



POLICY ROUNDTABLES

The Failing Firm Defence

2009

Introduction

The OECD Competition Committee held a roundtable discussion on the Failing Firm Defence in October 2009. This document includes an executive summary and the documents from the meeting: an analytical note by Anne-Layne Farrar, Jorge Padilla, and Henri Piffaut for the OECD, written submissions from Belgium, Canada, Chile, Denmark, France, Germany, Ireland, Japan, Korea, New Zealand, Poland, Spain, Switzerland, Turkey, the United Kingdom, the United States, Israel, the Russian Federation, South Africa, Chinese Taipei, the European Commission and BIAC, as well as an aide-memoire.

Overview

The failing firm defence has arisen infrequently in merger cases but is expected to be used more frequently in the current economic climate. The FFD exists in most OECD jurisdictions and exempts an otherwise anticompetitive merger from challenge under the competition laws if the target company is in such poor financial condition that its only other option would be to exit the relevant market. Topics included the elements of proof for the FFD, the question of whether they should be made more lenient during economic downturns, and the special case of mergers between financial institutions. The delegates expressed doubt that there was any need to make adjustments to the approach taken toward the FFD during economic crises. They generally agreed that the burden of proof for the FFD should remain on the merging parties. Jorge Padilla of LECG was the guest speaker.

Related Topics

Failing Firm Defence (1996)
Enhancing the Role of Competition in the Regulation of Banks (1998)
Mergers in Financial Services (2000)
Competition and Financial Markets (2009)
Exit Strategies (forthcoming 2010)

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COMPETITION COMMITTEE**

ROUNDTABLE ON FAILING FIRM DEFENCE

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FOREWORD

This document comprises proceedings in the original languages of a Roundtable on Failing Firm Defence held by the Competition Committee in October 2009.

It is published under the responsibility of the Secretary General of the OECD to bring information on this topic to the attention of a wider audience.

This compilation is one of a series of publications entitled "Competition Policy Roundtables".

PRÉFACE

Ce document rassemble la documentation dans la langue d'origine dans laquelle elle a été soumise, relative à une table ronde sur l'entreprise défaillante qui s'est tenue en octobre 2009 dans le cadre du Comité de la concurrence.

Il est publié sous la responsabilité du Secrétaire général de l'OCDE, afin de porter à la connaissance d'un large public les éléments d'information qui ont été réunis à cette occasion.

Cette compilation fait partie de la série intitulée "Les tables rondes sur la politique de la concurrence".

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EXECUTIVE SUMMARY

By the Secretariat

Considering the discussion at the roundtable, the delegates' written submissions and the Secretariat's background paper, several key points emerge:

- (1) *The failing firm defence (FFD) may arise more frequently during financial and economic crises.*

During economic crises such as the one that most OECD countries are currently experiencing, more firms may find themselves in financial difficulty. Some financially distressed companies will seek to improve their condition by merging with healthier competitors. Competition agencies may therefore face an increasing number of merger reviews involving financially troubled firms, some of which may be true failing firms while others may simply be weak competitors. In some of the cases, parties may put the FFD forward as an argument in favour of approving their transaction.

- (2) *The basic conditions required for a successful application of the FFD are relatively similar across countries.*

A merger that is expected to lead to anti-competitive effects should be prohibited when there is a causal link between the merger and the anticipated harm to competition. When one of the merging firms is 'failing' (i.e. it is likely to exit the market absent the merger), the future deterioration in competitive conditions does not necessarily result from the transaction and hence the causal link may be missing. In some circumstances, the post-merger scenario may be less anti-competitive than a counterfactual scenario in which the failing firm exited the market. In those cases, mergers involving failing firms should be approved even when the post-merger scenario is less competitive than the pre-merger scenario.

Although there are small differences between the approaches adopted by different competition authorities when applying the FFD, they all require three cumulative conditions before accepting a failing firm defence:

- Absent the merger, the failing firm will exit the market in the near future as a result of its financial difficulties;
- There is no feasible alternative transaction or reorganisation that is less anti-competitive than the proposed merger; and
- Absent the merger, the assets of the failing firm would inevitably exit the market.

The burden of proof to show that these conditions are fulfilled lies on the merging parties. They should convince the competition authority that the merger will lead to less anti-competitive effects than a counterfactual scenario in which the firm and its assets would exit the market.

One notable difference among jurisdictions is that some consider whether the failure of the firm and the liquidation of its assets could be a less anticompetitive alternative to the merger since the remaining firms in the market might compete for both the failing firm's market share and the assets that otherwise would have been transferred entirely to one purchaser. In particular, there is presently a difference of views between the stated policies of some national European competition agencies and the European Commission. The Commission has moved away from the requirement that absent the merger all the failing firm market share should accrue to the acquirer, but several EU countries have not yet reflected this change in their policies. The low frequency of the FFD and the gradual development of policy through case law may explain the lag.

- (3) *Not all countries have a formal FFD, but those that do have one consider it to provide legal certainty.*

A few countries do not have explicit failing firm defences. In these countries, mergers involving a failing firm are reviewed using the standard causality test in merger control. If applied properly, such a test would identify those transactions that should be approved despite their anti-competitive effects. However, such an approach may be difficult and costly to administer and may lead to less predictable outcomes. Those countries with an explicit FFD have found that (a) it yields outcomes that are broadly similar to the outcomes that would obtain under the properly applied traditional causality test and (b) it provides predictability for firms that are subject to merger control regimes.

- (4) *Failing division defences should be subject to standards that are similar to the FFD standards, but that are applied differently in light of factual differences between failing divisions and failing firms.*

In some instances, the merger under review involves the acquisition of a firm's division. In those cases, the merging parties may argue that the exit of that particular division from the market would occur (i) whether or not the merger materialises and (ii) irrespective of the financial health of the parent company. While most countries are open to the application of this so-called failing division defence (FDD), competition authorities should be aware of the possibility that parent companies may employ creative accounting methods to establish the illusion of a failing division. A division that is not currently profitable will not necessarily exit the market imminently. The losses may be temporary, and in any event the division may be important enough to the parent company that it would be unlikely to exit even if the losses continue. It may be difficult to assess the amount of money that the parent would invest in the division absent the merger, though. Consequently, parties should be required to produce clear evidence that, without the merger, the division would be likely to fail and its assets would be likely to exit the market imminently.

- (5) *The FFD criteria should not be relaxed in times of crisis. There may, however, be some room for streamlining the FFD review process.*

As of October 2009, competition authorities had not seen an increase in the number of mergers in which the parties claimed the FFD. This may be because there is a perception that the FFD criteria are too strict. That raises the question whether competition authorities should loosen the FFD criteria, particularly in light of the current global economic crisis. The consensus among the Committee delegates was that there is no justification for such a change. There are other policy

instruments (e.g. bankruptcy law and State aid) available to help failing firms through the crisis. Competition authorities are concerned that excessively lax standards may lead to too many type II errors, i.e. false negatives.

Nevertheless, competition authorities recognise that FFD investigations may be too lengthy, which is problematic given that the position of firms in distress may rapidly deteriorate, which in turn may cause inefficient liquidations. This may justify procedural changes to ensure a speedier review of mergers involving failing firms.

- (6) *Whereas not all delegates agreed that mergers involving financial institutions deserve special treatment, they did agree that systemic risk considerations should be taken into account in merger proceedings.*

Banks are special economic agents because of their importance for the stability of the financial system and the economy. The collapse of one key bank may have a domino effect that leads to widespread loss of confidence in the financial system and thus to a severe economic recession.

All countries acknowledge the importance and the special role of banks in their economies. Even so, while some countries do not consider that mergers involving failing financial institutions should be treated differently, others are prepared to treat mergers amongst financial institutions more leniently when bank failure is a possibility. Those against the special treatment of bank mergers argue that competition authorities should focus on promoting and preserving competition and leave prudential regulation to the Central Bank.

Some competition agencies argue that it may be more difficult to succeed with a FFD in mergers involving banks. This is because they anticipate that governments may intervene with some kind of financial support in order to prevent the failing bank from leaving the market. In other words, they consider that the assets of failing banks are unlikely to exit the market in practice.

SYNTHÈSE

par le Secrétariat

Compte tenu des débats ayant eu lieu au cours de la table ronde, des contributions écrites soumises par les délégués et du document de référence du Secrétariat, plusieurs points clés ont été mis en évidence :

- (1) *L'argument de l'entreprise défaillante est susceptible d'être évoqué plus fréquemment pendant les crises économiques et financières.*

Pendant les crises économiques telles que celle que traversent actuellement la plupart des pays de l'OCDE, davantage d'entreprises peuvent se trouver en difficulté sur le plan financier. Certaines de ces entreprises s'efforceront d'améliorer leur situation en fusionnant avec des concurrents plus solides. Les autorités de la concurrence risquent donc d'être confrontées à une multiplication des procédures de contrôle des fusions impliquant des entreprises en difficulté financière, dont certaines peuvent être réellement défaillantes, tandis que d'autres peuvent être simplement en situation de faiblesse face à la concurrence. Dans certains cas, les parties concernées peuvent mettre en avant l'argument de l'entreprise défaillante en vue de faire approuver leur transaction.

