Coca-Cola/Huiyuan: First Chinese Prohibition Decision under New Merger Control Rules

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On March 18, 2009, China's Ministry of Commerce ("MOFCOM") blocked Coca-Cola's planned acquisition of China Huiyuan Juice Group Limited ("Huiyuan") in the first prohibition decision adopted under the Chinese Anti-Monopoly Law (the "AML"), which entered into force in August 2008. Among other things, MOFCOM found that the transaction would have restricted competition in the Chinese fruit juice market, leading to increased fruit juice prices and reduced variety of products offered. This case has been closely watched as an indication of MOFCOM's approach to foreign companies' acquisitions of well-known Chinese companies.

I. THE FIRST PROHIBITION DECISION UNDER THE AML

According to MOFCOM's press release regarding the decision, MOFCOM has received 40 notifications of concentration and accepted 29 as complete since the AML took effect in August 2008. MOFCOM has completed its review of 24 transactions, of which 23 have been unconditionally cleared and one (Inbev/Anheuser-Busch) was approved subject to conditions. *Coca-Cola/Huiyuan* is the first transaction to have been prohibited under the AML. Since MOFCOM is only obliged to publish prohibition and conditional clearance decisions, *Coca-Cola/Huiyuan* is also only the second merger decision published under the AML.

II. PROTRACTED REVIEW PROCESS

Coca-Cola's proposed acquisition of Huiyuan was announced on September 3, 2008, and Coca-Cola filed its pre-merger notification on September 18, 2008. At MOFCOM's request, Coca-Cola supplemented the filing four times before it was considered complete, on November 19, 2008. The statutory review period began on November 20, 2008. After the initial 30-day review period, MOFCOM opened the 90-day second phase proceeding.

III. THE DECISION

In its decision, MOFCOM identified the following adverse impacts from the proposed transaction:

- Coca-Cola would be able to leverage its dominant position in the carbonated soft drink market to the fruit juice drink market, eliminating and restricting competition from current juice manufacturers and in turn damaging the lawful interests of juice consumers. Although the decision did not indicate how Coca-Cola could leverage its position in carbonated soft drinks, MOFCOM's press release referred to the possibility that Coca-Cola could engage in tying, bundling or other forms of exclusive dealing.

- Coca-Cola's market power on the juice market would be significantly enhanced by controlling two famous juice brands, *i.e.* "Meizhiyuan" (Minute Maid) and "Huiyuan." The transaction would significantly raise entry barriers for potential competitors in the fruit juice drink market.

- The transaction would reduce the space available to domestic small and medium-sized juice manufacturers and reduce the possibility for domestic enterprises to compete and independently innovate in the fruit juice drink market.

- The transaction would have adverse impacts on the competitive landscape in the Chinese fruit juice drink market and would not be good for the sustainable and healthy development of the Chinese juice industry.

- MOFCOM apparently considered claimed efficiencies, since the decision refers to the effects of the transaction on technological advances and on consumers. However, MOFCOM determined that the parties failed to provide sufficient evidence to prove that the positive impact of the transaction on competition would outweigh the negative impact or that the transaction "conformed to the requirements of social and public interests."

MOFCOM requested Coca-Cola to put forward viable solutions to problems that emerged in its examination, but Coca-Cola's proposed remedies were considered insufficient.

IV. IMPLICATIONS

A. PROCEDURE

MOFCOM's review of the *Coca-Cola/Huiyuan* transaction reveals several procedural aspects of significance to multinationals notifying transactions in China:

- MOFCOM may require a significant amount of supplemental information before accepting a notification as "complete" and starting its review period. Just as pre-notification consultations with the European Commission are an essential part of the notification process in the European Union, notifying parties must allow for this preliminary period in their timetables for review and approval of transactions notified in China, especially since merger notifications in China are suspensory.

- MOFCOM interprets the review periods under the AML to refer to calendar days, not business days, resolving an ambiguity in the text of the law.

