

Competition & Trade Update

In China

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Recent pollution control developments in China for electrical and electronic equipment – “China RoHS”

The term “RoHS” originated with an EU Directive — the Restriction of Hazardous Substances Directive (or RoHS) — which restricts the use of 6 hazardous materials¹ in the manufacture of various types of electronic and electrical equipment. It has been in effect since 1 July 2006.

Since the EU RoHS became effective on 1 July 2006, seven Chinese Ministries have jointly published the China RoHS — “Administrative Measures on the Control of Pollution Caused by Electronic Information Products” — effective since 1 March 2007. The China RoHS is similar to the EU RoHS in its purpose, the types and Maximum Concentration Values (“MCV”) of the restricted hazardous substances², although slight differences exist between the scope of application, method of implementation, etc.

The China RoHS Regulation requires that its measure be implemented in two regulatory steps:

Step 1 requires Chinese producers and importers of Electronic Information Products (EIPs) to label and mark EIPs according to a Chinese national standard³. This step has been well implemented since 1 March 2007. Step 1 also recommends that designers and producers

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¹ The restricted hazardous substances under the EU RoHS include lead (Pb), mercury (Hg), cadmium (Cd), hexavalent chromium (Cr6+), polybrominated biphenyls (PBB) and polybrominated diphenyl ethers (PBDE).

² China is actually applying the same six substances and the Maximum Concentration Values as those in the EU.

³ Marking Standard, SJ/T11364-2006.

of EIPs use technology and materials which are non-toxic or have low toxicity, harmless or cause low levels of harm, degrade easily, can be conveniently recycled, and are otherwise good for environmental protection.

While Step 1 of the Chinese RoHS has been well implemented for years, Step 2 has not yet been implemented. The original plan of the Step 2 is to publish a consolidated “key-Catalogue of EIP”⁴, which contains a full list of electronic information products that cause the most concerns.

According to this plan, Chinese designers, producers, sellers and importers of the Key-Catalogue EIPs must either:

- replace products with hazardous substances, or
- meet MCV requirements for restricted substances.

Also, compulsory certification must be obtained before the Key-Catalogue EIPs enters the Chinese market.

Recently, the Chinese government has envisaged revising the China RoHS regime, and in particular the implementation of Step 2. In July 2010, the “Draft Administrative Measures for the Control of Pollution caused by Electrical and Electronic Products”—the new China RoHS—was published by the Chinese Ministry of Industry and Information Technology and was notified to the World Trade Organization for public comments.

Based on the draft regulation, significant revisions of China RoHS are expected. Among other things, the key revisions will be:

- Coverage of products will be fine-tuned, as the new China RoHS is expected to apply to “Electrical and Electronic Products” instead of the current “Electronic Information Products”. According to the draft regulation, “Electrical and Electronic Products” refers to “equipment and its accessories which work with a voltage rating of at most 1500 volts for direct current and 1000 volts for alternating current”.
- The originally-planned “key-Catalogue EIPs” will be published in several batches. At this point, the Chinese government has only

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⁴ This catalogue, however, has never been officially published.

published the first batch of the list, which includes mainly computers, TV, and mobile phones.

- The requirements of Compulsory Certification (“CCC”) will be replaced by a so-called “Voluntary Certification” which is “promoted and supervised” by the Chinese government (see further comments below).

Industry watchers expected the new China RoHS to be published by mid -2011, but legislative work was delayed. In the meantime, various detailed regulations are expected to be published which relate to the implementation of the “Key Catalogue” and “Voluntary Certification”. It seems that the new China RoHS regime will not be established until the new detailed regulations are well in place.

Importantly, MNCs who produce, trade, or import electronic products in China no longer have to obtain compulsory certification for specific products that in the categories on the new list. The product can be placed on the market without compulsory certification. But the producer, trader, or importer must himself guarantee that if the product contains specific hazardous substances, the concentration is within the permissible MCV.

Also important to note is that a new system of “voluntary certification promoted by the State” will replace the compulsory certification system. Although literally a “voluntary” program, the term implies that the program is strongly recommended and might be under the surveillance of the government. Before the detailed regulation on the implementation of the “voluntary certification” is published, many manufacturers are concerned that such voluntary certification might become a de facto compulsory program when it is actually implemented.