- (2) *Les conditions essentielles à remplir pour qu'il soit fait droit à l'argument de l'entreprise défaillante sont relativement similaires d'un pays à l'autre.*

Une fusion dont on escompte des effets anticoncurrentiels doit être interdite dès lors qu'il existe un lien de causalité entre la fusion considérée et l'atteinte à la concurrence anticipée. Lorsqu'une des entreprises parties à la fusion est « défaillante » (autrement dit, lorsqu'il est probable qu'elle sorte du marché si l'opération de concentration considérée n'a pas lieu), la dégradation future des conditions de concurrence ne résulte pas nécessairement de cette transaction, de sorte que le lien de causalité susmentionné peut être absent. Dans certaines circonstances, les effets anticoncurrentiels estimés peuvent être moindres dans le scénario de l'après-fusion que dans le scénario contrefactuel consistant en une sortie du marché de l'entreprise défaillante. Dans ce cas, les fusions impliquant des entreprises défaillantes doivent être approuvées, même si le jeu de la concurrence est présumé être plus limité après qu'avant l'opération de concentration considérée.

Malgré de légères divergences entre les approches adoptées par les différentes autorités de la concurrence pour évaluer l'argument de l'entreprise défaillante, elles exigent toutes pour y faire droit que trois conditions soient simultanément remplies :

- en l'absence de la fusion considérée, l'entreprise défaillante sortira du marché dans un avenir proche du fait de ses difficultés financières ;
- il n'existe pas d'autre transaction ou réorganisation envisageable qui soit moins anticoncurrentielle que la fusion proposée; et
- en l'absence de la fusion considérée, les actifs de l'entreprise défaillante sortiraient inévitablement du marché.

C'est aux parties à la fusion qu'il incombe de démontrer que ces conditions sont remplies. Elles doivent convaincre l'autorité de la concurrence que leur fusion aura des effets moins

anticoncurrentiels que le scénario contrefactuel suivant lequel l'entreprise et ses actifs quitteraient le marché.

Une différence notable d'une juridiction à l'autre tient à ce que certains prennent en compte le fait que la faillite de l'entreprise et la liquidation de ses actifs pourraient être une alternative moins anticoncurrentielle dans la mesure où les entreprises subsistantes pourraient être en situation de concurrence à la fois pour les parts de marché de l'entreprise défaillante et pour ses actifs qui autrement auraient été entièrement transférés à un seul acquéreur. En particulier, il existe une divergence de vues entre les politiques déclarées de certaines autorités de concurrence européennes et la Commission. La Commission s'est écartée de l'exigence selon laquelle en l'absence de fusion, toutes les parts de marché de l'entreprise défaillante devraient revenir à l'acquéreur mais plusieurs pays de l'Union européenne n'ont pas encore traduit ce changement dans leur politique. La faible fréquence du recours à l'argument de l'entreprise défaillante et le développement progressif de la jurisprudence peuvent expliquer ce décalage.

- (3) *Les pays ne reconnaissent pas tous formellement l'argument de l'entreprise défaillante, mais ceux qui le font estiment que cela constitue un facteur de sécurité juridique.*

Quelques pays ne reconnaissent pas explicitement l'argument de l'entreprise défaillante. Dans ces pays, les fusions impliquant une entreprise défaillante sont examinées sur la base de l'analyse de causalité classique employée dans le cadre du contrôle des fusions. Si elle est réalisée correctement, une telle analyse permet de cerner les transactions qui doivent être approuvées malgré leurs effets anticoncurrentiels. Néanmoins, une telle approche peut être difficile et coûteuse à mettre en œuvre, et peut déboucher sur des résultats moins prévisibles. Les pays reconnaissant explicitement l'argument de l'entreprise défaillante sont parvenus à la conclusion que (a) cela débouche sur des résultats peu ou prou similaires à ceux que l'on obtiendrait en procédant correctement à une analyse de causalité classique et (b) cela garantit une certaine prévisibilité aux entreprises assujetties aux régimes de contrôle des fusions.

- (4) *L'argument de la division défaillante devrait obéir à des critères similaires à ceux de l'argument de l'entreprise défaillante, mais appliqués différemment à la lumière de différences entre divisions défaillantes et entreprises défaillantes.*

Dans certains cas, la fusion examinée implique l'acquisition d'une division d'entreprise. Les parties à l'opération de concentration projetée peuvent alors faire valoir que cette division sortirait du marché (i) que cette fusion ait lieu ou non et (ii) indépendamment de la santé financière de la société mère. Si la plupart des pays considèrent comme recevable cet « argument de la division défaillante », les autorités de la concurrence devraient être au fait de la possibilité que les sociétés mères puissent recourir à des artifices comptables pour créer l'illusion d'une division défaillante. Une division qui n'est pas profitable ne sortira pas nécessairement du marché de manière imminente. Les pertes peuvent être temporaires, et en tous les cas la division peut être suffisamment importante pour la société mère pour qu'il soit improbable qu'elle sorte même si la perte perdure. Il peut être cependant difficile d'évaluer la somme d'argent que la société mère devrait investir dans la division en l'absence d'une fusion. Par voie de conséquence, les parties devraient être requises d'apporter une preuve claire que sans la fusion, la division échouerait probablement et que ses actifs sortiraient probablement du marché de manière imminente.

- (5) *Les critères d'examen de l'argument de l'entreprise défaillante ne doivent pas être assouplis en période de crise. Néanmoins, il peut être envisageable de simplifier la procédure d'examen de cet argument.*

Au mois d'octobre 2009, les autorités de la concurrence n'avaient observé aucune augmentation du nombre de fusions dans le cadre desquelles les parties invoquaient l'argument de l'entreprise défaillante. Cela tient peut-être au sentiment que les critères d'examen de cet argument sont trop stricts. On peut donc se demander si les autorités de la concurrence devraient assouplir ces critères, en particulier au vu de la crise économique mondiale actuelle. Le consensus qui s'est fait jour parmi les délégués du Comité est que rien ne justifie une telle modification. Il existe d'autres instruments d'action (tels que le droit de la faillite et les aides d'État) permettant d'aider les entreprises défaillantes pendant la crise. Les autorités de la concurrence craignent que des critères excessivement souples ne puissent déboucher sur un trop grand nombre d'erreurs de seconde espèce, c'est-à-dire de faux négatifs.

Néanmoins, les autorités de la concurrence reconnaissent que les investigations concernant l'argument de l'entreprise défaillante peuvent être d'une durée excessive, ce qui pose problème étant donné que toute entreprise en difficulté risque de voir sa situation se dégrader rapidement, ce qui peut ensuite déboucher sur des liquidations inefficaces. Cela peut justifier une révision des procédures visant à garantir un examen plus rapide des fusions impliquant des entreprises défaillantes.

- (6) *Si les délégués ne sont pas tous d'avis que les fusions impliquant des établissements financiers doivent faire l'objet d'un traitement spécial, ils s'accordent sur l'idée que les considérations de risque systémique doivent être prises en compte dans le cadre des procédures de contrôle des fusions.*

Les banques constituent des agents économiques particuliers, compte tenu de l'importance qu'elles revêtent pour la stabilité du système financier et de l'économie. L'effondrement d'un établissement bancaire clé peut avoir un effet domino débouchant sur une perte de confiance généralisée dans le système financier et, partant, sur une grave récession économique.

Tous les pays reconnaissent l'importance et le rôle particulier des banques dans leur économie. Cela dit, si certains pays ne considèrent pas que les fusions impliquant des établissements financiers défaillants doivent faire l'objet d'un traitement différent, d'autres sont disposés à faire preuve de davantage d'indulgence à l'égard des fusions entre établissements financiers en cas de risque de faillite bancaire. Ceux qui s'opposent à ce qu'un traitement spécial soit réservé aux fusions bancaires font valoir que les autorités de la concurrence doivent s'attacher à promouvoir et préserver la concurrence, et laisser la réglementation prudentielle à la banque centrale.

Certaines autorités de la concurrence estiment qu'il est sans doute plus difficile de faire valoir l'argument de l'entreprise défaillante dans le cadre des fusions bancaires. Elles anticipent en effet la possibilité que les pouvoirs publics interviennent en accordant une forme ou une autre d'aide financière pour empêcher la sortie du marché de la banque défaillante. En d'autres termes, elles jugent peu probable que les actifs des banques défaillantes sortent concrètement du marché.

BACKGROUND NOTE¹

By the Secretariat

1. Introduction

Merger control provisions aim to block or condition transactions that would substantially lessen (or significantly impede) competition as a result of an increase in the market power of the merging parties. A *sine-qua-non* condition for a competition authority to block or condition a transaction is the existence of a strict causal link between the transaction under assessment and the anticipated harm to competition. The failing firm defence applies to instances in which, while the anticompetitive effect of the merger is not disputed, there is no such strict causal link – *i.e.* situations where the markets affected by the merger will experience an increase in concentration and a significant lessening of competition whether or not the merger takes place.

The failing firm defence has been applied by competition agencies across the world since the inception of merger control, though in exceptional circumstances only. In the United States, the first case in which the failing firm defence was accepted was *International Shoe* in 1930.² The burden of proof was placed on the failing firm, which had to show that its “resources [were] so depleted and the prospect of rehabilitation so remote that it faced the grave probability of a business failure.”³ In the European Union, the first case in which this defence was invoked, although not accepted, was *Aerospatiale-Alenia/De Havilland* in 1991, just one year after the launch of EC merger control.⁴

Competition agencies have identified over time the precise criteria which need to be fulfilled before a firm can resort to the failing firm defence in merger control. The general consensus appears to be that failing firm defences should only be accepted when there is clear and cogent evidence that (a) competition will be weaker in the future and (b) the contemplated merger will not have an incremental distortionary effect on the competitive process. More precisely, competition agencies around the world have accepted a failing firm defence when the allegedly failing firm and its assets would exit the market in the near future if not taken over and there is no less anti-competitive alternative purchase than the proposed merger.

