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A critical reflection on the ‘Public Interest Exemption’ in China’s merger control regime

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ABSTRACT

The Anti-Monopoly Law (AML) in China allows the responsible authority for merger control to consider not only the competition interest but also other public interest reasons when it reviews a takeover or merger. Where the responsible authority considers that the benefits of a takeover or merger to the public interest outweigh the harms to competition, it may ‘exempt’ the transaction. This ‘public interest exemption’ has never been formally applied since the introduction of the law in 2008. One explanation for this can be found in the ambiguity of the law: there are no legal provisions that clarify the public interest considerations. A second explanation is that China did not establish a separate review procedure for this public interest exemption. In practice, some approval decisions made by the enforcement authority led to confusion, as it was unclear whether the transactions were ‘exempted’ for public interest reasons or for industrial policies. This article reflects on the role of the public interest exemption in China. By drawing lessons from the past and examining the public interest exemption regime in Germany, it aims to provide suggestions for future reforms, against the background of the promulgation of the Amendment to the AML in 2022.

KEYWORDS: Merger control, Competition interest, Public interest, National security, China, Germany

JEL CLASSIFICATIONS: K21

I. INTRODUCTION

Takeovers and mergers may generate both positive and negative effects on efficiency, consumer welfare, and market competition. It is for that reason that jurisdictions around the world have introduced ex ante merger control in their competition law regimes. In their assessments of takeovers and mergers, jurisdictions do not only focus on the effects on competition, but also take into account other non-competition factors. So-called ‘public interest

the national security review regime in China. As to the foreign takeovers that are subject to a security review, the Security Review Notice 2011 only covers (i) foreign takeovers that are in the defence sectors and related to defence security, and (ii) foreign takeovers aiming to obtain actual control of the domestic entities in the sectors of agriculture, energies and resources, infrastructure, transportation, key technology, and the manufacture of major equipment.³⁷ The Measures for the Security Review extend the application scope of security review by incorporating foreign investors' investments which result in the acquisition of the actual control of enterprises in sectors of important cultural products and services, important information and internet products and services, and important financial services.³⁸ With regard to the considerations to take into account in the security review, the Security Review Notice 2011 requires that the influence of a foreign takeover on the following aspects should be scrutinized: (i) on the national defence security, (ii) on the stable operation of the national economy, (iii) on the basic social life order, and (iv) on the research capacity of the crucial technologies pertaining to national security.³⁹ The above rules show that the national security interest in China's merger control regime does not only refer to the defence security but also reaches out to other economic and social aspects in foreign takeovers. Regarding the second question, the national security review runs parallel to the merger control procedure. Under the Measures for the Security Review, the Office of the 'foreign investment security review working mechanism' (Security Review Office) is responsible for the security review in foreign takeovers.⁴⁰ Foreign investors or their related parties of investments falling within the scope of a security review should proactively report to the Security Review Office before making the investment,⁴¹ and the Security Review Office will conduct a two-stage review procedure (general review and special review) of the investment.⁴²

To conclude, 'national security' constitutes an important consideration that the AML aims to protect and the public interest nature of it becomes clear from the general objectives of the law (in Article 1), the recognition of the crucial position of State-controlled economy in security-related sectors (in Article 8), and the required national security review of foreign takeovers (in Article 38). On the one hand, according to Article 34 AML, in theory, the Enforcement Department II may exempt an anti-competitive takeover or merger if it regards that the national security interest is overriding in this transaction; and where the Security Review Office finds that the foreign takeover has or may have impact on national security in a security review, it, according to Article 38 AML, may decide to prohibit the transaction which has gone through the merger control. On the other hand, the scope of factors relating to 'national security' (as specified by the relevant screening regulations for foreign direct investment (FDI)) goes beyond the potential scope of the 'public interest' (as indicated by the context of Article 1 and Article 34 AML, which exclude the competition and other economic factors). This difference further shows the ambiguity in the definition of 'public interest' under the AML and implies the challenge in confining the public interest exemption to purely non-competition considerations in China's merger control practice.

³⁷ Security Review Notice 2011 (n 34) art 1.

³⁸ Measures for the Security Review (n 36) art 4(1)(2).

