

MOFCOM's Conditional Approval for Western Digital's Acquisition of Hitachi's Hard Disk Drive Business

On 2 March 2012, the Ministry of Commerce of People's Republic of China ("**MOFCOM**") announced its decision to approve the acquisition of the hard disk drive ("**HDD**") business of Viviti Technologies Ltd., formerly known as Hitachi Global Storage Technologies Ltd. ("**Hitachi**"), by Western Digital Corporation ("**Western Digital**"), subject to the divestiture of production assets and several behavioural remedies. This follows MOFCOM's decision in Seagate/Samsung in the same market. In their parallel assessment of the Western Digital/Hitachi transaction, the EU and U.S. antitrust authorities raised similar competitive concerns and also ordered the divestiture of the production assets. However, MOFCOM went further and ordered Western Digital to hold Hitachi separate for at least the next two years, which demonstrates once more MOFCOM's increased confidence and its willingness to apply a harsher regime than other authorities. After seven months Western Digital withdrew and resubmitted its notification with MOFCOM's consent, thereby causing the review deadlines to start over again and leading to a review procedure that lasted eleven months in total from initial notification.

Competition assessment

To a large extent the competitive assessment is the same as in the Seagate/Samsung decision. MOFCOM defines a separate HDD market with a global dimension. This market is already highly concentrated and transparent, and further characterized by product homogeneity, innovation and significant entry barriers. MOFCOM concludes that the transaction would have a negative impact on competition and the welfare of Chinese consumers because it would reduce competitive pressure in general and innovation in particular and increase the likelihood of coordination among the remaining players. The combination of Western Digital and Hitachi would result in a market share of 47% compared to 43% for Seagate/Samsung and 10% for Toshiba. MOFCOM mentions the parallel Seagate/Samsung transaction, however, pointing out that according to its decision Seagate and Samsung remain independent competitors for the time being.

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Remedies

To address its concerns, MOFCOM imposed the following remedies:

- > Western Digital shall divest Hitachi's 3.5-inch HDD production assets to a third party within six months;
- > Hitachi's HDD business shall be operated as an independent competitor with respect to, in particular, R&D, procurement, production and sales, safeguarded by firewalls between their respective teams (however, Western Digital and Hitachi may cooperate on R&D after MOFCOM's approval);
- > Western Digital and Hitachi shall reasonably determine capacity and output based on market demands;
- > Western Digital and Hitachi shall not materially change their current business models and shall not force customers to buy products exclusively from them;
- > Western Digital and Hitachi shall maintain the momentum of R&D investment of recent years; and lastly,
- > Western Digital shall appoint a monitoring trustee to supervise the performance of the above remedies.

Western Digital may apply to MOFCOM for a release from its obligations under the remedies (ii) and (iii) above after two years. The application must set out the progress of implementation of the decision, the reasons for such release, and the relevant evidence.

Commentary

Not for the first time MOFCOM requires stricter remedies than other competition authorities notwithstanding the global nature of the markets, thereby demonstrating its increased confidence and willingness to reach and impose its own conclusions. The decision is also remarkable with regards to various substantive and procedural aspects.

First, as in Seagate/Samsung MOFCOM obliges the acquirer to hold the entire target separate, with review only possible after the longer period of at least two years. When Western Digital applies for a review of this obligation, it is unclear which legal standards and procedural framework MOFCOM will apply. The decision only refers to the evidence brought forward in the application and the competitive situation in the market at the time of the review. It is unclear whether this will entail another lengthy procedure equivalent to a normal merger investigation. It might be argued that the decision is more akin to a prohibition than a clearance as for the time being Western Digital is not allowed to take control. While it remains to be seen whether the rationale of the transaction is thereby put into question, Western Digital already signalled that *"[c]ompliance with these undertakings may limit*

synergies that could otherwise be achieved and involve significant costs or require changes in business practices that result in reduced revenue.”¹

Secondly, the remedies go beyond what MOFCOM imposed in the parallel Seagate/Samsung investigation. In that case there was no divestiture obligation and the hold separate was imposed for a minimum of only one year. MOFCOM, like the EU and U.S. authorities, appears to have concluded that the loss of Hitachi as an independent competitor would be more detrimental to competition than the loss of Samsung. In view of the extensive hold separate remedy, the additional divestiture obligation seems redundant. However, at the time of MOFCOM's decision, Western Digital had already agreed to sell the respective assets to Toshiba thereby complying with the European Commission's earlier decision of November 2011.

Thirdly, it is interesting to see the different approaches of competition authorities when reviewing two parallel transactions within the same market. In accordance with its established policy, the European Commission analysed Seagate/Samsung, which was notified first, independently, i.e. ignoring the intended acquisition of Hitachi by Western Digital. In contrast, for the review of the Western Digital/Hitachi transaction, it took the pending combination of Seagate and Samsung already into account (with an obvious disadvantage to the second notified transaction). The FTC assessed both transactions assuming that the other transaction will go ahead. In contrast, MOFCOM analysed both transactions as if the other one has not (yet) taken place. This approach – besides avoiding a race to be the first to notify (EU) and the uncertainty whether the transactions will be completed (U.S.) – seems understandable in view of the hold separate obligations imposed on the acquirer in both cases.

Finally, the case demonstrates that in difficult cases involving remedy discussions, MOFCOM's review may even be extended beyond the already lengthy deadlines if the initial notification is withdrawn and resubmitted. Such an approach is not available before the European Commission after opening of the in-depth investigation (Phase 2). This could jeopardise the predictability of the statutory deadlines if it is habitually used as a device to gain more time.

For MOFCOM's decision, please click [here](#) for the Chinese version and [here](#) for the English translation.

¹ Press release of 8 March 2011, cf. www.wdc.com/en/company/pressroom/releases.aspx?release=96593e40-7be2-4ebf-ad35-68cf58ab194d.

For MOFCOM's Seagate/Samsung decision, please click [here](#) for our commentary of December 2011, [here](#) for the Chinese version of the decision and [here](#) for the English translation.

Author: None

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