In times of financial and economic distress, many firms are likely to find themselves in financial trouble. In the United States, total bankruptcy filings (business and non-business) increased from 603,633 in 2006 to 847,141 in 2007 and rose further to 1,117,771 in 2008.⁵ A similar trend can be found in Europe.

¹ Prepared by Anne-Layne Farrar, Jorge Padilla and Henri Piffaut. The authors are economists at LECG Consulting. They wish to acknowledge the support of Ingrid Liedorp as well as the comments of Jeremy West and Joe Phillips. This paper does not reflect the views of LECG or any of its clients.

² *International Shoe v FTC*, 280 U.S. 291 (1930).

³ *Ibid.*, p. 302.

⁴ Case IV/M.053 *Aerospatiale-Alenia/de Havilland* OJ 1991, L334/42, para.31.

⁵ See bankruptcy statistics of American Bankruptcy Institute: http://www.abiworld.org/AM/Template.cfm?Section=Annual_U_S_Filings1&Template=/TaggedPage/TaggedPageDisplay.cfm&TPLID=62&ContentID=36294.

Standard & Poor's (S&P) estimates that the overall default rate could increase to as high as 11% in 2009, compared with an average rate of about 3% for the past 15 years.⁶ Also in Japan, company bankruptcies in December 2008 were approximately 25% higher than a year before.⁷

In many cases, the assets of failed companies have greater value if kept together than if liquidated piecemeal. Owners of those firms will try to keep them alive as ongoing concerns. However, failed firms may have no option other than selling the firm to a third party if they want to avoid liquidation when their creditors are unable or unwilling to renegotiate their claims, as is typically the case in a credit crunch. We should expect, therefore, an increase in the number of mergers involving financially distressed companies during a credit crunch. Those mergers can make perfect sense for both acquirers and targets in time of financial crisis. The question, of course, is whether they are harmful to consumers.

Some of those mergers would have been clearly unacceptable from a competition standpoint in normal times, when both acquirer and target remain financially healthy, but may not have a differential impact on the strength of competition when the target experiences severe financial distress. If so, prohibiting those mergers would constitute incorrect public policy. The question is whether the criteria for a valid failing firm defence, developed and applied during the days of the Great Moderation, are still relevant while we undergo the Great Recession. This appears to be an appropriate time to revisit the application of the failing firm defence in merger control.

The framework of analysis which currently underlies the failing firm defence policies of most OECD members has been subject to some criticism. First, it has been criticised because it leads to lengthy investigations which do not take into account that the position of firms in distress may rapidly deteriorate and result in inefficient liquidations. Second, it has been criticised for its allegedly overly rigid criteria which, especially in the context of tight credit markets, may cause the exit of assets from the market; assets which may be crucial to the economy for reasons of employment, innovation, export force or dependency in the overall industry value chain.

This paper provides an overview of the failing firm defence policies applied in various OECD jurisdictions. It assesses the effectiveness of current policies and evaluates whether they are equipped to deal efficiently with mergers taking place in the midst of a credit crunch. The paper also discusses options for reform.

Our main conclusions are:

- In times of financial and economic crisis, such as the one we are currently experiencing, more firms may find themselves in financial difficulty. Firms in financial distress will seek to safeguard their long-term survival possibly by merging with direct, healthier competitors.
- Competition agencies may thus face an increasing number of mergers involving firms in financial distress, some of which may be true failing firms while others may simply be weak competitors or flailing firms. In some of those cases, the failing firm defence may be put forward as an argument for the approval of the transaction.
- We have reviewed the failing firm defence policies of several OECD members. Those policies generally involve a number of strict conditions: the allegedly failing firm and its assets must exit

⁶ European bankruptcy laws - Out of pocket, *The Economist*, 30 December 2008. Available at www.economist.com/displaystory.cfm?story_id=12855376.

⁷ See "More firms go bankrupt in Japan". 13 January 2009. Available at: <http://news.bbc.co.uk/2/hi/business/7826009.stm>.

the market in the near future absent the merger and there must be no less anti-competitive alternative purchase than the proposed merger. It falls on the merging parties to demonstrate that those requirements are met. Given the high standard of proof, there are very few cases in which the failing firm defence has been invoked successfully.

- This paper addresses the question whether this state of affairs is desirable. We have seen that the criteria used to assess failing firm defences today is geared towards minimising type II errors – *i.e.* erroneous merger clearances or insufficient remedies – and may thus result in too many type I errors – *i.e.* erroneous prohibitions or excessive remedies. This because the current failing firm defence framework presumes that certain but-for scenarios, such as the permanence of a trimmed down and handicapped company in the market, are necessarily superior from a competitive perspective than the merger under review. Such a presumption is not always justified. So mergers may be blocked even when they represent the least anticompetitive option.
- We have also seen that a more effects-based approach focused on identifying the most likely counterfactual and comparing the outcomes of the post-merger scenario with those of such realistic counterfactual may lead to less type I errors though it makes type II errors more likely. An effects-based approach may also result in higher implementation costs and lengthier investigations. It may also be less predictable.
- OECD member states should consider whether the bias of the current failing firm defence policies is justified. Whether they decide to reconsider their current policies or not, there are some aspects of those policies that are difficult and others, such as the viability of the so-called failing firm defence, which are unclear. Competition agencies around the world should seriously consider issuing guidance on how they will analyse failing/failing firm/division defences.

The remainder of this paper is structured as follows. In Section 2 we review the policies towards the failing firm defence adopted in a number of OECD countries. In Section 3 we discuss the potential implications of the current financial crisis for the application of the failing firm defence in practice. In Section 4 we discuss the arguments in favour and against the adoption of a more lenient approach to mergers involving financially distressed companies. Finally, Section 5 concludes.

2. Existing FFD Policies

2.1 Introduction

In the previous section we have explained why the failing firm defence is the subject of renewed interest. In this section we review of the policies in place in several OECD jurisdictions. We also provide a comparison of the criteria that need to be fulfilled in different jurisdictions in order for the failing firm defence to be approved. Finally, we discuss the allocation of the burden of proof and the compatibility of existing failing firm defence policies with the fundamental principles of merger analysis.

2.2 Failing Firm Defence Policies in OECD Countries

OECD countries have incorporated the failing firm defence to their merger control policies in several different ways. In some jurisdictions it is explicitly discussed in merger guidelines. This is the case *inter alia* of the EU, Japan, the UK and the US. Other countries, such as Australia, do not formally incorporate the defence in their competition laws or their merger guidelines, but evaluate such arguments as part of their standard merger review process. This *ad hoc* approach has given rise to a body of case-law, which serves as the country's *de facto* failing firm defence policy. What seems to matter most from a policy perspective is whether there are specific criteria under which the defence will be assessed, not whether

those criteria are formulated in the competition statutes, in merger guidelines, or in the case law. In what follows, we review the policies of several OECD jurisdictions.

2.2.1 United States

The failing firm defence was first recognised by the US Supreme Court in *International Shoe* in 1930.⁸ The Court defined the first requirement of the defence as the liquidation of the firm absent the merger. The burden of proof was placed on the failing firm, which had to show that its “resources [were] so depleted and the prospect of rehabilitation so remote that it faced the grave probability of a business failure.”⁹ The Court furthermore prospectively assessed the strength of competition under two scenarios. In the first scenario the troubled firm was acquired by a competitor, whereas in the alternative scenario no merger took firm and the assets of the distressed company were liquidated. The Court concluded that the merger scenario was the least distortive option in that case.

Thirty years later in *Philadelphia National Bank*,¹⁰ the Supreme Court remarked that the defence could be more easily applied to the banking sector “due to the greater public impact of a bank failure compared with ordinary business failure”.¹¹ This ruling suggested that in considering failing firm defence arguments non-competition goals, such as financial stability, could play a role. It was not until the late 1960s, in *Citizen Publishing*,¹² that the Court first laid out the three requirements which should be met for the defence to be accepted: (1) The acquiring company must show that the target is in imminent danger of failure; (2) The failing firm must have no realistic prospect for successful reorganisation; and (3) The failing firm must show that it has made a reasonable, good faith attempt to locate an alternative buyer and there is no viable alternative purchaser that poses less anti-competitive risk.

The 1997 Horizontal Merger Guidelines published by the US Department of Justice and the Federal Trade Commission recognised that

*... a merger is not likely to create or enhance market power or to facilitate its exercise, if imminent failure, as defined below, of one of the merging firms would cause the assets of that firm to exit the relevant market. In such circumstances, post-merger performance in the relevant market may be no worse than market performance had the merger been blocked and the assets left the market.*¹³

The Guidelines list four conditions for a valid failing firm defence, which are consistent with the Supreme Court ruling in *Citizen Publishing*:

- The allegedly failing firm would be unable to meet its financial obligations in the near future;
- It would not be able to reorganise successfully under Chapter 11 of the Bankruptcy Act;

⁸ See note 2 *supra*.

⁹ *Ibid.*, p. 302.

¹⁰ *United States v Philadelphia National Bank*, 374 U.S. 321 (1963).

¹¹ Kokkoris, I. 2007. Failing firm defence under the Clayton Act. 28 *European Competition Law Review*, pp. 158-166.

¹² *Citizen Publishing Co v United States*, 394 U.S. 131, 138-139 (1969).

¹³ US Department of Justice and the Federal Trade Commission Horizontal Merger Guidelines as revised April 8, 1997, p. 5.0.