³⁹ Security Review Notice 2011 (n 34) art 2.

⁴⁰ Measures for the Security Review (n 36) art 3. The Security Review Office is located in the NDRC, under the leadership of both the NDRC and MOFCOM.

⁴¹ *ibid*, art 4.

⁴² *ibid* arts 8–9.

III. PROBLEMS IN IMPLEMENTING THE PUBLIC INTEREST EXEMPTION PROCEDURE: IS THERE A SEPARATE PUBLIC INTEREST REVIEW UNDER THE AML?

Relevant procedural rules in the AML

According to Article 26 and Article 30⁴³ AML, the anti-monopoly enforcement authority should first conduct a preliminary review of a concentration of undertakings which reaches the threshold level as set by the State Council and where the undertakings concerned make a declaration to it.⁴⁴ If it decides to conduct further review after the preliminary review, a second-stage review must be completed within 90 days since such decision is made (which is subject to a maximum extension period of 60 days).⁴⁵ In the second-stage review, the enforcement authority should make the decision whether to prohibit the concentration and inform the undertakings concerned.⁴⁶ Thus, in theory, it is at this stage that the responsible authority may decide whether to implement the public interest exemption in Article 34. Nevertheless, it is unclear from the AML whether there is a separate public interest review procedure which is independent of the merger control review at this stage, and (if yes) whether such exemption review should be initiated subject to the application by undertakings of the concentration concerned.

At first sight, Article 34 may give the impression that there is a two-step review procedure: in the first step the enforcement authority should review the concentration's effect on competition and decide whether it eliminates or restricts competition (merger control review); and in the second step there is a separate public interest exemption review, meaning that where such (potential) negative effects are found, the enforcement authority should then decide whether to exempt the concentration for other public interest reasons. However, comparing this with the relevant rules under the GWB, which establishes a typical two-step review procedure for merger control and public interest exemption, it can be observed that the AML does not actually establish such a separate public interest exemption review system.

The German two-step review procedure

Section 42(1) of the GWB allows the Minister of the Federal Ministry for Economic Affairs and Climate Action (BMWK)⁴⁷ (the Minister) to authorize a concentration of undertakings which has been prohibited by the Federal Cartel Office (BKartA) if its restraint to competition is outweighed by 'advantages to the economy as a whole' resulting from the concentration, or if the concentration is justified by 'an overriding public interest'. When reviewing a concentration of undertakings, the BKartA considers only the effects on competition of the concentration.⁴⁸ A decision based on the competition criteria closes the merger control

⁴³ The original art 25 AML before the amendment.

⁴⁴ The Amendment 2022 added two paragraphs to art 26 which empower the enforcement authority to require declaration from the undertakings concerned where the concentration does not reach the threshold but there is evidence showing that it has or may have the effect of eliminating or restricting competition, and to review the concentration where the undertakings concerned fail to make such declaration according to this article.

⁴⁵ AML (n 1) art 31 (the original art 26 AML before the amendment). The Amendment 2022 added a new article to the AML (art 32) stipulating the circumstances in which the enforcement authority may suspend the periods for the review.

⁴⁶ *ibid.*

⁴⁷ Before December 2021, the responsible authority was the 'Federal Ministry for Economic Affairs and Energy (BMWi)'. With the change of responsibilities subject to Organisationserlass des Bundeskanzlers Olaf Scholz, the Federal Ministry for Economic Affairs and Energy (BMWi) was renamed 'Federal Ministry for Economic Affairs and Climate Action (BMWK)' in December 2021. See Bundesministerium für Wirtschaft und Klimaschutz (BMWK), 'Bundesministerium für Wirtschaft und Energie (BMWi) "heißt jetzt" Bundesministerium für Wirtschaft und Klimaschutz (BMWK)' (1 February 2022) <<https://www.exist.de/EXIST/Redaktion/DE/Aktuelles/Nachrichten/Wichtige-Mitteilung-fuer-alle-EXIST-Projekte.html>> last accessed 15 December 2022.

⁴⁸ GWB (n 9) s 36. See J Busche and A Röhling, *Kölner Kommentar zum Kartellrecht* (Carl Heymanns 2014) 330.

