification in materials filed with CFIUS.[44] Penalties for a material misstatement can be up to $250,000; penalties for a failure to file or a failure to comply can be up to $250,000 or the value of a transaction, *whichever is greater*.[45] In October 2022, the Treasury Department released guidelines that identified aggravating and mitigating factors CFIUS considers in deciding whether to impose a penalty.[46]

32 2021 CFIUS Annual Report, at 4.

33 31 C.F.R. § 800.401(b) and (c).

34 2021 CFIUS Annual Report, at 4.

35 31 C.F.R. § 800.501(b).

36 50 U.S.C § 4565(p), added by FIRRMA, established a $20 M annual fund, and authorized the collection of filing fees.

37 2021 CFIUS Annual Report, at 45.

38 50 U.S.C § 4565(f).

39 Exec. Order No. 14083, 87 Fed. Reg. 57369 (Sep. 15, 2022).

40 *Id.*

41 *Id.*

42 50 U.S.C § 4565(l).

43 2021 CFIUS Annual Report, 38-9.

44 U.S. Dept. of Treasury, CFIUS Enforcement and Penalty Guidelines, available at https://home.treasury.gov/policy-issues/international/the-committee-on-foreign-investment-in-the-united-states-cfius/cfius-enforcement-and-penalty-guidelines.

45 See 31 C.F.R. §§ 800.901, 802.901.

46 *See* CFIUS Enforcement Penalty Enforcement Guidelines.

IV. HOW CHINESE BUYERS HAVE FARED IN CFIUS REVIEW

According to the express language of section 721 of the Defense Production Act and CFIUS regulations, China is of no greater focus for CFIUS than any other country. By the numbers reported by CFIUS, Chinese investors represent a meaningful percentage of covered notices reviewed by CFIUS, but hardly a majority. In 2021, Chinese acquirers had the highest number of filed notices (44), accounting for 16.5 percent of all written notices filed that year.[47] But the two next highest were investors from staunch U.S. allies Canada (28 notices or 10.3 percent) and Japan (26 notices or 9.6 percent).[48] Over the three-year period from 2019 through 2019, Japanese investors filed more covered notices than did Chinese investors, 91 to 86.[49] And in terms of transactions concerning U.S. critical technology companies, Chinese acquirers were involved in only 10 of 184 in 2021, fewer than Germany, South Korea, and Japan, among others.[50]

But these numbers do not tell the whole story. Since the passage of FIRRMA, Chinese investment in U.S. companies has plummeted, from a peak of $45B in 2016 to an average of $7B from 2018 through 2020.[51] By contrast, in 2020, Japanese investment in the United States was $651 B,[52] and Canadian investment in the United States was $495 B.[53] In other words, while the raw number of Japanese and Canadian transactions reviewed by CFIUS is comparable to that of Chinese transactions, the proportion of all Chinese transactions that get reviewed by CFIUS appears to be much higher than for Japanese or Canadian transactions.

Moreover, while it is exceedingly rare for a U.S. President to block a transaction at the recommendation of CFIUS, most that have been blocked involve an acquirer with ties to China. By way of example, President Obama blocked only two deals in total in his eight years in office. Both involved Chinese acquirers.[54]

Withdrawn Transactions

The number of transactions blocked does not fully convey the heightened CFIUS scrutiny on transactions involving a Chinese acquirer. Some transactions are withdrawn and abandoned once CFIUS makes clear to the parties that no mitigation could sufficiently resolve its national security concerns and threatens to recommend a Presidential block. Parties may prefer to abandon their transaction rather than suffer the reputational harm associated with a public pronouncement by the President that their transaction presents unacceptable risk to U.S. national security.

In 2021, notices for 74 transactions were withdrawn and, of those, nine were abandoned because "either CFIUS informed them that it was unable to identify mitigation measures that would resolve the national security risk posed by the transaction, or the Committee proposed mitigation measures that the parties chose not to accept."[55] CFIUS does not publicize the number of withdrawn transactions broken down by nationality of the acquirer. But we know at least one of the abandoned transactions in 2021 involved a Chinese company. In March 2021, Wise Road Capital entered into an agreement to purchase Magnachip Semiconductor Corporation, a South Korea-based company, for $1.4 billion.[56]

47 2021 CFIUS Annual Report, at 32.

48 *Id.*

49 *Id.*

50 2021 CFIUS Annual Report, at 49.

51 Thilo Hanemann, et al., *Two-Way Street: 2021 Update US-China Investment Trends*, US-China Investment Project at 19 (May 2021), https://rhg.com/wp-content/uploads/2021/05/RHG_TWS-2021_Full-Report_Final.pdf.

52 Foreign Direct Investment (FDI) from Japan in the U.S. 2000 to 2001, available at https://www.statista.com/statistics/188907/foreign-direct-investment-from-japan-in-the-united-states-since-1990/.

53 Foreign Direct Investment (FDI) from Canada in the U.S. 2000 to 2001, available at https://www.statista.com/statistics/188881/foreign-direct-investment-from-canada-in-the-united-states-since-1990/.

54 Presidential Order Regarding the Acquisition of Four U.S. Wind Farm Project Companies by Ralls Corporation, DCPD-201200764 (Sep. 28, 2012), available at https://obamawhitehouse.archives.gov/the-press-office/2012/09/28/order-signed-president-regarding-acquisition-four-us-wind-farm-project-c; Presidential Order Regarding the Proposed Acquisition of a Controlling Interest in Aixtron SE by Grand Chip Investment GMBH (Dec. 2, 2016), available at https://obamawhitehouse.archives.gov/the-press-office/2016/12/02/presidential-order-regarding-proposed-acquisition-controlling-interest.

55 2021 CFIUS Annual Report, at 37.

56 Joyce Lee, *U.S. Treasury says China private equity's Magnachip purchase poses security risks*, Reuters (Aug. 30, 2021), https://www.reuters.com/business/us-treasury-says-china-private-equitys-magnachip-purchase-poses-security-risks-2021-08-31/.

The parties did not initially file a notice with CFIUS. CFIUS called in the transaction, and the parties filed a notice in June 2021.[57] After review, CFIUS conveyed to the parties that no mitigation could resolve its national security concerns and that it expected to recommend that President Biden block the transaction.[58] The parties abandoned their transaction in December 2021.[59] Other recent examples of transactions abandoned by Chinese acquirers include the 2018 Ant Financial/MoneyGram[60] and 2022 Asymchem/Snapdragon deals.[61]

Called-in Transactions

Some Chinese companies acquiring a U.S. business have chosen not to file a voluntary notice and closed their transaction, only to be ordered by CFIUS to unwind the deal, sometimes years later. Such was the case with Beijing Kunlun Technology Company's acquisition of California-based dating app, Grindr LLC. Kunlun first acquired a majority stake in Grindr in 2016, then acquired the remainder in 2018, choosing not to notify CFIUS either time.[62] CFIUS investigated the transaction in 2019 and expressed concerns to the parties over the access and potential use of personal data of U.S. citizens.[63] Kunlun entered into a national security agreement with CFIUS that required it to sell Grindr, which it ultimately did in 2020.[64]

Borqs Technologies acquisition of Holu Hou Energy ("HHE") met a similar fate very recently. In October 2021, Borqs, a Chinese company that specializes in software and products related to the Internet of Things ("IoT"), acquired a 51 percent stake in HHE, a Hawaii-based solar energy storage supplier. Borqs announced in December 2022 that CFIUS had sent a letter indicating that Borqs was "required to negotiate with CFIUS to fully divest its ownership interests and rights" in HHE.[65] According to Borqs, CFIUS was concerned that Borqs' IoT software development and sourcing in China would enable the Chinese government to exert influence over HHE's operations and gain access to its technology.[66] Borqs has not announced the consummation of the divestiture as of this writing.