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Remedies Imposed on the Seagate/Samsung Transaction in China

In its decision of 12 December 2011, China’s Ministry of Commerce (“MOFCOM”) conditionally approved Seagate’s acquisition of Samsung’s hard drive (“HDD”) business (“Transaction”). Its decision differs from that of the U.S. Federal Trade Commission (“FTC”) and the European Commission (“EC”) who both approved the Transaction unconditionally.

MOFCOM's reasoning was that the Transaction would exclude and restrict competition on the HDD market. MOFCOM therefore imposed remedies on the Transaction which we focus on below.

MOFCOM's Remedies

Thinking that the Transaction will exclude and restrict effective competition on the HDD market, MOFCOM required Seagate to make the following commitments ("Commitment"):

- Maintain Samsung as an independent competitor on the HDD market.

MOFCOM specified measures that Seagate must take to keep Samsung as an independent "competitor" in this market. They are:

- ▶ Set up an independent subsidiary to take over Samsung's HDD business;
 - ▶ Continue Samsung's existing sales;
 - ▶ Set up a firewall to prevent the exchange of information on competition between Seagate and Samsung's sales teams;
 - ▶ Keep Samsung's production line operating independently;
 - ▶ Establish an independent pricing mechanism for Samsung; and
 - ▶ Create an independent R&D center for Samsung products, with technical support by Seagate.
- Maintain and expand the production capacity of Samsung's products.
 - Do not force clients to enter into exclusive purchase agreements on hard disk products with Seagate or companies it controls.
 - Do not force TDK China Co. Ltd. to exclusively supply hard disk heads to Seagate or companies it controls, or limit the number of hard disk heads supplied by TDK China Co. Ltd. to other hard disk manufacturers.
 - Maintain investment in the R&D to promote innovation.
 - Appoint an independent authorized supervisor to monitor Seagate's performance of these Commitments.

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Note that MOFCOM has allowed Seagate to apply for release from Commitment (1) and (2) after it has implemented MOFCOM's requirements for one year.

Comments on MOFCOM'S Remedies

Under the implementing regulations⁵ of the Anti-Monopoly Law ("AML Rules"), MOFCOM may impose remedies - either structural, behavioral, or a combination - on a case-by-case basis. Structural remedies include the divestiture of assets or businesses, while behavioral remedies include granting access to infrastructure such as networks or platforms, licensing key technologies, and terminating exclusive agreements by the undertakings.

In the Seagate/Samsung Transaction, MOFCOM requested that Seagate should establish an independent subsidiary to take over Samsung's HDD business to maintain the independence of Samsung products.

Notwithstanding the requirement for Seagate to create a new subsidiary, we note that this remedy in Commitment (1) does not match the definitions of behavioral or structural remedies in the AML Rules because:

- Seagate will be the investor of the newly established subsidiary;
- Seagate has to make commitments to keep this subsidiary an "independent" competitor on the market; and
- Seagate has to expand and develop Samsung's relevant products in the future.

Therefore, in general, it is more a behavioral remedy with an effect equivalent to what a structural remedy (divestiture) would achieve.

A similar (but different) case is Boeing/McDonnell Douglas in the EU. The EC found that the takeover by Boeing of one of its main rivals in aircraft manufacture on the world market would strengthen its existing dominant position. It proved impossible to find third parties of sufficient commercial stature to acquire the McDonnell Douglas' business, so that

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⁵ Measure for the Undertaking Transaction Examination, which took effect on 1 January 2010.

finally the conditions agreed by Boeing involved not disposals, but acceptance that, among others:

- It would guarantee customer support to all purchasers of McDonnell Douglas' aircraft of the same quality as that given to its own customers;
- It would not enter into any additional exclusive arrangements with airlines for a 10 year period, and would not enforce certain existing exclusive agreements; and
- It would license certain patents to third parties on a non-exclusive basis.

There is speculation on MOFCOM's reasons for choosing this particular remedy in addition to those it has already expressed. Some experts comment that because the FTC and EC have already cleared the Transaction, and the EC imposed a divestiture remedy in the Western Digital/Hitachi merger⁶, MOFCOM is inclined to a softer approach. Other experts insist that MOFCOM focused more on protecting the interests of Chinese consumers, and imposed remedies that achieve that result.

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⁶ The Western Digital notified the EC its proposed acquisition of Hitachi one day later than Seagate/Samsung notification. Then the Western Digital/Hitachi transaction was examined by the EC in the light of the Seagate/Samsung deal.

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