The NDRC did not publish detailed reasoning for its decision in this case. This takeover caused controversy because a national security review was conducted in the retail sector, where Yonghui and Zhongbai conduct their major businesses. Normally the retail sector is not regarded as a security-sensitive sector. It is neither closely related to the defence interest nor regarded as the frontier of technology development. It is also hard to consider the retail sector as bearing crucial importance for national economy or the social life order. From this case, it could be observed that the scope of sectors and industries as relevant to national security, the public interest nature of which is implied in the relevant provisions of the AML (Articles 1, 8, and 38), is hard to predict in China's merger control practice.

The merger between China CNR Corporation Limited and China South Locomotive and Rolling Stock Corporation Limited: the protection of SOEs

In March 2015, MOFCOM unconditionally approved the merger between China's two State-owned train manufacturers—the China CNR Corporation Limited (CNR) and the China South Locomotive and Rolling Stock Corporation Limited (the China CSR).⁷⁰ After the merger, the China CRRC Corporation Limited (CRRC) was established and became a super-giant in both domestic and international railway transportation equipment market.⁷¹

Before the merger, the CNR and the China CSR together already controlled China's domestic rolling stock market.⁷² In the international market, in 2010, the CNR ranked third and the China CSR ranked first in the world's top 10 largest manufacturers of new rolling stock;⁷³ between 2011 and 2014, the CNR and the China CSR ranked first and second respectively among the world's rolling stock suppliers for consecutive years before the merger.⁷⁴ The two companies claimed that the merger aimed to achieve synergy effects, increase the R&D capability in high-technology, improve the competitive advantages, and promote Chinese high-end equipment manufacturing to go further into the world.⁷⁵ According to an officer of the State-owned Assets Supervision and Administration Commission of the State Council (SASAC), before the merger, there were serious competition problems between the two companies, particularly by lowering their offer price to win the market overseas.⁷⁶ The market regulators worried that the continuation of such situation would incrementally impede the Chinese companies' competitiveness in the international market.⁷⁷ Professionals from the SASAC suggested that the synergy effects gained from the merger would largely strengthen the companies' capacity in the R&D of high-technology and

⁷⁰ See MOFCOM, 'List of Cases of the Unconditionally Approved Concentrations of Undertakings of the First Quarter of 2015' (3 April 2015) <<http://fldj.mofcom.gov.cn/article/zcfb/201504/20150400932418.shtml>> last accessed 15 December 2022.

⁷¹ Liu, 'The Defence of Public Interest in Anti-competitive Concentration of Undertakings' (n 7) 124; See the news about this merger at Xiaoting Lin, 'The China CSR and CNR Merged into the CRRC' *Xinhuanet* (31 December 2014) <http://www.gov.cn/xinwen/2014-12/31/content_2798737.htm> last accessed 15 December 2022.

⁷² See the relevant data at 'Shares of CNR, CSR Surge after Merger Announcement' *Xinhuanet* (31 December 2014) <https://www.chinadaily.com.cn/business/2014-12/31/content_19208682.htm> last accessed 15 December 2022; Macquarie Research, 'China CNR Corp: The Other Twin Brother' (26 June 2014) <http://pg.jrj.com.cn/acc/Res/HK_RES/STOCK/2014/6/26/1efc5efd-629a-420a-a040-4427e3428ebb.pdf> last accessed 15 December 2022; Economist Intelligence, 'Assessing Mega-mergers through the CSR-CNR Lens' (6 September 2016) <http://country.eiu.com/article.aspx?articleid=944580878&Country=China&topic=Economy_1> last accessed 15 December 2022.

⁷³ David Briginshaw, 'CSR Tops the Rolling Stock League, But Can It Stay There?' *International Railway Journal* (20 April 2012) <<https://www.railjournal.com/rolling-stock/csr-tops-the-rolling-stock-league-but-can-it-stay-there/>> last accessed 15 December 2022.

⁷⁴ CRRC, 'CRRC Corporation Limited: 2015 Annual Results Announcement' (29 March 2016) <https://www.crccgc.com/Portals/250/pdf/CRRC_AR2015.pdf> last accessed 15 December 2022.