There are exceptions, however. In 2021, CFIUS cleared at least two deals involving Chinese acquirers: Tencent's acquisition of Sumo Group, a UK-based gaming company with some U.S. operations,[67] and Genimous Technology's acquisition of Spigot, a U.S.-based digital marketing company.[68]

Both clearances were reportedly subject to mitigation.[69] Genimous acknowledged its mitigations related to the handling of sensitive personal data of U.S. citizens;[70] Tencent's may have as well, given the personal data typically collected by games. These transactions could signal

57 This transaction is also notable for the ostensibly limited connection of the target to the United States. According to Magnachip, while it is a U.S. holding company listed on the New York Stock Exchange, its entire business is located outside of the United States. Magnachip Semiconductor Corporation, Form 8-K (May 26, 2021), https://www.sec.gov/ix?doc=/Archives/edgar/data/1325702/000119312521177243/d185128d8k.htm. That CFIUS called in this transaction should serve as a warning that even a narrow U.S. nexus can bring a transaction within CFIUS' reach.

58 Magnachip Semiconductor Corporation, Form 8-K (Aug. 27, 2021), https://investors.magnachip.com/node/12536/html.

59 Magnachip Semiconductor Corporation, Form 8-K (Dec. 31, 2021), https://www.sec.gov/Archives/edgar/data/1325702/000119312521355865/d152828d8k.htm.

60 Greg Roumeliotis, *U.S. blocks MoneyGram sale to China's Ant Financial on national security concerns*, Reuters (Jan. 2, 2018), https://www.reuters.com/article/us-moneygram-intl-m-a-ant-financial/u-s-blocks-moneygram-sale-to-chinas-ant-financial-on-national-security-concerns-idUSKBN1ER1R7.

61 Rick Mullin, *US Treasury Department derails Asymchem's acquisition of Snapdragon*, Chemical & Engineering News (September 12, 2022), https://cen.acs.org/business/investment/US-Treasury-Department-derails-Asymchem-acquisition-of-Snapdragon/100/web/2022/09.

62 Carl O'Donnell, Liana B. Baker & Echo Wang, Exclusive: *Told U.S. security at risk, Chinese firm seeks to sell Grindr dating app*, Reuters (Mar. 27, 2019), https://www.reuters.com/article/us-grindr-m-a-exclusive/exclusive-told-u-s-security-at-risk-chinese-firm-seeks-to-sell-grindr-dating-app-idUSKCN1R809L.

63 See Tim Fitzsimons, *Inside Grindr, fears that China wanted to access user data via HIV research*, NBC News (Apr. 2, 2019), https://www.nbcnews.com/feature/nbc-out/inside-grindr-fears-china-wanted-access-user-data-hiv-research-n989996.

64 Yuan Yang & James Fontanella-Khan, *Grindr sold by Chinese owner after US national security concerns*, Financial Times (Mar. 7, 2020), https://www.ft.com/content/a32a740a-5fb3-11ea-8033-fa40.

65 Stephen Nakrosis, *Borqs to Divest Holu Hou Energy on CFIUS National Security Concerns*, Market Watch (Dec. 19, 2022), https://www.marketwatch.com/story/borqs-to-divest-holu-hou-energy-on-cfius-national-security-concerns-271671490198.

66 *Id.*

67 James Batchelor, *Tencent's Sumo acquisition continues following US national security investigation*, Games Industry.biz (December 14, 2021), https://www.gamesindustry.biz/tencents-sumo-acquisition-continues-following-us-national-security-investigation.

68 Tang Shihua, *China's Genimous Gains After US Govt Allows It to Keep Stake in US Data Services Firm Spigot*, Yicai Global (Oct. 8, 2021), https://www.yicaiglobal.com/news/china-genimous-gains-as-us-government-allows-it-to-keep-stake-in-us-data-service-firm-spigot.

69 Batchelor, *supra* and Shihua, *id.*

70 Shihua, *supra*.

that CFIUS may view acquisitions involving U.S. businesses with access to sensitive personal information as more susceptible to mitigation than the other two types of TID businesses.

V. BEYOND CFIUS

The tensions between the United States and China that led to FIRRMA have not gone away since 2018. Indeed, several additional measures that seek to regulate M&A activity implicating the U.S.-China relationship were either very recently signed into law or are under active consideration.

The Merger Filing Fee Modernization Act ("MFFMA") of 2022 requires parties to a transaction subject to HSR pre-merger notification obligations to include in their filing information concerning any subsidies received "from countries or entities that are strategic or economic threats to the United States."[71] The MFFMA's findings expressly cite concerns about China's "Made in China 2025 plan" through which the Chinese Communist Party seeks to "support enterprises to carry out mergers and acquisitions, equity investment and venture capital overseas."[72] The MFFMA's findings go on to warn that "[f]ailure to appreciate the gravity of this challenge and defend U.S. competitiveness would be dire . . . [and] risks setting back U.S. economic and technological progress for decades."[73] The MFFMA requires the FTC, with the concurrence of the DOJ, and in consultation with CFIUS, to engage in a rulemaking to update the HSR form to account for this new requirement.[74] This law does not become effective until the HSR form is updated;[75] a timeline for the rulemaking has not been announced as of this writing.

Both Congress and the Biden Administration have expressed interest in creating a mechanism through which some U.S. investments in foreign countries can be reviewed — colloquially termed "reverse" or "outbound" CFIUS. In May 2021, a bipartisan group of Senators proposed the National Critical Capabilities Defense Act ("NCCDA"), which would "establish a whole-of-government process to screen outbound investments and the offshoring of critical capacities and supply chains to foreign adversaries, like China and Russia, to ensure the resiliency of critical supply chains."[76] The NCCDA would create a CFIUS-like twelve-member interagency committee charged with monitoring outbound investments in identified countries of concern, including China.[77] A scaled-down version of this proposal that only impacts transactions involving semiconductor manufacturers was included in the CHIPS and Science Act passed in August 2022.[78] Approximately a month after the CHIPS and Science Act passed, the sponsors of the NCCDA sent a letter to President Biden, urging him to take executive action to establish the full version of the committee as envisioned in their proposed legislation.[79] On October 12, 2022, the Biden Administration released its National Security Strategy, which referenced the possibility of taking executive action to address the screening of outbound investment "to prevent strategic competitors from exploiting investments and expertise in ways that threaten national security."[80] At the time of this writing, despite expectations of its imminent release, President Biden has not issued an executive order concerning outbound CFIUS.