- It has made unsuccessful good-faith efforts to elicit reasonable alternative offers of acquisition of the assets of the failing firm that would both keep its tangible and intangible assets in the relevant market and pose a less severe danger to competition than does the proposed merger; and
- Absent the acquisition, the assets of the failing firm would exit the relevant market.¹⁴

Failed Division Defence

In some instances the merger under review involves the acquisition of a firm's division. In those cases, the merging parties may argue that the exit of that particular division from the market would occur (i) whether or not the merger materialises and (ii) irrespective of the financial health of the parent company. While there is no consensus among US courts, the 1997 Horizontal Merger Guidelines include a provision allowing the acquisition of a failing corporate division if the following circumstances are met: (a) the division has a negative cash flow on an operating basis; (b) there is evidence that, absent the acquisition, the assets of the division would exit the market in the near future; and (c) the owner of the failing division has made unsuccessful good-faith efforts to elicit reasonable alternative offers of acquisition of the assets of the failing division.¹⁵

"Flailing Firm" Defence

In 1974, the Court decided in *General Dynamics*¹⁶ to allow a 5 to 4 merger by considering that the target company's probable future ability to compete was severely limited. While acknowledging that the firm's competitive weakness did not meet the standard of proof for the failing firm defence, the Court nevertheless held that the acquisition would not substantially lessen competition.¹⁷ The *General Dynamics* decision became the "flailing," "quasi-flailing," or "weakened firm" defence and was first applied by the lower courts in *US v. International Harvester Co.*,¹⁸ where the court found that a planned acquisition did not violate the merger laws because the acquired company lacked the financial resources necessary to operate competitively. The flailing firm defence applies to situations where the target firm, while not in imminent danger of insolvency, is unlikely to represent a significant competitive constraint in the future, possibly due to its financial and/or economic weakness. Flailing firms are firms in financial distress which are unlikely to exit the market in the near future. Their long term prospects may actually be quite healthy and, therefore, they should be expected to be able to exert in the near future a competitive constraint, albeit possibly a rather feeble one, on other market players.

2.2.2 *European Union*

A failing firm defence was first considered by the European Commission in *Aerospatiale-Alenia/De Havilland*.¹⁹ The Commission did not accept the defence in that case as it considered that (a) De Havilland could remain an independent, efficient competitor on the market and (b) there could be other potential purchasers of De Havilland and those transactions would give rise to fewer, if any, competitive concerns.²⁰

¹⁴ *Ibid.*, p. 5.1.

¹⁵ *Ibid.*, p. 5.2.

¹⁶ *United States v General Dynamics Corp.* (1974) 415 U.S. 486.

¹⁷ *Ibid.*, at 510 – 511.

¹⁸ 564 F.2d 769, 774 (7th Cir. 1977).

¹⁹ See note 4 *supra*.

²⁰ *Ibid.*, p. 31.

The first successful application of the defence in the EU was in *Kali und Salz*, 1993.²¹ In this case the Commission found that there was no strict causal link between the proposed merger and the anticipated loss of competition in the German market, since effects of equal magnitude would result absent the merger due to the exit of the target firm from the market. The Commission concluded that (1) the acquired undertaking would in the near future be forced out of the market if not taken over by another undertaking; (2) the acquiring undertaking would at any rate be the party to take over the market share of the acquired undertaking if it were forced out of the market; and (3) there was no less anti-competitive alternative purchaser.

The requirement that the acquiring firm should absorb all the market share of the failing firm in the absence of the merger was considered to be excessively restrictive by the French government in its appeal against the European Commission's decision. However, the Court of Justice of the European Communities upheld the Commission's failing firm defence analysis.²² The Court held that the purpose of the "absorption of market share" criterion was to ensure that there was no causal link between the deterioration of the market's competitive structure and the merger. In particular, the Court noted:

*The criterion of absorption of market shares, although not considered by the Commission as sufficient in itself to preclude any adverse effect of the concentration on competition, therefore helps to ensure the neutral effects of the concentration as regards the deterioration of the competitive structure of the market. This is consistent with the concept of causal connection set out in Article 2(2) of the Regulation.*²³

The Commission applied the *Kali und Salz* criteria in a restrictive manner for a long time. For example, in *Saint-Gobain/Wacker-Chemie/NOM* it concluded that Wacker-Chemie could find alternative solutions and that those alternatives had a smaller effect on competition.²⁴ Likewise, in *Blokker/Toys "R" US (II)* the Commission concluded that "[the requisite] lack of causality between the operation and its effects on the market [had] not been established," since it had not been shown that "the whole market share of Toys "R" US would go to Blokker."²⁵

The Commission did not accept any failing firm defence after *Kali und Salz* until 2001, where it cleared *BASF/Eurodiol/Pantochim*.²⁶ This decision represented an important step in the development of the defence in the EU. The "absorption of market share" criterion was considered to be too restrictive. The Commission stated that it was sufficient to show that the assets of the failing firm would inevitably exit the market absent the merger and that there was no less anticompetitive alternative to the merger.²⁷

²¹ Case IV/M308 *Kali und Salz/MdK/Treuhand*. OJ 1994 L186/30.

²² Joined cases C-68/94 *French Republic v Commission*; C30/95 *Société Commerciale des Potasses et de l'Azote (SCPA) and Entreprise Minière et Chimique (EMC) v Commission* [1998] ECR I-1375.

²³ *Id.* p. 116.

²⁴ Case IV/M.774 *Saint-Gobain/Wacker-Chemie/NOM*. OJ 1997 L247/1. For a discussion, see Kokkoris, I. 2006. Failing firm defence in the European Union: A panacea for mergers? 27 *European Competition Law Review* 2006, pp. 494-509.

²⁵ Case IV/M.890 *Blokker/Toys "R" US (II)*, OJ 1998 L316/1.

²⁶ Case COMP/M.2314 *BASF/Eurodiol/Pantochim*. OJ 2002 L132/45.

²⁷ *Ibid.*, p. 142.

The Commission's current position in connection with the defence can be found in its Horizontal Merger Guidelines,²⁸ where it states that it "may decide that an otherwise problematic merger is nevertheless compatible with the common market if one of the merging parties is a failing firm" provided that "the deterioration of the competitive structure that follows the merger cannot be said to be caused by the merger".²⁹ Acceptance of a failing firm defence requires establishing that

*First, the allegedly failing firm would in the near future be forced out of the market because of financial difficulties if not taken over by another undertaking. Second, there is no less anti-competitive alternative purchase than the notified merger. Third, in the absence of a merger, the assets of the failing firm would inevitably exit the market.*³⁰

Furthermore, the Guidelines clearly allocate the burden of proof in failing firm defence cases: "It is for the notifying parties to provide in due time all the relevant information necessary to demonstrate that the deterioration of the competitive structure that follows the merger is not caused by the merger."³¹

Failed Division Defence

The European Commission first considered a failing division defence in *Bertelsmann/Kirch/Premiere*.³² It analysed the merger under the criteria applied to failing firms but it set "particularly high standards".³³ This more restrictive approach was justified on a number of grounds, including the possibility that the parent company employs creative accounting methods to establish the illusion of a failing division. The merging parties could not convince the Commission of the lack of a causal link between the merger and the deterioration of the competitive structure and the failing division defence was rejected.

Failing Firm Defence

In *NewsCorp/Telepiu*,³⁴ the Commission also rejected a failing division defence. However, it cleared the merger by taking into account the economic realities of the sector. The Commission concluded that the acquired party was unlikely to be able to pose a very significant competitive threat in the future given its poor financial health. This decision has been read as giving rise to a failing firm defence not too dissimilar from that adopted in the US *General Dynamics* case.³⁵

In its investigation of the merger *KLM/Martinair*,³⁶ the Commission assessed the competitive constraints that Martinair would impose on KLM absent the merger. The Commission acknowledged that there was a high likelihood that Martinair's long-haul passenger operations would be discontinued in the near future in the absence of a merger with KLM.³⁷ It found that given Martinair's financial position,

²⁸ European Commission. 2004. Guidelines on the assessment of horizontal mergers under the Council Regulation on the control of concentrations between undertakings (2004/C 31/03).

²⁹ *Ibid.*, p. 89.

³⁰ *Ibid.*, p. 90.

³¹ *Ibid.* p. 91.

³² Case COMP/M.993 Bertelsmann/Kirch/Premiere. OJ 1999 L53/1.

³³ *Ibid.*, p. 71.

³⁴ Case COMP/M.2876 NewsCorp/Telepiu. OJ 2004 L110/73.

³⁵ See Caffarra, C et al. 2003. Merger to Monopoly. 11 *European Competition Law Review*, p. 625.

³⁶ Case COMP/M.5141 KLM/Martinair, OJ 2009 C 51/04.

³⁷ *Ibid.*, p. 163.

restructuring was not a realistic option³⁸ and that no alternative purchaser would be interested in taking over Maersk's 50% share in Martinair.³⁹ The Commission did not formally apply a failing division defence in this case. Nevertheless, it concluded that the merger-specific effects would be limited:

*Martinair's specific situation makes it likely that the competitive constraint exerted by Martinair will be eroded in the foreseeable future. From the above it can therefore be concluded that the merger-specific effects of the proposed concentration with respect to the parties' passenger air transport activities are likely to be limited.*⁴⁰

This decision seems to support the view that a failing firm defence is available in Europe provided the facts show that the merger constitutes the least anticompetitive solution for the failing firm's financial problems.