⁷⁵ Lin (n 71).

⁷⁶ Ye Yang and Bin Zhang, 'Merger Between China CSR and CNR Expected to be Finished in June' *Economic Information* (26 March 2015) <http://dz.jckb.cn/www/pages/webpage2009/html/2015-03/26/content_3624.htm> last accessed 15 December 2022. See also Lujing Zhang, 'Academician Said That the Merger between the China CSR and CNR Should Have Taken Place Earlier: Vicious Competition Caused Overseas Buyers to Doubt Chinese Technology' *PEOPLE.CN* (4 November 2014) <<http://politics.people.com.cn/n/2014/1104/c1001-25968923.html>> last accessed 15 December 2022.

⁷⁷ Zhang (ibid).

environmental protection (the achievement of environmental objectives of the Federal Government), as a general objective stipulated in Article 20a of the Constitution (Grundgesetz), belonged to the overriding public interest.⁸⁸

Secondly, in addition, the Minister also recognized that in principle, the following considerations were exemption reasons under section 42 GWB, which is different from the ambiguous situation in China:

- a) *preservation of important know-how*: the Monopolies Commission held that, to be recognized as a public interest, the preservation of the know-how caused by the merger must have a particularly high value for society.⁸⁹
- b) *strengthening of international competitiveness*: section 42(1) of the GWB explicitly provides that the international competitiveness of the merging entity is a public interest consideration that has to be taken into account in the Ministerial Authorization. The Monopolies Commission held that 'the company size is not a prerequisite for international competition',⁹⁰ and emphasized that 'the primary protection objective of the GWB is domestic competition and therefore improving international competitiveness should, in principle, be regarded as secondary'.⁹¹ It clearly illustrated that 'improving the international competitive position of a company is to be interpreted restrictively by the law, that is, it must be demonstrated in concrete terms that the company cannot survive in the long term without the merger on international markets'.⁹²
- c) *retention of the employment rate in the region*: the Monopolies Commission admitted that 'in principle, general public has a special interest in maintaining and safeguarding jobs'.⁹³ The Minister and the Monopolies Commission applied rigid criteria in assessing this argument in individual cases. For example, they held that, instead of an anti-competitive merger, 'other socially and competitively viable solutions (such as funds from social, regional or structural policy) should be first sought for to solve unemployment problems'.⁹⁴ Besides, the Monopolies Commission assessed whether the employment effect brought by the merger would last in the long term, and insisted that restrictions on competition were justified by the preservation of jobs only if the latter could avoid long-term structural unemployment.⁹⁵ Moreover, the Monopolies Commission often compared the unemployment rate of the region affected by the merger with the average unemployment rate of a wider region (usually the average national rate) to assess the quantitative weight of the problem and the urgency to solve the problem through the merger.⁹⁶ In some cases, it also compared the prevalence of unemployment among certain occupational groups.⁹⁷
- d) *protection of societal interests in the healthcare area*: in principle, the Monopolies Commission admitted that the achievement of healthcare policy objectives, the expansion of the research focus of medicine, and the significant improvements of the level of

⁸⁸ See the Special Report of E.ON/RUHRGAS para 158.

⁸⁹ See the Special Report of Miba/Zollern para 147.

⁹⁰ See the Special Report of THYSSEN/HÜLLER-HILLE para 53.

⁹¹ See the Special Report of E.ON/RUHRGAS para 192.

⁹² *ibid.*

⁹³ See the Special Report of THYSSEN/HÜLLER-HILLE para 43, the Special Report of MAN/SULZER para 52 and the Special Report of Uniklinikum Greifswald/Kreis Krankenhaus Wolgast para 130.

⁹⁴ See the Special Report of THYSSEN/HÜLLER-HILLE para 43 and the Special Report of MAN/SULZER para 52.

⁹⁵ See the Special Report of THYSSEN/HÜLLER-HILLE para 43.

⁹⁶ See eg Table 10 in the Special Report of THYSSEN/HÜLLER-HILLE; Tables 17 and 18 in the Special Report of VAW/KAISER/PREUSSAG.

⁹⁷ See the Special Report of THYSSEN/HÜLLER-HILLE para 49.