Yet another legislative proposal sought to establish an interagency task force regarding China, this one charged with investigating "allegations of systemic market manipulation and other potential violations of antitrust laws" in the United States committed by companies in China."[81] The task force would focus on three critical industries: (1) the pharmaceutical and medical devices industry; (2) the renewable energy industry; and (3) the steel and aluminum industries.[82] This provision was included in the United States Innovation and Competition Act of 2021,

---

71 Merger Filing Fee Modernization Act, Title 2 § 201(b).

72 *Id.* at § 201(a)(3).

73 *Id.* at § 201(a)(4).

74 *Id.* at § 202(c).

75 *Id.* at § 202(d).

76 Press Release, Bob Casey & John Cornyn, U.S. Senators, Casey and Cornyn Release a Joint Statement on National Critical Capabilities Defense Act (May 24, 2021), https://www.casey.senate.gov/news/releases/casey-and-cornyn-release-a-joint-statement-on-national-critical-capabilities-defense-act.

77 Proposed Amendment 1853 to S. 1260, available at https://www.casey.senate.gov/imo/media/doc/casey-cornyn_nccda_amendment.pdf.

78 CHIPS Act of 2022 § 103.

79 Letter from Sen. R. Casey, et al., to President J. Biden (September 27, 2022), available at https://www.casey.senate.gov/news/releases/supporters-of-outbound-investment-legislation-urge-administration-to-take-executive-action-to-safeguard-national-security-protect-supply-chains.

80 National Security Strategy (Oct. 2022) at 33, available at https://www.whitehouse.gov/wp-content/uploads/2022/11/8-November-Combined-PDF-for-Upload.pdf.

81 United States Innovation and Competition Act of 2021, S.1260, 117th Cong. § 5102(a) (2021).

82 *Id.* at § 5102(a)-(b).

which passed the Senate in June of 2021. The Innovation and Competition Act was ultimately folded into the CHIPS Act, but this Chinese market manipulation task force provision was not included.

And while beyond the scope of this article, it is worth noting that a major cross-border transaction by a Chinese acquirer could also be subject to foreign direct investment ("FDI") regimes besides CFIUS. As of September 2022, there are more than 50 FDI regimes around the world; many—such as Belgium, the European Union, Estonia, Ireland, the Netherland, and the United Kingdom—have been established in the last several years, in many cases with CFIUS experts providing technical assistance. And, like CFIUS, existing regimes, such as those in Australia, China, Germany, and Japan, have seen their powers increase. This proliferation of FDI regimes has especially affected buyers with ties to China. In 2022, FDI regimes blocked 20 transactions around the world, 16 of which featured buyers that were either based in China or Hong Kong or that were European-based subsidiaries of Chinese companies.[83]

VI. PRACTICAL CONSIDERATIONS

In light of the above, CFIUS risk for a Chinese acquirer should always be considered higher than a similarly situated transaction involving a buyer from virtually any other country. As such, Chinese acquirers should be assessing CFIUS risk early in the deal process, as is typically done to assess competition risk. And just as failing to account for significant competition risk can jeopardize a transaction, so too can failing to account for CFIUS risk.

Unlike the relatively simple calculation to determine whether a transaction will trip the HSR filing thresholds, determining whether to notify CFIUS of a transaction is a much more complex and holistic endeavor. There are several key questions to evaluate:

- **Is the target a TID U.S. business?** Diligence should start with determining whether the U.S. target is a TID U.S. business. The presence of a TID business is a precondition to fulfilling either prong of the mandatory filing test, and failing to file a mandatory declaration will expose the parties to substantial penalties. As a starting point, counsel should look to whether the target has any U.S. export control licenses to determine if it is involved with any "critical technologies" that would trigger a mandatory declaration. A target that is a TID U.S. business by virtue of its involvement in critical infrastructure or with sensitive data does not trigger a mandatory filing (unless the transaction would grant a foreign government a substantial interest in them - see next question), but is nonetheless likely to be of interest to CFIUS if acquired by a Chinese company.
- **Will the Chinese government obtain any interest in the target through the transaction?** Chinese acquirers should ensure they have a clear understanding of any ownership interest in their groups held by the Chinese government, or any organ thereof. CFIUS will likely be interested in any transaction regardless of the affected industry if the Chinese government will obtain a controlling interest post-transaction. And a substantial interest short of a controlling interest will trigger a mandatory filing if the target is a TID U.S. business.
- **Does the target implicate any of the areas highlighted by the Biden Administration CFIUS executive order?**
    - Is the target involved in microelectronics, artificial intelligence, biotech and biomanufacturing, quantum computing, advanced clean energy, climate adaptation technologies, or any other technology identified on the U.S. Critical and Emerging Technologies list?[84] A transaction that could affect U.S. leadership in any of these spaces is apt to get attention from CFIUS.
    - Does the target play a key role in the supply chain for any of the above technologies or that of the defense, public health, information technology, energy, transportation, or agricultural sectors? This is an incredibly broad list that has the potential to swallow up the other factors. Two aspects to pay particular attention to is whether the target directly supplies the U.S. government and the degree to which buyers have viable alternative suppliers that could replace the target.
    - Has any sector in which the target participates already seen significant investment from Chinese companies? Counsel should conduct diligence on the ownership of competitors of the target to try to detect any concentration of Chinese investment.
    - Does the target provide cybersecurity products or services? CFIUS will look at whether foreign control of the target could provide a pathway to cyber incursions into U.S. elections or critical infrastructure.

With CFIUS' resources for identifying and calling in transactions greatly expanded post-FIRRMA, a transaction that features some or all of these factors is not likely to fly under the radar.

83 Luuk Klein, *FDI screening killed at least 20 mergers globally totaling over USD 6bn in 2022*, Ion Analytics (Jan. 20, 2023), https://community.ionanalytics.com/fdi-screening-killed-at-least-20-mergers-globally-totaling-over-usd-6bn-in-2022.

84 Exec. Office of the President, Critical and Emerging Technologies List Update, Rep. of the Nat'l Sci. & Tech. Council (Feb. 2022), available at https://www.whitehouse.gov/wp-content/uploads/2022/02/02-2022-Critical-and-Emerging-Technologies-List-Update.pdf.

In addition, just as parties facing an HSR review consider what remedies the DOJ or FTC might seek in order to clear a transaction, parties facing a CFIUS review should think early on about what mitigations CFIUS may require — and whether a transaction subject to those mitigations would remain worthwhile. Parties facing both types of scrutiny might consider whether there are acceptable remedies that address both sets of concerns (e.g. a divestiture of the U.S. portion of a target's business that would satisfy CFIUS could also eliminate a product overlap of concern to the FTC or DOJ).