2.2.3 Australia

Australia has not formally incorporated a failing firm defence in its Trade Practices Act (section 50) or in the merger guidelines adopted by the Australian Competition and Consumer Commission (ACCC). However, "the failing firm argument may form an essential element of the counterfactual analysis in which the ACCC determines the likely nature of competition in the market absent the merger."⁴¹ Recently, the ACCC has adopted the defence in one of its merger decisions.⁴²

2.2.4 Canada

The Merger Enforcement Guidelines published by the Competition Bureau of Canada consider a firm to be failing if (i) it is insolvent or is likely to become insolvent; (ii) it has initiated or is likely to initiate voluntary bankruptcy proceedings; or (iii) it has been, or is likely to be, petitioned into bankruptcy or receivership.⁴³

The Competition Bureau assesses whether imminent failure is probable; whether alternatives exist to the proposed merger that would result in a materially greater level of competition; whether retrenchment or restructuring would prevent the firm's failure and enable it to survive as a meaningful competitor; and whether liquidation would result in a materially higher level of competition in a substantial part of the market relative to the merger.⁴⁴

The Guidelines also list the typical information that the Bureau may seek during the merger investigation to assess failing firm defences, which include financial documents, the position of the firm in the market and the firm's relationship with its creditors and suppliers.

³⁸ *Ibid.*, p. 166.

³⁹ *Ibid.*, p. 174. The other 50% was already in the hands of KLM pre merger.

⁴⁰ M.5141, p. 175.

⁴¹ Poddar, D. 2009. The global financial crisis – will it affect merger review? Article by Australian commercial law firm Mallesons Stephan Jacques. Available on 05-08-2009 at <http://www.mallesons.com/publications/2009/Jun/9918866w.htm>.

⁴² ACCC. 2009. Public competition assessment of 13 March 2009 in the case P & M Quality Smallgoods Pty Ltd - proposed acquisition of Hans Continental Smallgoods Pty Ltd.

⁴³ Competition Bureau Canada. 2004. Merger Enforcement Guidelines. September 2004, Part 9 – Failing firm.

⁴⁴ *Ibid.*

2.2.5 France

In *Moulinex*,⁴⁵ the *Conseil d'État* accepted the possibility of a failing firm defence under the following three criteria: (1) the firm in difficulty would rapidly exit the market if not taken over, (2) there is no alternative transaction with less harm to competition and (3) the exit of the firm would not be less harmful for consumers than the proposed acquisition. This decision concerned the acquisition of a firm in bankruptcy proceedings by its most direct competitor. The Ministry of Finance had cleared the transaction on the basis of the failing firm defence criteria stated in *Kali und Salz*.⁴⁶ The *Conseil d'État* annulled the clearance decision because it found that the Ministry of Finance had insufficient reasons for concluding that competitors could not have acquired some brands from the liquidated company, or could not have replaced the failing firm in the market in case of exit. In other words, the *Conseil d'État* concluded that conditions (2) and (3) had not been established.

2.2.6 Germany

The *Bundeskartellamt* accepts the failing firm defence in those merger investigations for which it can be shown that the merger is not the cause of the anticipated deterioration of competition. The following conditions have to be met in order to prove that such a causal link is absent:

- Absent the merger, the failing firm will exit the market (“*Sanierungsbedürftigkeit*”);⁴⁷
- There are no alternative purchasers for the failing firm which would pose a less severe threat to competition (“*Nachweis eines fehlenden alternativen Erwerbers*”);⁴⁸
- Absent the merger, the market share of the failing firm is expected to accrue in whole or to a considerable extent accrue to the acquirer anyway (“*Verstärkung auch bei Ausscheiden*”).⁴⁹

The conditions are identical to those applied under EC law prior to the European Commission’s *BASF/Eurodiol/Pantochim* decision. A recent case in which these criteria were applied is *LBK/Mariahilf*.⁵⁰ The merging parties were not able to convince the *Bundeskartellamt* that the three criteria were met.

2.2.7 Ireland

The Merger Guidelines published by the Irish Competition Authority discuss the failing firm defence. The criteria listed by the Competition Authority are as follows:

- The alleged failing firm must be unable to meet its financial obligations in the near future;
- No possibility exists that the firm will be successfully reorganised under the process of Examinership;

⁴⁵ Decision of Conseil d'État, Section du contentieux, of 6 February 2004, N°s 249262-252297-252350-252809, SOCIETE ROYAL PHILIPS ELECTRONIC et autres.

⁴⁶ See note 21 *supra*.

⁴⁷ Bundeskartellamt decision of 06-06-2007 in the case LBK/Mariahilf, B 3 - 85111-Fa-6/07, p. 235-253.

⁴⁸ *Ibid.*, p. 254-261.

⁴⁹ *Ibid.*, p. 262-267.

⁵⁰ *Ibid.*

- The firm has made good-faith and verifiable efforts to elicit reasonable alternative offers of acquisition that would keep its assets, both tangible and intangible, in the relevant market and be less of a threat to competition than the proposed merger.[...]; and
- Without the merger taking place, the assets of the failing firm would definitely exit the relevant market.⁵¹

The Guidelines note, however, that these conditions may “rarely be met in practice.”⁵²

2.2.8 Japan

The failing firm defence is set out in part IV of the Japan Fair Trade Commission’s (JFTC) merger guidelines.⁵³ The JFTC’s guidelines state:

*the possibility that the effect of the business combination may be substantially to restrain competition in a particular field of trade is usually thought to be small if a party to the combination has excess debt or is unable to obtain finance for working capital and it is likely to go bankrupt and exit the market in the near future, and it is difficult to find any business operator that can rescue the party with a combination that would have less impact on competition than the business operator that is the other party to the combination.*⁵⁴

In other words, the failing firm defence will be accepted when (a) the target firm will exit the market in the near future due to its financial difficulties (bankruptcy or severe financial distress); and (b) there is no less anti-competitive combination.

2.2.9 Korea

The failing firm defence policy of the Korean Fair Trade Commission (KFTC) requires merging parties to show that the failing firm’s assets are unlikely to be utilised in the absence of the merger and that it is unlikely that there a less anti-competitive merger is possible.⁵⁵

One merger in which the failing firm doctrine was successfully invoked is the acquisition of Kia by Hyundai. On the basis that Kia was deemed to be bankrupt and unable to recover, the acquisition was approved.⁵⁶ On the other hand, in SK Telecom’s acquisition of Shinsegi Telecom, the defence was invoked by the merging parties, but the KFTC did not consider that Shinsegi would realistically be forced out of the market, nor that its assets would be worthless unless it merged with SK Telecom.⁵⁷

⁵¹ Irish Competition Authority. 2002. Notice in respect of Guidelines for Merger Analysis. 16 December 2002, p. 5.17.

⁵² *Ibid.*, p. 5.17.

⁵³ Japan Fair trade Commission. 2007. Guidelines to application of the Anti-monopoly Act concerning review of business combination.

⁵⁴ *Ibid.*, Part IV, (8), A-B, pp. 32-33.

⁵⁵ Yun, M. 2002. Policies to Improve Monopolistic/Oligopolistic Market Structure. Korea Institute for International Economic Policy. Available on 16-09-2009 at: <http://unpan1.un.org/intradoc/groups/public/documents/APCITY/UNPAN014166.pdf>.

⁵⁶ *Ibid.*

⁵⁷ *Ibid.*

2.2.10 United Kingdom

Both the Office of Fair Trading (OFT) and the Competition Commission (CC) recognise the failing firm defence in their current merger guidelines:

*Failing firm claims are, in essence, ones that the target business will exit the market without the merger; any harm to competition should therefore not be attributed to the merger.*⁵⁸

*Where the CC considers that one of the firms would fail then the situation in the market without the merger may be similar to that which would result from the merger, and thus the merger itself may not lead to any significant changes in the extent of competition in the market.*⁵⁹

The OFT guidelines give two conditions that have to be met for a failing firm claim to be considered: (a) inevitable exit of the target business absent the merger and (b) no realistic and substantially less anti-competitive alternative.⁶⁰ The OFT specifies that “less anti-competitive alternative” outcomes can include a scenario where the target business fails and its assets are transferred to remaining players.

The CC guidelines also give two conditions to be met: (a) the firm is unable to meet its financial obligations in the near future and (b) the firm is unable to restructure itself successfully.⁶¹ The CC guidelines also give some examples of various circumstances that the CC will take into account. These include the possibility that the failing firm will be acquired by a different firm and consideration of how the market share of the failing firm would be divided among remaining players if it exits the market.

The OFT and the CC also recognise the failing firm defence in their recently released draft joint merger guidelines.⁶² The draft guidelines give three conditions that have to be met for a failing firm claim to be considered: (1) the inevitability of exit of the firm in question; (2) no substantially less anti-competitive alternative buyer for the firm; and (3) failure of the firm is not a substantially less anti-competitive outcome than the merger.⁶³

The failing firm defence has been invoked in mergers affecting the UK market, including First West Yorkshire,⁶⁴ Tesco/Kwik Save,⁶⁵ CDMG Group/Ferryways NV/Searoads Stevedores NV,⁶⁶ Homebase/Focus DIY,⁶⁷ Stagecoach/Eastbourne Buses/Cavendish Motor Services,⁶⁸ and HMV/Zavvi.⁶⁹

⁵⁸ Office of Fair Trading. 2008. Restatement of OFT’s position regarding acquisitions of ‘failing firms’. December 2008, p. 4.

⁵⁹ Competition Commission. 2003. Merger references: Competition Commission Guidelines. June 2003, p. 3.61.

