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China Proposes Merger Reporting Thresholds in Draft Rules

The State Council, through its Legal Office, is soliciting comments on the definition of "concentration" and the thresholds for reportable transactions under the PRC Anti-Monopoly Law (the "AML") and published the Rules on Notification of Business Concentration (Draft for Comments) (the "Rules"). The actual Rules will take effect on August 1, 2008, together with the AML, and will supersede the current reporting thresholds under the Regulations on Mergers and Acquisitions of Domestic Enterprises by Foreign Investors (the "M&A Rules").

Under the draft circulated for comments, the concept of control has been introduced to the definition of "business concentration". Anti-monopoly filings are required when there is a merger or an acquisition of "control" over another business. "Control" is not merely the acquisition of shares of over 50% of a target company but includes the right to appoint the majority of the directors on the board or exert decisive influence on the production and operational decisions of another business by contract or other means. This potentially expands the scope of filings and will impact those investments utilizing the indirect "nominees" structure.

On reporting thresholds, the draft Rules define the significance of a transaction by measuring the business of more than one party to the transaction, and potentially reduce the filing requirements. The following business concentrations now require filings:

- (i) the combined worldwide revenue of all parties to the business concentration in the prior fiscal year exceeds RMB 9 billion AND the PRC revenue of each of at least two parties exceeds RMB 300 million;
- (ii) the combined PRC revenue of all parties to the business concentration in the prior fiscal year exceeds RMB 1.7 billion AND the revenue of each of at least two parties in the PRC exceeds RMB 300 million; or
- (iii) the business concentration will result in the market share of the parties to the business concentration in the PRC exceeding 25%.

These Rules, as drafted, represent significant improvement from the M&A Rules as under the M&A Rules, PRC reporting obligations can be triggered by the significant presence of an acquirer's business in the PRC alone, whether in an inbound acquisition or in an offshore acquisition, regardless of the significance of the target's business in the PRC or worldwide. Now reporting obligations will only arise under the revenue-based tests if each of at least two parties to a business concentration has PRC revenue in excess of RMB 300 million.

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