With this knowledge up front, an acquirer can better account for CFIUS risk in a merger agreement through similar tools to those used in managing antitrust risk:

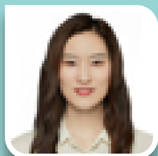
- In the case in which the acquirer believes a mandatory filing is required, it may want to write expressly into the agreement that the parties agree that a filing is required and commit to such a filing within X days of signing. To further incent a reluctant seller, the buyer could commit to paying the buyer's filing expenses.
- If the acquirer has concluded that there are several mitigation measures it is willing to take and others that would cause it to want to walk away from the deal, it has several options. It could include a regulatory efforts clause that commits it to agree to mitigations in order to close the transaction, but only with regard to the specific mitigations it is willing to accept. This approach signals the acquirer's commitment to the deal without requiring it to accept every mitigation CFIUS seeks. If the acquirer is concerned that identifying specific mitigations in a regulatory efforts clause could lead CFIUS to view those as a starting point for negotiations, it might instead opt for a commitment to agree to mitigations up to a certain dollar or materiality threshold.
- The termination date, the date by which the parties can terminate if the transaction has not closed, is often driven by the expected delay caused by HSR review. A second request could delay closing by 9-12 months (sometimes more if remedies need to be negotiated across jurisdictions and especially if litigation ensues). This will typically be longer than needed to resolve a CFIUS review. But a CFIUS case involving a Chinese acquirer could involve pulling and refiling and lengthy mitigation negotiations that stretch the review out for a year or more. Thus, even if a transaction is expected to sail through an antitrust merger review or does not even meet HSR thresholds, a Chinese acquirer may want to set a termination date far enough in the future to account for a protracted CFIUS review.

Chinese acquirers considering large, cross-border transactions should also keep in mind another distinction between antitrust and CFIUS review: CFIUS and the many other FDI regimes around the world are not likely to coordinate with one another in the way that parties have grown accustomed to the DOJ and FTC coordinating with ex-U.S. competition authorities on cross-border merger review. FDI review implicates a country's sensitive national security information, which countries are very hesitant to share with other countries — sometimes even with allies — for fear of exposing weak points or compromising sources and methods. FDI and competition authorities are typically separate bodies or separate parts of a single body that are formally or informally walled off from one another. As such, there may not be significant coordination even between the FDI and competition authorities within a jurisdiction. Notably, the U.S. may soon represent an exception to this, as the new rule requiring disclosure of non-U.S. sources of investment on the HSR form seems likely to foster increased contact between CFIUS and the FTC and DOJ. Regardless, parties should understand that coordinating the timelines for FDI review in multiple jurisdictions with one another and with parallel competition merger reviews is quite difficult and can be a source of significant pain.

All told, Chinese acquirers today face increased obstacles to investing in a U.S. business, but with sufficient planning and forethought, it remains possible to navigate this challenging path and reach a positive resolution.

THE INTERACTION OF IPRs AND ANTITRUST: FROM THE PERSPECTIVE OF CHINESE PRIVATE ANTITRUST LITIGATIONS

BY HAO ZHAN, YING SONG & RUICHEN LIU[1]



1 Hao Zhan, Partner of AnJie Broad Law Firm. Ying Song, Partner of AnJie Broad Law Firm. Ruichen Liu, Associate of AnJie Broad Law Firm.

I. ANTITRUST LEGISLATION RELATED TO IP IN CHINA

A. The AML

The AML contains only one provision to set up the basic principle on how to deal with IPR-related antitrust issues, namely the Article 55 of the AML 2008 (Article 68 of the AML revised in 2022). The article reads "[t]his Law shall not apply to undertakings' conduct of exercising IPRs in accordance with laws and administrative regulations on IPRs; however, this Law shall apply to undertakings' conduct of abusing intellectual property rights to exclude or restrict competition." As the general vague stipulation on the relationship between IPRs and the AML, it is very often difficult for businesses to figure out the fine line of two different law systems. It could be more complicated in patent-related cases because of the complexity and edge-cutting nature of patent claims. For instance, it is not an easy job to define the relevant market of IPRs due to the nature of intangibility and potential competitive constraints from newly created IPs. In these cases, traditional factors to assess market power and competitive effects may not be able to draw a whole picture of competitive landscape in the relevant market either. Moreover, regular activities of exploring the IPRs, such as licensing or not licensing and seeking for injunctions, may also be determined as having stepped into the prohibitive zone of antitrust law, when some specific criteria are met. In short, the sole provision under the AML is far from sufficient.

B. Provisions on Prohibiting the Abuse of IPRs to Exclude or Restrict Competition

Through recent decades, China has made a great deal of efforts to elaborate the sole general provision of the AML by formulating supplementary regulations and guidelines. These supplementary rules not only serve as a good legal basis for antitrust public enforcement, but also become significant references to Chinese courts in private antitrust litigations.

Specifically, back to the year of 2015, the former State Administration for Industry and Commerce (hereinafter "SAIC"), one of the three former antitrust regulators of China, published the *Provisions of the State Administration for Industry and Commerce on Prohibiting the Abuse of Intellectual Property Rights to Exclude or Restrict Competition* (hereinafter *"SAIC Provisions"*), which took effect on July 1, 2015. It is commendable that the *SAIC Provisions* set up the basic analysis approach of defining a relevant market and an abuse of dominance based on the attributes of IPRs. The *SAIC Provisions* also introduced the "safe harbor" in the field of IPRs. However, as there were three central-level authorities in charge of the AML enforcement and the former SAIC only governed non-price related antitrust enforcement at that time, the *SAIC Provisions* did not touch upon any facet in connection to price related antitrust violations and concentrations of undertakings.

After China's antitrust institutional reform in 2018, the newly established and uniform antitrust authority in China, namely the State Administration for Market Regulation (hereinafter "SAMR"), published new *Provisions on Prohibiting the Abuse of Intellectual Property Rights to Exclude or Restrict Competition (2020 Revision)* (hereinafter "SAMR Provisions") to replace the *SAIC Provisions*. Compared with the rules its predecessor made, the *SAMR Provisions* made only with minor amendments; in particular, having supplemented provisions on price-related monopolistic acts and concentrations of undertakings.

With the amended AML entering into force in August 2022, the necessity to renew the practical regulations in the field of IPRs became a realistic issue. For that reason, shortly after the announcement of the AML 2022, the SAMR published several drafts of supplementary antitrust regulations, including the new *Provisions on Prohibiting Abuse of Intellectual Property to Exclude or Restrict Competition) (Draft for Comments)* (hereinafter *"Draft Provisions"*). The *Draft Provisions* properly reflected the modifications of the AML and also refined the rules based on the experience accumulated from the practices. Though the SAMR has not published the official version yet, it is expected to be wrapped up and released soon.