⁶⁰ See note 58 *supra*, p. 10.

⁶¹ See note 59 *supra*, p. 3.62.

⁶² OFT/CC. 2009. Consultation document: Merger assessment guidelines. April 2009, p. 4.27.

⁶³ *Ibid.*, pp. 4.27-4.33.

⁶⁴ OFT decision of 26 May 2005, ME/1517/05 First West Yorkshire/Black Prince Buses - Anticipated acquisition by First West Yorkshire Limited of Black Prince Buses Limited.

⁶⁵ OFT decision of 11 December 2007, ME/3387/07 Tesco/Kwik Save - Anticipated acquisition by Tesco Stores Limited of five former Kwik Save stores (Handforth, Coventry, Liverpool, Barrow-in-Furness and Nelson).

⁶⁶ OFT decision of 24 January 2008, ME/3145/07 CDMG Group/Ferryways NV/Searoads Stevedores NV - Completed acquisition by the CdMG group of companies of Ferryways NV and Searoad Stevedores NV.

In *HMV/Zavvi* the OFT considered the proposed acquisition of Zavvi by HMV once Zavvi had entered into administration (*i.e.* bankruptcy). The OFT concluded that an acquisition by HMV did not create the realistic prospect of a substantial lessening of competition.⁷⁰ The OFT explicitly noted that Zavvi was unlikely to emerge from bankruptcy even in a re-organised form⁷¹ due to “difficult current economic and market conditions and the prohibitive level of investment required to turn around the Zavvi business”.⁷² It also found that there were no other realistic substantially less anti-competitive purchasers for Zavvi stores despite the marketing efforts of the administrator and respective landlords.⁷³ No other retailers operating in the same market as the parties had expressed interest.⁷⁴ For some of Zavvi’s stores a second potential purchaser was identified, however its offer was not realistic given its poor commercial terms and the short term nature of the purchaser’s business model.⁷⁵ Finally, the OFT concluded that competition would not be stronger if Zavvi’s assets exited the market.⁷⁶

In contrast, in *Stagecoach/Eastbourne Buses/Cavendish Motor Services* the CC’s provisional findings reject the failing firm defence proposed by the parties as there is no compelling evidence that the target firms are likely to exit the market in the immediate future.⁷⁷ Moreover, the CC considers that there are restructuring measures available to the failing firms which would enable them to restore their financial viability, and that purchasers other than Stagecoach are available.⁷⁸

2.3 *Comparison of Failing Firm Defence Policies*

As is obvious from the above discussion, the criteria under which a failing firm defence will be accepted are quite similar across OECD countries. Competition agencies require evidence that, absent the merger, the target firm will most likely be forced to leave the market in the near future. They demand a comparison of the competitive effects of the proposed merger with those of alternative transactions or of an organic reorganisation. They require evidence that the firm’s assets will inevitably exit the market in the absence of the merger. Finally, the burden of proof is placed on the merging parties.

Despite these similarities, however, there are also a number of differences. First, while in some jurisdictions, such as the EU and the US, it is explicitly stated that the exit of the failing firm must be caused by its financial difficulties, the cause of the target firm’s failure is not always explicitly stated as part of the requirements for a successful defence. In a number of European jurisdictions we find references

⁶⁷ OFT decision of 7 August 2008, ME/3427/07 Homebase/Focus - Completed acquisition by Home Retail Group plc of 27 stores from Focus (DIY) Ltd.

⁶⁸ Competition Commission’s provisional findings report of 06-08-2009: The completed acquisitions by Stagecoach Group PLC of Eastbourne Buses Limited and Cavendish Motor Services Limited, p. 6.3.

⁶⁹ OFT decision of 14 May 2009: ME/4036/09 Anticipated acquisition by HMV of 15 Zavvi stores.

⁷⁰ *Ibid.*, p. 53.

⁷¹ See note 69 *supra*, p. 33.

⁷² *Ibid.*, p. 36.

⁷³ *Ibid.*, p. 30.

⁷⁴ *Ibid.*, p. 43.

⁷⁵ *Ibid.*, p. 49.

⁷⁶ *Ibid.*, p. 52.

⁷⁷ See note 68 *supra*, p. 6.4.

⁷⁸ *Ibid.*, pp. 6.4-6.5.

to the “the rapid disappearance of the firm”,⁷⁹ “the cessation of operations”,⁸⁰ or “the short-term exit of the failing firm”,⁸¹ but no explicit reference to financial distress as the underlying cause of the failing firm’s exit. This may have significant implications if it opens the door to successful failing firm defences in declining industries experiencing overcapacity where mergers do not take place to keep the assets of financially distressed companies in the market but rather they seek an orderly and likely anticompetitive downsizing of the industry.

Second, there appear to be subtle differences in the counterfactual analyses required by different jurisdictions. All jurisdictions require the proposed merger to be compared against a counterfactual scenario with no merger and a counterfactual scenario where the failing firm is sold to an alternative purchaser. However, some jurisdictions also require explicitly showing that the anticompetitive effects of the merger will not be more severe than those that would follow from the reorganisation or restructuring of the failing firm.⁸²

Third, differences exist in the level of effort that failing firms are required to exert in order to elicit alternative, and possibly less anticompetitive, acquisition offers. Both the US (“unsuccessful good-faith efforts”⁸³) and Ireland (“good-faith and verifiable efforts”⁸⁴) require the merging parties to show that they undertook reasonable steps to elicit those alternative options. Other jurisdictions simply investigate the existence of such alternative transactions without a formal requirement on the failing firm to demonstrate that it contemplated, analysed and discarded other options. In practice the type of evidence demanded might be quite similar in different jurisdictions, considering that the burden of proof lies on the merging parties.

Finally, while, as explained above, the European Commission has moved away from the requirement that absent the merger all the failing firm market share should accrue to the acquirer, several EU countries have failed to reflect this change in their policies.⁸⁵ The development of policy through case law and the limited application of the failing firm defence may explain the lag. It seems, therefore, likely that these countries will update their policy and replace it with the new requirements as soon as the failing firm defence is invoked in a new case.

⁷⁹ Direction Générale de la Concurrence, de la Consommation et de la Répression des Fraudes (DGCCRF). 2007. Lignes directrices relatives au contrôle des concentrations; procédure et analyse, p. 444.

⁸⁰ Failing firm defence policy of the Hellenistic Competition Commission. See http://www.concurrences.com/rubrique.php3?id_rubrique=626&lang=en.

⁸¹ Decision of the Nederlandse Mededingingsautoriteit (NMa) on 12-05-2000 in case 1538 De Telegraaf – De Limburger, p. 226.

⁸² See for instance the policies of the UK (“the firm is unable to restructure itself successfully” - Competition Commission (2003) *op. cit.* at footnote 59, para. 3.62), Ireland (“No possibility exists that the firm will be successfully reorganised under the process of Examinership” - Irish Competition Authority (2002) *op. cit.* at footnote 51) and the US (“it would not be able to reorganize successfully under Chapter 11 of the Bankruptcy Act” – US DOJ and FTC (1997) *op. cit.* at footnote 13).

⁸³ See US DOJ and FTC (1997) *op. cit.* at footnote 13.

⁸⁴ See Irish Competition Authority (2002) *op. cit.* at footnote 51.

⁸⁵ For instance Bulgaria, Greece, Denmark, Switzerland, Italy and Greece did not yet replace the old criterion with the new one put forward in the Commission’s *BASF/Eurodiol/Pantochim* decision. See http://www.concurrences.com/rubrique.php3?id_rubrique=626&lang=en.

2.4 *Burden of Proof*

The criteria for a successful failing firm defence in all the jurisdictions reviewed above are very demanding and, consequently, the burden of proof placed on the merging parties is very high. The parties must show that the assets of the target firm would exit the market in the near future but for the merger. This requires showing that the value of the business as an ongoing concern is less than its liquidation value. This comparison will provide a good indication as to whether or not keeping the firm 'alive' is a profitable course of action. However, the proof cannot be absolute since it is subject to a number of assumptions regarding future cash flows, discount rates and rates of return. Furthermore, the value of the firm as an ongoing concern will depend on the attitudes of its stakeholders regarding potential financial and/or economic restructuring. And the liquidation value of the firm cannot be determined without a detailed analysis of the health of the industry in which it operates. As is well known, a firm's assets are worth more if sold to competitors in a thriving industry than in an industry that is contraction. Finally, the timing of exit may be difficult to establish with precision in many cases.

The parties must also show that there is no alternative transaction with less anti-competitive effects. This is also analytically demanding. If forecasting the competitive effects of a merger is difficult on its own, comparing prospectively the effects of two competing mergers is a much more complex exercise. In practice it may require detailed information about potential acquirers that will not be available to the failing firm unless it enters into negotiations with several parties at once. It may also prove to be highly complex and time consuming since there are many potential alternatives.

In *Deloitte & Touche/Andersen*,⁸⁶ the European Commission considered a counterfactual scenario in which Andersen assets would be taken over by the remaining Big Four audit and accounting firms and a second one in which there would be no take-over and the existing clients from Andersen would be dispersed among the remaining Big Four firms.⁸⁷ The second scenario involved two different sub-scenarios depending on the attribution of shares: (i) equal shares of Andersen's market share among the Big Four players; and (ii) a distribution of Andersen's market share in proportion to the shares of the Big Four firms.

