Update China Desk
China Law Brief

08/2012
English Version

From Practice of China's Merger Control: Wal-Mart, e-Commerce, Value-added Telecommunication Services and VIE

Dr. Yiliang Dong, LL.M.

Since 2010, foreign investors are allowed to sell their own goods and products through direct online distribution in China, while direct online distribution of goods of third parties is still subject to approval. Other value-added telecommunications services ("VATS") are still limited to foreign investment and subject to approval.

On 13 August 2012, the Chinese Ministry of Commerce ("MOFCOM") announced its conditional approval of an acquisition by the American company Wal-Mart Store Inc of control over a Chinese online supermarket Shanghai Yishiduo e-Commerce Co., Ltd. ("Yishiduo"). In this transaction, Wal-Mart acquired through indirect share purchase the control over an offshore company which conducts the control over Yishiduo based on the contractual arrangement.

Due to the limited access for foreign investors and the unclear legal basis of the so-called "variable Interest Entity" (VIE), which will be discussed in the following, the areas of e-Commerce in China and VATS are extremely sensitive issues. For this reason, the recent decision of MOFCOM is not only relevant in the sense of competition law, but also with regard to the regulation of foreign investment.

According to MOFCOM Yishiduo operates the largest online supermarket in China. The company has two main business areas: Direct online distribution and value-added telecommunications services. The transaction of Wal-Mart by the indirect acquisition of control only relates to Yishiduo's business area of online direct distribution. MOFCOM defines the B2C online direct distribution market as the relevant product market and the Chinese market as the relevant geographic market. It analyzed the transmission of the competitive advantages of Wal-Mart's business to Yishiduo online direct distribution through this proposed acquisition of control. However, MOFCOM did not have competition doubt regarding the direct online distribution market.

Moreover, MOFCOM reviewed also the market of VATS, the second business division of Yishiduo, which is, however, not included in this transaction. In its decision, MOFCOM ran a hypothetical analysis, claiming that the Chinese VATS market would be restricted or distorted, if Wal-Mart would gain access to this market indirect through the business division of Yishiduo. Correspondingly, MOFCOM imposed, mainly in this respect, the three conditions under which the transaction has been approved: 1) The transaction must be limited solely to the direct online distribution through its own internet sales platform, 2) Without prior approval, Wal-Mart may not provide any VATS to third parties, and 3) Wal-Mart may not operate the VATS of Yishiduo by means of a VIE structure.

From the competition perspective, this decision of MOFCOM is odd and incomprehensible. However, the background is that foreign investors have only limited access to the Chinese VATS market and therefore many foreign investors try to circumvent this regulation by means of VIE structure. The VIE is a business structure that allows an investor, without being in possession of the majority of shares, exercise on the control over other entity by means of contractual arrangement.

Anyway, the decision of MOFCOM is still questionable, i.e. to prevent Wal-Mart from indirect access to the VATS market by coupling a competition assessment with a regulatory review. MOFCOM would have hold back with the insinuation of a possible circumvention of sector specific regulation by Wal-Mart and had better carry out an *ex post* supervision. After all, the access to VATS market and the VIE structure are sector specific regulatory issues which are not directly relevant to competition law.

Dr. Yiliang Dong, LL.M.
董一梁 （法学博士/律师）
Attorney-at-Law PRC (Lü Shi)
China Desk
Heuking Kühn Lüer Wojtek
Tel: +49 (40) 35 52 80-29
Fax: +49 (40) 35 52 80-80
Email: yiliang.dong@heuking.de

Your Contact: „China Desk“

in cooperation with

Global Law Office (Beijing, Shanghai, Shenzhen) ◆ www.globallawoffice.com.cn

CHINA DESK

Please find out more information about our China Desk on our website under

http://www.heuking.de/en/about-us/international/china-desk.html

INFORMATION

- **We will be glad to receive your any comments or suggestions. Please contact us via email: china-desk@heuking.de.**
- **This Newsletter "*Update China Desk*" does not constitute legal advice. While the information contained in this Newsletter has been carefully researched, it only offers a partial reflection of the law and its developments. It can be no substitute for individual advice appropriate to the facts of an individual case.**
- **This Newsletter is sent as a group email. To unsubscribe to this newsletter, please write to: china-desk@heuking.de.**