C. The Anti-Monopoly Guidelines in the Field of IPRs

In order to make the antitrust enforcement in the field of IPRs by three former antitrust authorities coherent with each other, the Anti-Monopoly Committee of the State Council (hereinafter "AMC") has commissioned the former SAIC, the National Development and Reform Commission, the Ministry of Commerce and National Intellectual Property Administration to draft a more universal guidelines in the field of IPRs. In January 2019, the AMC has published the Guide of the *Anti-Monopoly Committee of the State Council for Countering Monopolization in the Field of Intellectual Property Rights* (hereinafter *"IPR Guidelines"*).

In general, these guidelines encompass basic principles and approach for determining the monopolistic abuse of IPRs and detailed analytical approaches for market definition, assessment of anti- and pro-competitive effects, and determination of unlawful behaviors under the AML, in the field of IPRs. Notably, the *IPR Guidelines* also recognize the antitrust risks of patent pooling activities, activities related to

SEPs and collective management of copyrights. Compared to the *SAMR Provisions*, the *IPR Guidelines* provide more detailed and applicable guidance. For instance, there is only one clause governing the monopoly agreements in the field of IPRs in the *SAMR Provisions*, while the *IPR Guidelines* institute a whole chapter (7 clauses) to frame how to assess the competitive effects of IPR-related agreements in several particular scenarios including joint R&D, cross-licensing, sole and exclusive grant-back, non-assertion clauses, standard development and so on.

II. RECENT JUDICIAL PRACTICE IN CHINA AND KEY ISSUES

The Chinese courts have started their judicial review on the interaction of IPRs and antitrust issues for a while, and one representative case regarding abuse of SEPs, is *Huawei v. IDC*. In recent years, more patentees have been involved in the abuse of market dominance litigations and the courts have begun to play a role when conducting the antitrust assessment in the non-SEPs scenario. The *Hitachi Metals Case* is a notable example. Furthermore, novel issues have also been brought forward in monopoly agreement cases. For example, the SPC made its leading judgment in finding the patent settlement agreement as cartel in the *Transformer Switch* Case. The SPC also voluntarily examined the legality of a settlement agreement with the suspicion of pay-for-delay in the drug sector. Thus, a deep insight into these leading cases will facilitate a better understanding of how the monopolistic abuses of IPRs are assessed and dealt with in China's judicial practice.

A. The Transformer Switch Case: Pitfall of IP Settlement Agreement

The parties in the IP disputes may reach a settlement agreement to avoid the enormous amount of costs in the long-standing litigations and the risks of the disputed IP being invalid. Notably, the agreements are very often with a horizontal nature, particularly in patent cases, for the firms are either actual or potential competitors in the market for the ultimate products or in the innovation market itself. As a result, IP settlement agreements sometimes raise significant antitrust issues.[2]

After exploring the preliminary criteria of determining the monopoly agreement in the drug pay-for-delay case, the *AstraZeneca v. Jiangsu Aosaikang Pharmaceutical* case,[3] the SPC began to review whether other kinds of patent settlement agreements other than reverse payment agreements constitute monopoly agreements in other industries. The *Monopoly Agreement Dispute Concerning Transformer Charger* (hereinafter the *"Transformer Charger Case"*)[4] should be the first one in China's private antitrust enforcement up to date, having discussed in much detail how the elements of a horizontal monopoly agreement should be determined, and how to solve the conflict between the adjudicative documents of the previous patent dispute and that of the latter anti-monopoly civil litigation. The SPC's reasoning in this case could help people figure out under what conditions may a patent settlement agreement constitute an unlawful monopoly agreement.

1. Case Background

In the *Transformer Charger Case*, the agreement in question is a settlement agreement entered by the parties to settle patent disputes thereb-etween. The defendant, a transformer charger company named Wuhan Taipu Transformer Changer Co. Ltd. (hereinafter "TTCC") filed a patent infringement lawsuit (hereinafter "Patent Dispute") against the plaintiff, a power equipment company named Huaming Power Equipment Co. Ltd. (hereinafter "HPEC") in 2015, on the ground that the technical features of the shielding cover of a certain type of transformer tap changers (hereinafter "Transformer Charger") produced and sold by HPEC had infringed TTCC's patents. As a counter measure, HPEC soon after applied to National Intellectual Property Admission for a declaration of invalidity of the patent in question and also applied to the court hearing the case, Wuhan Intermediate People's Court, for a stay of proceeding.

In 2016, to solve their IP disputes, both parties entered a settlement agreement. In the settlement agreement, the parties agreed that:

> (i) The transformer charger in question was divided by type, and except for the type of the transformer charger in question, HPEC shall not manufacture or commission any third party (or purchase from it) other than TTCC to manufacture all other types of transformer charger bodies and related parts in question. Meanwhile, HPEC shall be the overseas market agent for TTCC's shareholding company and undertakes not to manufacture on its own in the overseas market, nor to act as agent for similar products of other enterprises.

2 Herbert Hovenkamp, Mark Janis & Mark A. Lemley, Anticompetitive Settlement of Intellectual Property Disputes, 15 Minn. J. L., Sci. & Tech. 3 (2014).

3 *AstraZeneca v. Jiangsu Aosaikang Pharmaceutical*, (2021) Zui Gao Fa Zhi Min Zhong No. 388.

4 *Monopoly Agreement Dispute Concerning Transformer Charger*, (2021) Zui Gao Fa Zhi Min Zhong No. 1298.

(ii) HPEC should first confirm with TTCC on TTCC's price of main part of transformer charger before deciding the quotation by itself, and then quote the price to TTCC with the purchase of the main part. In addition, the parties agreed that, for substitutable imported chargers and special chargers, if one party informs the other party of the price information, the transaction price of the informed party cannot be lower than that of the actively informed party.
(iii) If HPEC breaches the above agreement, it shall compensate TTCC all losses incurred therefrom and additionally pay high liquidated damages.

However, HPEC did not fulfill the said settlement agreement, and TTCC thereby sued HPEC for its violation of the settlement agreement twice respectively in January 2017 and June 2018. In May 2019, HPEC filed a lawsuit to the Wuhan Intermediate People's Court (hereinafter the "Court of First Instance"), requesting to declare that the settlement agreement in question was void due to its violation of the AML. Unfortunately, the Court of First Instance dismissed the claims of HPEC. HPEC then appealed to the SPC in 2021 and the SPC in the end overruled the first instance judgment, finding **that the relevant provisions of the settlement agreement in question constituted a horizontal monopoly agreement prohibited by Article 13(1) of the AML 2008, and that the settlement agreement in question was void**.

2. Disputed Issue: What is the boundary between legitimate settlement agreements and Monopoly Agreement

In the final judgment, the SPC discussed in detail how to distinguish an unlawful monopoly agreement disguised by the form of patent settlement agreements, from a legitimate settlement agreement in the following three steps:

Step 1: What is the market relationship of the parties of patent settlement agreements

As stipulated in the Article 13(1) of the AML 2008 (Article 17 of the AML 2022), the horizontal monopoly agreements can only be reached among competitors (actual or potential). Thus, it is always the first place to examine the competition relationship between the concerned parties when looking into a claimed horizontal monopoly agreement. In the *Transformer Charger Case*, HPEC and TTCC are both engaged in the production and sales of transformer tap changers and can be regarded as competitors from the perspective of the AML. Then the Step 1 test was satisfied.