Furthermore, this kind of counterfactual analysis is a highly problematic exercise from a commercial perspective. A distressed firm is by definition in a very precarious situation. To request that it should launch itself into a beauty parade before all its competitors may harm its ability to sell on the market and accelerate its exit. The firm will have to spend resources in searching reasonable alternative acquirers and divert resources away from other more productive activities. Competitors are likely to use the search to their competitive advantage, dissuading customers to source from a company on the brink of exit.⁸⁸ These commercial realities should be taken into account when assessing whether the failing firm has satisfactorily satisfied the requirement to search for alternatives, and engage in parallel negotiations.⁸⁹

Finally, the parties are required to show that the target firm's assets will exit the market but for the merger. In particular, the merging parties need to exclude the possibility that some of the failing firm's assets may be taken over by third parties absent the merger. In other words, the parties have to provide evidence that no competitor or potential new entrant into the relevant markets affected by the transaction may be interested in a meaningful share of the assets of the failing firm.⁹⁰ This is obviously cumbersome.

⁸⁶ European Commission decision of 01/07/2002 in case M.2810 Deloitte & Touche/Andersen (UK).

⁸⁷ *Ibid.*, p. 49.

⁸⁸ Shehadeh, R., J. Larson and I. Knable Gotts. The effect of financial distress on business investment: implications for merger reviews. In *Antitrust*, Spring 2009, Vol. 23, Issue 2, p. 12.

⁸⁹ See EC Horizontal Merger Guidelines, note 34 *supra*, p. 217.

⁹⁰ See note 45 *supra*.

In strict terms, it would require considering the possibility of partial acquisitions in the context of a formal or informal liquidation process. This requires in turn identifying which assets may be attractive to actual or potential competitors, assessing the likelihood that those assets will end up in the hands of precompetitive acquirers in the context of a liquidation of the firm, and evaluating the time needed for those asset transfers to materialise. This is not a trivial task.

2.5 *Counterfactual Analysis and the FFD*

In order to assess the potential competitive harm resulting from a merger, competition agencies typically compare the competitive outcomes that are expected to characterise the post merger scenario with those that would emerge under the so-called counterfactual scenario. In other words, the standard approach in merger control involves two steps. First, the competition agency in charge of the merger review identifies the appropriate counterfactual — *i.e.* the market structure which is expected to prevail in the absence of the merger. Second, it compares that counterfactual scenario to the post merger scenario. Note that the burden of proof in both steps of this counterfactual (or but-for) analysis lies with the competition agencies.

In a merger investigation of two financially healthy firms, the counterfactual scenario is typically characterised by the competitive conditions at play in the pre-merger situation. This is the right approach unless those conditions are expected to be different in the near future even absent the merger. However, when one of the merging parties is a failing firm, the competitive situation before the merger or *status quo* is unlikely to provide a valid approximation of the competitive structure of the affected markets in the absence of the merger. In other words, the competitive threat imposed by the failing firm prior to the merger is likely to overstate the competitive constraint that the firm would be able to impose in the future absent the merger. This makes the choice of an appropriate counterfactual a more complex exercise. In fact, there may be more than one relevant counterfactual scenario when one of the merging parties is in financial distress and deciding which is the most appropriate one in each particular case is far from simple.

One of the various potential counterfactual scenarios which could be compared with the post-merger scenario when assessing a failing firm defence involves the exit from the market of all the assets of the failed firm. Another possible scenario would have all those assets being purchased by an incumbent, and in yet another scenario the purchaser would be a potential entrant. Other possible counterfactual scenarios would involve the restructuring and retrenching of the failed firm and the sale of some of its assets to incumbents and/or entrants.

Understanding which counterfactual scenario(s) are most relevant for a given case requires investigating the various options open to the failing firm to determine which ones represent real possibilities. But this is bound to be difficult, as various possible courses of action need to be analysed with fairly limited information, given the commercial risks involved in openly exploring multiple merger and/or restructuring alternatives when a firm is in financial distress.

And yet the implications of choosing one counterfactual scenario rather than another are potentially radical. To see why, consider a proposed merger involving two incumbent firms, where the target firm is in financial distress. If the right counterfactual scenario involves the exit of all of the failing firm's assets, the merger is unlikely to distort competition relative to the counterfactual scenario. On the contrary, the merged entity may retain a significant fraction of the failed firm's assets and so the merger may result in a lower reduction in supply than in the asset-exit counterfactual. In that case the merger should be approved because its anticompetitive impact is smaller than the anticompetitive impact of the failing firm's exit.

If, on the other hand, the right counterfactual is one where the failing firm's assets are purchased by one (or more) new entrant(s),⁹¹ then the proposed merger is unlikely to be approved because its impact on competition is likely to be more detrimental than the impact of alternative transaction(s). The merging parties could defend the relative merits of their proposal and get their deal through, however, if they could demonstrate that their merger would give rise to economies of scale and scope or demand side efficiencies which the new entrants would not be in a position to match or, alternatively, that the new entrants have no experience in the market and are only interested in stripping the assets of the failing firm so that the failing firm would not be able to compete effectively under the new ownership.

Suppose, instead, that the right counterfactual involves the sale of the failing firm to a company which is already active in the market. In that case, a proper assessment of the proposed merger requires comparing the effects of two alternative mergers: the proposed merger, where the acquiring party is an incumbent (otherwise there will be no need to resort to a failing firm defence), and a merger with another incumbent. While this is not an impossible job, it is fair to recognise that it is necessarily a much more complicated exercise than the standard merger analysis where the merger is compared to the *status quo*. The results of this complex comparison could in principle be favourable to the merging parties or not.

One may also conclude that absent the merger, the failing firm will not leave the market in the short term. Firms with high sunk costs may be particularly reluctant to leave the market.⁹² They may also be kept alive by lenient bankruptcy codes. Or they may be able to renegotiate their debt and restructure their businesses. A counterfactual scenario where the failing firm manages to stay in the market either as a "zombie" or a shrunk version of its former self need not be more competitive than the post-merger scenario. Zombie firms may create significant distortions: under a limited liability cover or thanks to automatic stay provisions under the country's bankruptcy code, the failing firm may engage in inefficient pricing and non-pricing policies which are nothing but opportunistic bets for resurrection. The inefficiencies resulting from such policies would have to be compared with the effects from the increase in concentration after the proposed merger. Downsized firms may be unable to compete effectively or at least as effectively as the merged entity would be able to do.

The failing firm defence policies reviewed in Section 2.1 do not follow the two step process which characterises standard merger control policy. The typical failing firm defence is, instead, structured as follows:

- First, merging parties and competition agencies conclude that the merger will distort competition by comparing the post-merger scenario to the pre-merger scenario;
- Second, the merging parties must show that the failing firm will exit the market absent the merger. Otherwise, the merger will be blocked or remedies will be required;

⁹¹ A counterfactual scenario where several firms purchase the assets of the failing firm may be more competitive than one where there is a sole purchaser. However, the goodwill attached to the failing firm may disappear when their assets are so fragmented that the ability to compete of those purchasers is seriously impaired. See Oxera. 2009. "Failing, or just flailing? The failing firm defence in mergers." Oxera Agenda March 2009. Available on 26-08-2009 at: http://www.oxera.com/cmsDocuments/Agenda_March2009/Failing%20firm%20defence.pdf.

⁹² See O'Brien, J. & T.Folta. 2009. "Sunk costs, uncertainty and market exit: A real options perspective." Oxford Journal Industrial and Corporate Change. Available on 22-09-2009 at: <http://icc.oxfordjournals.org/cgi/content/abstract/dtp014>.

- Third, the merging parties must also demonstrate that there is no less anticompetitive merger. That is, they have to determine whether there are alternative mergers and then compare those merger scenarios to the proposed merger;
- Fourth, the merging parties must also show that all assets of the failing firm will exit the market but for the merger. Otherwise, the merger will be blocked or conditioned.

This structure is problematic: a merger involving a failing firm may be blocked (or remedied) for not satisfying the above conditions even when it represents the least anticompetitive solution for the failing firm's financial problems. To see why this is the case, let us consider each of the four conditions separately.

The first condition compares the post-merger scenario with the pre-merger scenario, but that comparison is only relevant if the pre-merger scenario constitutes an appropriate proxy of the structure of the market in the absence of the merger, which is unlikely if the target firm is in financial distress. Importantly, this comparison determines the allocation of the burden of proof; the burden of proof shifts from the agencies to the parties when the post-merger scenario is less competitive than the pre-merger scenario.

The second condition is based on the presumption that having a financially distressed firm in the market, possibly gambling for resurrection or crippled after restructuring, is better for consumers than the proposed merger. This presumption is not justified: the presence of a handicapped, financially distressed firm in the market is likely to distort productive efficiency and may crowd out relatively efficient firms to the ultimately detriment of long-run consumer welfare.

The third condition is consistent with the standard two-step process in merger control. However, the responsibility to demonstrate the absence of more competitive alternatives falls on the merging parties, which are less well equipped to undertake the sort of analysis that competition agencies typically perform in reviewing mergers between financially healthy firms, which are much simpler. Most importantly, the parties will not be able to elicit as much information from third parties as the agencies typically do. The reversion of the burden of proof may therefore lead to erroneous decisions.

The fourth condition is based on the presumption that the market structure that will result from the merger will necessarily be less competitive than a market structure where the assets of the failed firm are shared among a number of actual and/or potential competitors. But this need not be the case: a market with a few large symmetric players and multiple minnows may be less competitive than a market with fewer minnows if the large players become less symmetric.