- While MOFCOM has long had a practice of meeting with notifying parties and holding informal meetings with third parties to collect information, the decision indicates that MOFCOM sought written comments and held site visits and more formal meetings and hearings in its investigation of the *Coca-Cola/Huiyuan* transaction. MOFCOM also involved Chinese partners of Coca-Cola and consulted outside legal, economics and agricultural experts.

- The decision confirms that MOFCOM will take efficiencies into account, but the notifying parties bear the burden of showing that efficiencies outweigh the adverse effect on competition, if any.

B. SUBSTANTIVE REVIEW

The implications of *Coca-Cola/Huiyuan* for MOFCOM's substantive appraisal of high-profile transactions under the AML are less clear, but potentially more significant than the procedural implications:

- The decision is short, and MOFCOM's analysis is less clear and complete than comparable decisions under the EC Merger Regulation. Notably, the decision does not describe how MOFCOM defined the relevant market or discuss the market shares of the parties or their competitors or whether the parties are close competitors.

- More generally, the decision does not articulate a clear theory of harm that would justify prohibition of the transaction. The decision's reference to leveraging suggests that MOFCOM applied a conglomerate effects theory of the kind abandoned many years ago in the United States and applied by the European Commission only rarely, cautiously, and in situations where the evidence has been compelling.

- Although MOFCOM's spokesman stressed that non-competition law considerations played no role in the decision, the decision's references to the transaction's effect on domestic small and medium-sized manufacturers and the sustainable and healthy development of the Chinese fruit juice drink industry suggest that industrial policy considerations did in fact play a significant role. If so, MOFCOM's approach could be consistent with the AML requirement that MOFCOM take account of the "development of the national economy" and "other considerations that may affect market competition as identified by the AML enforcement authority." In this regard, MOFCOM may have been influenced by recent publicity in China regarding the alleged negative effect of foreign acquisitions on prominent national brands, such as *Mininurse*, *Nanfu* and *Lebaishi*.

- Both *Coca-Cola/Huiyuan* and *InBev/Anheuser-Busch* evidence MOFCOM's willingness to use the merger control process to address future, non-merger-specific conduct. In *InBev/Anheuser-Busch*, MOFCOM required the parties to refrain from specified, future acquisitions to prevent further consolidation of the Chinese beer market. Here, MOFCOM expressed concern that Coca-Cola might leverage its existing position in carbonated beverages in the fruit juice market. Although the Chinese authorities would have the power under the AML to address such future transactions or conduct if and when the need arose, MOFCOM preferred to impose conditions on or prohibit notified transactions to avoid the risk of such future anti-competitive conduct or transactions.

C. REMEDIES

The decision indicates that Coca-Cola proposed remedies that MOFCOM judged insufficient. According to press reports, MOFCOM asked Coca-Cola to divest the Huiyuan brand as a condition to approval. Such a divestiture would represent a second form of remedy acceptable to MOFCOM, in addition to the restrictions on future acquisitions imposed in *Inbev/Anheuser-Busch*.

The decision, as supplemented by press reports regarding the negotiation of remedies in *Coca-Cola/Huiyuan*, suggests that, from a procedural perspective, MOFCOM appears to take a flexible approach to remedies. MOFCOM apparently took the initiative of proposing remedies to Coca-Cola, and there is no suggestion in the decision or in press reports that the submission of remedies was subject to particular formal or timing requirements, as in the EU. From a substantive perspective, the decision implied that remedies under the AML need only "alleviate," as opposed to "removing," the anti-competitive effects of the transaction. This interpretation is consistent with the AML, but more flexible than the draft implementing rules published by MOFCOM in January 2009.

V. CONCLUSION

As the first prohibition decision under the AML, *Coca-Cola/Huiyuan* is a landmark in the evolution of Chinese merger control. In view of the lack of any clear theory of harm and speculation that the decision was politically motivated, however, it is questionable how reliable the decision will be as an indication of MOFCOM's substantive merger analysis. That MOFCOM would consider the broader implications of notified transactions should perhaps not be surprising, since the AML explicitly requires MOFCOM to take broad economic factors into account. Nonetheless, MOFCOM's decision may give pause to Western companies considering acquisitions of high-profile Chinese companies, particularly companies with prominent local brands.

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