Step 2: Whether the agreements contain any hardcore restrictions stipulated by the AML regardless of whether it is patent-related

After examining the contents of the settlement agreement at dispute, the SPC reached a conclusion that it contained market division, production and sales restriction and a high chance of price cartel, and any of them constitutes a per-se illegal horizontal agreement for the reasons set out below:

- First of all, the transformer chargers in question were divided by type, and HPEC was prohibited by the settlement agreement from manufacturing all other types of transformer charger bodies and related parts in question. It meant that the agreement set a clear dividing line of what could be manufactured and sold by the two parties.
- Second, the settlement agreement also limited the production and sales of HPEC's products by stopping production and restricting the sales of specific types of products.
- Third, as the settlement agreement had stipulated that HPEC should not manufacture all other types of transformer charger bodies and related parts in question, when there was only one manufacturer or supplier, the cost and profit margin of HPEC were largely fixed, which directly led to the dependency of HPEC's sales price on the price HPEC paid to TTCC for those products commissioned to TTCC. In the overseas market, as HPEC could not sell products from any third party other than TTCC and the actual sales price of HPEC to users was the price HPEC paid to TTCC, the sales price of HPEC had, as a matter of fact, been limited by TTCC.

Step 3: Whether the patent settlement agreement have anti-competitive effects

According to the Article 13(2) of the AML 2008, a monopoly agreement is an agreement, decision, or other concerted act to exclude or restrict competition. The SPC concluded that as for the five types of horizontal agreements explicitly prohibited by Article 13(1) of the AML 2008, they are typical horizontal monopoly agreements that can be deemed as having effects of eliminating or restricting competition, where the per se illegal rule should applies. In this case, the burden of proof shifts to the defendant to prove that the agreement has the effects of promoting competition and the pro-competitive effects outweigh its effects of eliminating and restricting competition. Moreover, the SPC also pointed out in its final judgment that the context or purpose of the settlement agreement and the subjective intention of the parties in entering into the settlement agreement are only reference factors rather than decisive, and it is not sufficient to determine or deny the effect of the settlement agreement on market competition.

<u>**Key arguments from the side of TTCC**: Whether the settlement agreements fall into the scope of a legitimate exercise of patent right</u>

In the first hearing, TTCC argued that 1) the settlement agreement involved was a general civil and commercial contract instead of a monopoly agreement; 2) the agreement at dispute was reached by the two parties to resolve the patent infringement dispute and preventing subsequent patent infringement, whose validity was confirmed by previous judicial judgments.

To respond to the abovementioned arguments of TTCC, the SPC concluded that according to Article 55 of the AML 2008, what the court will consider when assessing if a patent settlement agreement constitutes a monopoly agreement is whether the settlement agreement is a necessity to lawfully exercise the patent rights. The approach adopted by the SPC in the *Transformer Charger Case* is quite similar to the patent scope test adopted by U.S. courts which emphasizes the consideration of the exclusivity of patent rights when conducting antitrust review of reverse payment agreements. Assuming that the patent in dispute is valid, it is necessary to determine the scope of protection of the patent rights in dispute and the scope of exclusivity of the agreement, compare and determine whether the agreement exceeds the necessary scope for protection of the patent rights. If it does, the monopoly should be found; otherwise, it does not constitute monopoly. Moreover, the SPC distinguished basic patents and secondary patents in the *Transformer Charger* Case. The SPC maintained, in general, the infringers may hold a more favorable position in the patent infringement dispute regarding secondary patents as it is more possible to challenge the validity of secondary patents; and in this case the patentees are more motivated to reach a settlement agreement outside the scope of the patent to prolong the period of exclusive rights of the secondary patents and maintain their monopolistic interests.

Back to the *Transformer Charger* Case, the SPC found that the disputed patent in the previous patent dispute between HPEC and TTCC as the context of the disputed settlement agreement was a secondary patent to improve the stability of the transformer chargers, instead of an unavoidable basic patent. The patent in question was about the transformer chargers with a specific structure but nothing about the shapes or types of transformer chargers. Thus, the division of transformer chargers by type had already exceeded the protected claims under TTCC's patents in the previous patent dispute. For the overseas markets, the settlement agreement in question divided the products into chargers produced by the transformer charger company's participating companies and chargers produced by other companies, to the effect of limiting the scope of chargers produced by HPEC, while this limitation was not substantially related to the scope of protection of the patent in question. As the SPC concluded in its final judgment, the concerned settlement agreement lacked substantial relevance to the scope of protection of the patent right in question, and the agreement had the effect of excluding and restricting competition, consequently constituted a horizontal monopoly agreement under the AML.

To conclude, the *Transformer Charger Case* is a milestone for Chinese courts to set up a clear way to assess whether an IP-related agreement constitute a horizontal monopoly agreement. It also makes explicit that it will not escape from the governance of the AML even if the agreement is in disguise of the protection of IPRs. The reasoned assessment made by the SPC does not only provide a definitive analytical approach for assessment of the monopoly agreement in similar cases, but also set a reference modal for the self-assessment of businesses in the practice of settlement negotiation, IP licensing and cooperation talks with competitors.

B. The Hitachi Metals Case: Controversial Extension of "Essential Facilities" Doctrine into Non-SEPs

As mentioned above, the Chinese courts have made efforts to deal with the complex interaction between lawful exclusive patent rights and antitrust law requirements of non-refusal to deal. For example, in the case of *Huawei v. IDC*,[5] the court concluded that as for a SEP holder, failure to license on the FRAND basis and compelling the licensees to accept unfair high licensing fees by means of bringing about infringement injunctions against others could be regarded as an abuse of dominance, as SEP holders could be deemed as holding naturally the dominant position in each SEP market.

Where the disputed patent is not a SEP, to assess whether refusal of license constitutes an abuse of dominance can be a more difficult matter for the courts. It took more than six years for China's Ningbo Intermediate People's Court to render the first instance judgment in a dispute between four Ningbo magnetic material manufacturers and Hitachi Metals, Ltd. (hereinafter the "HML"), which has aroused hot debates on the application of "essential facilities" doctrine by the Ningbo Intermediate People's Court to define abusive refusal to license in the case of non-SEPs (hereinafter the *"Hitachi Metals Case"*).[6] As the doctrine of "essential facilities" itself is controversial, it has been seldom applied by antitrust authorities worldwide even in the case of SEPs, let alone non-SEPs. Furthermore, it was even the first time that Chinese courts applied the "essential

5 *Huawei v. IDC*, (2013) Yue Gao Fa Min San Zhong No. 306.

6 *Ningbo Ketian Magnetic Industry Co., Ltd. v. Hitachi Metals, Ltd., (2014) Zhe Yong Zhi Chu No. 579; Ningbo Permanent Magnetic Industry Co., Ltd. v. Hitachi Metals, Ltd., (2014) Zhe Yong Zhi Chu No. 580; Ningbo Tongchuangqiang. Magnetic Materials Co., Ltd. v. Hitachi Metals, Ltd., (2014) Zhe Yong Zhi Chu No. 581; Ningbo Huahui Magnetic Industry Co., Ltd. v. Hitachi Metals, Ltd.*, (2014) Zhe Yong Zhi Chu No. 582.

facilities" doctrine. Thus, it is meaningful to look into details of the reasoning and conclusion made by the Ningbo Intermediate People's Court's application of the "essential facilities" doctrine in the first instance judgment and its appropriateness.

1. Case Background

In August 2013, an Alliance established by seven Chinese companies including the four plaintiffs in the *Hitachi Metals Case*– i.e. Ningbo Tongchuangqiang. Magnetic Materials Co., Ltd., Ningbo Permanent Magnetic Industry Co., Ltd., Ningbo Ketian Magnetic Industry Co., Ltd. and Ningbo Huahui Magnetic Industry Co., Ltd. (hereinafter "Four Plaintiffs"), filed a complaint to the U.S. Patent Office against HML for invalidation of its core patents of sintered neodymium-iron-boron (hereinafter "sintered NdFeB"), a type of rare earth magnets. In May 2014, the Alliance and HML negotiated in San Francisco yet failed to reach an agreement; the seven companies have not obtained the relevant licenses. Therefore, four plaintiffs sued HML for abuse of dominance to Ningbo Intermediate People's Court; the case was officially accepted on December 11, 2014.

The first hearing was held on December 17, 2015, and the second one on March 10, 2017. And then, the dormant case was back to life in early 2021. The regional court handed down all four decisions on April 23, 2021, in favor of Four Plaintiffs. The Ningbo Intermediate People's Court has extended the "essential facilities" doctrine to licensing of non-SPEs in its ruling and compelled HML to license its non-SEPs. HML then appealed the case to the SPC and the SPC has already held the hearing in November 2021.

2. The "Radical" Application of "Essential Facilities" Doctrine in the Hitachi Metals Case

The Ningbo Intermediate People's Court in the *Hitachi Metals Case* mainly relied on the "essential facilities" doctrine to create a brand-new concept of "essential patent" and concluded that HML held a dominant position in the market of its sintered NdFeB patents and had abused its dominant position by refusing to license its patents to Four Plaintiffs.

Nonetheless, as mentioned above, the application of the "essential facilities" doctrine to a non-SEP by the Ningbo Intermediate People's Court has been criticized as an excessive misapplication of this carefully balanced legal concept after the judgment was rendered for several grounds. Firstly, some people criticized that the concept of "essential patents" was neither a well-accepted concept of patent law nor a concept under the antitrust law; secondly, it was argued that the application of "essential facilities" doctrine has strict conditions and the first instance judgments made by the Ningbo Intermediate People's Court did not give a detailed explanation to support why it applied such a doctrine; and thirdly, concerns rested on that it might flip the balance between the exclusive nature of IPRs and the intervention of antitrust law embodied in the "essential facilities" doctrine.

Indeed, the "essential facilities" doctrine usually refers to a duty imposed on a monopoly that controls access to an important resource "essential" or "bottleneck" facility to deal with its competitors by providing access to such a "facility" that it controls and is deemed necessary for effective competition, at a reasonable price.

i) The strictness of the "essential facilities" doctrine

It is widely agreed that strict standards need to be met before applying the doctrine of "essential facilities," because it restricts the rights of property owners. Specifically, if the "essential facilities" doctrine is applicable, the owners of essential facilities bear the responsibilities to share their essential facilities with other competitors. Otherwise, the antitrust law must respect the freedom of business operators to choose their trade counterparties. Article 7 of the *SAMR Provisions* lays out the preconditions for the application of essential facilities: (1) the IPRs cannot be reasonably substituted, and it is indispensable for other operators to participate in the competition in the relevant market; (2) refusal to license the IPRs will adversely affect competition or innovation in the relevant market and harm the interests of consumers or public interests; (3) licensing the IPRs will not cause unreasonable harms to the right holders. The Ningbo Intermediate People's Court also summarized the conditions of applying the doctrine as follows: (1) the facilities are indispensable for other business operators to participate in competition; (2) the monopolist has control of the essential facilities; (3) the competitor cannot duplicate the same facilities within a reasonable effort; (4) the monopolist unreasonably refuses the competitor to utilize the essential facilities; (5) it is possible for the monopolist to provide the essential facilities. In addition to the above five conditions, it should also be taken into consideration whether the refusal to license the IPR will have negative influence on competition or innovation on the relevant market and thus harm consumer or public interests.[7]

7 Ningbo Ketian Magnetic Industry Co., Ltd. v. Hitachi Metals, Ltd., (2014) Zhe Yong Zhi Chu No. 579.

In the foreign practices, at least three tests should be considered to see whether the IPRs in question were indispensable for competition in the market: (1) the refusal is preventing the emergence of a new product for which there is a potential consumer demand; (2) the refusal is not justified by an objective consideration; (3) the refusal will exclude any or all competition or will eliminate any or all competition in a secondary market.[8] As the preconditions to apply the "essential facilities" doctrine are hard to satisfy, such doctrine applies in rare cases in practice. In fact, this is the first time for Chinese courts to apply the "essential facilities" doctrine in real antitrust civil litigations.

ii) The balance between IPRs and antitrust law

Many scholars stressed, when applying the "essential facilities" doctrine in the case of IPRs, it is necessary to balance different legal interests under different legal systems. As the "essential facilities" doctrine sets limitations of the holders' abilities to choose trade counterparties at their discretion and even the exercise of IPRs in full, a balance needs to be reached to avoid interest conflicts among legal systems of antitrust law, contract law and IP laws. Regarding the relationships between contract law and antitrust law, it is well acknowledged that an undertaking shall "freely to exercise his own independent discretion as to parties with whom he will deal";[9] antitrust and competition law "does not restrict the long-recognized right of trader or manufacturer engaged in an entirely private business."[10]

Undoubtably, as the first "essential facility" doctrine case, the first instance judgment in the *Hitachi Metals Case* raised controversies on whether it is appropriate to apply this doctrine where there was not any industrial standard in the manufacture of NdFeB. It has been argued that theocratically, when it comes to non-SEPs, it should be more prudent for antitrust law to intervene the freedom to choose trade counterparties and whether to trade of the holders of non-SEPs, because compared to SEPs, the holders of non-SEPs may bear less responsibilities to share their patents and their legal patent rights may be impeded by compelling them to license.

iii) What the key factor of applying the "essential facilities" doctrine should be

As stipulated by Article 55 of the AML 2008 which reads "[t]his Law is not applicable to undertakings' conduct in exercise of intellectual property rights pursuant to provisions of laws and administrative regulations relating to intellectual property rights; but this Law is applicable to undertakings' conduct that eliminates or restricts competition by abusing their intellectual property rights," the key to define an abuse of IPRs is whether the concerned behavior will actually bring anti-competitive effects to the relevant market involved. It is also the case when applying the "essential facilities" doctrine in the IP-related antitrust litigations.

It is a pity that the Ningbo Intermediate People's Court in the *Hitachi Metals Case* did not provide a detailed assessment of anti-competitive effects having been created by the HML's refusal to license to demonstrate why the "essential facilities" doctrine was applied in the case of HML. It has been argued that the real market conditions of sintered NdFeB business during the litigation proceedings can be a good supporting material to conduct such assessment which might have been neglected by the Ningbo Intermediate People's Court in the *Hitachi Metals* Case.

From the assessment above, it can be revealed that the anticompetitive effects of refusal to license IPRs should not only be the simple summarization of the monopolistic effects of a given exercise of IPRs legally entrusted by IPR laws. Additional conditions, having actual effects of eliminating or severely restricting market competition have to be satisfied. Moreover, when rendering its final judgment, the SPC should consider avoiding the risks of abusive application of the "essential facilities" doctrine to jeopardize its protection of IPRs, so as to render the clauses of AML an empty shell.

III. CONCLUSION

From a deep glance into the recent judicial practices in relation to the interaction of IP and antitrust, it is observed that Chinese courts have formed a basic framework to examine and determine the monopoly agreements in the scenario of settlement agreements. Scrutiny on cartels under the disguise of IP activities has been increasingly reinforced. Although the case of *Huawei v. IDC* clarified a boundary for SEP holders' legitimate licensing, it is less clear that how far antitrust will go to constrain the rights of non-SEP holders. Controversies mainly lie in that the

8 *IMS Health GmbH & Co OHG v. NDC Health GmbH & Co KG*, [2004] E.C.R. I-5039.

9 *United States v. Colgate*, 250 US 300, 39 S. Ct. 465 (1919).

10 *Id.*

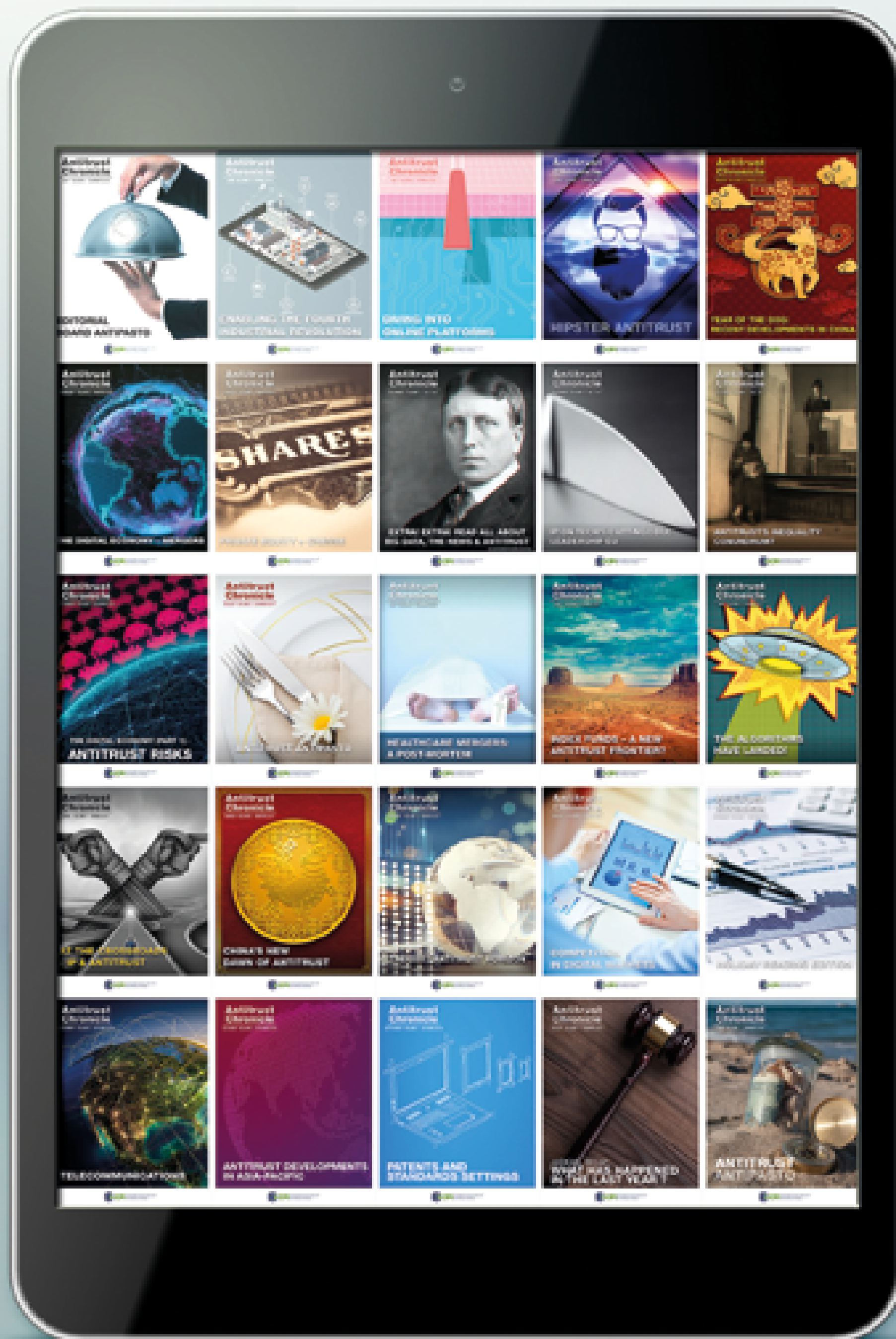
over intervention from the antitrust perspective may weaken the IP incentivized innovation in the long run. In particularly, the extended application of the "essential facilities" doctrine in the IP field aroused a lot of debates worldwide. Indeed, a sound balance between IP and antitrust is not an easy mission in any jurisdiction of the world. With the emerging application of the Internet of Things and smart cars in China and worldwide, it is foreseeable that Chinese courts will face increasing disputes with the feature of intersection between IP and antitrust. Because the revision of the AML in 2022 added "encouraging innovation" as one of the aims of the AML, the significance of this topic becomes more remarkable. Chinese courts will have to face such challenges and to properly respond to disputes of this kind, thus it is meaningful to keep a watchable eye on Chinese evolving judicial practices on the vibrant interaction of IP and antitrust.

CPI COMPETITION POLICY™ INTERNATIONAL

CPI Subscriptions

CPI reaches more than 35,000 readers in over 150 countries every day. Our online library houses over 23,000 papers, articles and interviews.

Visit competitionpolicyinternational.com today to see our available plans and join CPI's global community of antitrust experts.



CPI COMPETITION POLICY™ INTERNATIONAL