In sum, a merger involving a failing firm may be blocked (or remedied) for not satisfying the above conditions even when it represents the least anticompetitive solution for the failing firm's financial problems. This may be the case in a number of circumstances. For example, it would be the outcome of the failing firm defence assessment if restructuring is possible but highly inefficient, or if there are potential buyers for the failing firm's assets but those purchasers are unlikely to use those assets efficiently, or when there is an alternative purchaser for the failed firm's business, which is however less likely to compete effectively in the market, and the merging parties find it too difficult to discharge their burden of proof.

2.6 *Conclusions*

The criteria set out in different jurisdictions for the assessment of failing firm defence claims in horizontal merger control are very similar. They require the merging parties to show that the allegedly failing firm and its assets would exit the market in the near future if not taken over and that there is no less

anti-competitive alternative purchase than the proposed merger. These requirements are very demanding. Not surprisingly, the number of cases in which the failing firm defence has been successfully invoked is limited. For instance, in the UK, the OFT has only cleared five mergers on failing firm defence grounds since 2003, when the OFT's merger guidelines were published.⁹³ The number of merger cases in which competition authorities or courts have accepted the defence in other jurisdictions is also very limited.

Merging parties contemplating a failing firm defence are likely to be dissuaded by more than just the strict nature of the criteria applied to such claims. Even when the defence is accepted, it is usually only after an extensive scrutiny and, in some instances, the imposition of significant remedies.⁹⁴ In addition, a failing firm defence claim requires recognition that the proposed merger is anticompetitive. After all, the failing firm defence is based on the claim that the merger, while harmful to competition, is a lesser evil. Merging parties may well be reluctant to make that admission.

Finally, and as importantly, under the current criteria, merger review under a failing firm defence may result in too many incorrect prohibitions or in the imposition of disproportionate remedies. A merger should only be blocked or conditioned if the post-merger scenario is less competitive than a properly constructed counterfactual scenario. The counterfactual scenario must reflect the market structure which is expected to prevail in the absence of the merger. As shown above, the strict application of the failing firm defence criteria applied in all jurisdictions which we have considered may lead to conclusions regarding the proposed merger which are different from those that would result from a proper counterfactual analysis.

3. Merger Control and the FFD in a Credit Crunch

3.1 Introduction

The current crisis started in the financial sector and can be traced back to the collapse of the subprime market in the summer of 2007. As a result of the breakdown of this market, banks stopped lending, which impacted the real economy adversely. The economies of developed and emerging markets all entered into recession due to the limited availability of short-term funding for businesses. Though the monetary policies of the largest economies in the world have provided considerable liquidity to worldwide capital markets and the co-ordinated stimulus packages of those economies are pulling demand all around the world, the crisis is far from over.

In the context of the current financial crisis, more firms are likely to find themselves in financial difficulty. As mentioned in Section 1, total bankruptcy filings have spiralled upwards in recent months all

⁹³ OFT. 2003. Mergers - Substantive assessment guidance. OFT 516, Published in May 2003. These mergers were: (i) ME/1517/05 First West Yorkshire/Black Prince Buses - Anticipated acquisition by First West Yorkshire Limited of Black Prince Buses Limited, OFT decision, 26 May 2005; (ii) ME/3387/07 Tesco/Kwik Save - Anticipated acquisition by Tesco Stores Limited of five former Kwik Save stores (Handforth, Coventry, Liverpool, Barrow-in-Furness and Nelson), OFT decision, 11 December 2007; (iii) ME/3145/07 CDMG Group / Ferryways NV / Searoads Stevedores NV - Completed acquisition by the CdMG group of companies of Ferryways NV and Searoad Stevedores NV, OFT decision, 24 January 2008; and (iv) ME/3427/07 Homebase/Focus - Completed acquisition by Home Retail Group plc of 27 stores from Focus (DIY) Ltd, OFT decision, 7 August 2008; and (v) OFT decision of 14 May 2009: ME/4036/09 Anticipated acquisition by HMV of 15 Zavvi stores.

⁹⁴ For instance in 2001 the Australian Competition and Consumer Commission (ACCC) imposed conditions on the approval of the acquisition of Impulse Airlines by Qantas Airways. Qantas was required to allow access to peak slots at Sydney Airport and had to offer certain slots to other carriers. See Bnet. 2001. ACCC approves commercial agreement between Qantas Airways and Impulse Airlines. Available on 18-08-2009 at: http://findarticles.com/p/articles/mi_m0CWU/is_2001_May_21/ai_74807690/.

over the world.⁹⁵ Many SMEs and large firms have been unable to escape the effects of the crisis. Firms such as General Growth Properties (GGP), the second largest real estate investment trust and mall operator of the US, automobile manufacturers Chrysler and General Motors, and Japanese property developer Zephyr, to name a few, have all recently filed for bankruptcy protection.

The financial problems of those firms may be resolved by merging with financially healthier partners. A successful merger will prevent a failing firm's bankruptcy and retain the firm's assets in the market, which may be privately profitable not only for the stakeholders of the failing firm but also for the acquirer's shareholders, and beneficial to the competitive process and consumer welfare. It is therefore possible that competition agencies face an increasing number of failing firm or flailing firm defences in coming months or years. Whether this is indeed the case will depend on external factors – such as the depth and the duration of the credit crunch and recession – as well as on internal factors – such as the nature of the competition agencies' responses to those defences. This section considers whether existing failing firm defence policies are apt to deal with mergers involving failing/flailing firms in the midst of the current credit crunch.

3.2 *Merger Control and the Credit Crunch*

The current financial crisis and economic recession present a number of challenges for merger control.

First, during a credit crunch firms in financial distress need not be cost inefficient and their products need not be in lack of demand. Healthy firms may find themselves in distress because the lack of credit in the economy makes it impossible to obtain the working capital needed to maintain their operations. Letting an efficient firm with products for which there is a significant demand exit the markets where it operates because of the defective functioning of the capital markets is not in the best interest of consumers. Rather it will give rise to an additional market failure: increased market power. It will reduce competition and harm consumers. In those circumstances it may be preferable to let competitors in financial trouble merge, even when this raises potential competition concerns, as this may allow them to achieve the real and financial synergies needed to remain active in their traditional markets. It is therefore of key importance that the failing firm defence regime does not foreclose this option unless there is clear evidence that there are less anticompetitive options and that those options are indeed realistic. However, for the reasons explained in Section 2.5, given the structure of the failing firm defence now in place in the jurisdictions we have reviewed there is some risk that a merger involving a distressed target may be blocked (or remedied) even when it represents the least anticompetitive solution for the failing firm's financial problems.

Second, during a credit crunch of the magnitude of the current one, entire industries may be falling into financial distress. The banking industry is an obvious example. The automotive industry, the steel industry,⁹⁶ the US hotel industry,⁹⁷ the newspaper industry,⁹⁸ and the diamond industry⁹⁹ constitute other

⁹⁵ See <http://www.fastupfront.com/blog/business/21-famous-corporate-bankruptcies-from-2001-2009/> and also <http://news.bbc.co.uk/2/hi/business/8091298.stm>.

⁹⁶ See for instance: “Steel production to decline by 10% in 2009, say analysts”. 29 December 2008. Available at: <http://www.irishtimes.com/newspaper/finance/2008/1229/1229728603954.html> and “Now, US steel industry asks for government bailout”. 2 January 2009. Available at: http://www.domain-b.com/economy/worlddeconomy/20090102_us_steel_industry.html.

⁹⁷ See for instance: “More distress on the horizon for U.S. hotels”. 23 July 2009. Available at: http://www.hotelmarketing.com/index.php/content/article/more_distress_on_the_horizon_for_us_hotels/.

⁹⁸ See for instance: Bandyk, M. 2009. “Newspaper Bailout Seriously Considered”. 25 March 2009. Available at: <http://www.usnews.com/blogs/risky-business/2009/03/25/newspaper-bailout-seriously-considered.html>.

examples. The main challenge for competition agencies engaged in a merger review in one of these declining industries is to define the appropriate counterfactual given that the pre-merger situation or *status quo* is unlikely to provide a valid approximation of the market structure that would be expected in the near future absent the merger. The industry may become much more concentrated even in the absence of the proposed merger, since one or both merging parties may have to exit but for the merger. There may also be concurrent merger transactions given that other industry participants may try to merge in order to avoid bankruptcy.

This may suggest that merger control should be relatively more lenient in distressed industries. However, there are factors pointing in the opposite direction. Note, in particular, that entry may be much more difficult in the context of a credit crunch, as new entrants would have limited, if any, access to credit.¹⁰⁰ Entrants may have the ideas but lack the funding with which to penetrate the market. Also, a distressed industry may see one merger after another as failing firms combine with each other to avoid bankruptcy. The analysis of each concrete merger should therefore take into account the possibility of sequential mergers. In other words, when a whole industry is in distress, the counterfactual scenario may have to include all expected future mergers. The impact of the current merger on competition and consumer welfare is much more likely to be negative when other mergers are also expected in the near future. Likewise, the adverse impact of a given merger is bound to be greater if some competitors leave the market in the near future due to their inability to raise credit.

Furthermore, two other factors would need to be considered before adopting a softer stance in connection with mergers in financially distressed industries:

- *Confusing industrial decline with short-lived downturns.* It is very difficult to distinguish whether an industry is at risk of collapse or is simply experiencing a short-lived downturn.¹⁰¹ This is an extremely important distinction since a change in market structure may have a negative long-run impact on consumer welfare. Competition authorities should thus be careful not to overreact in response to the business cycle by approving mergers that would harm consumers in the long run: “recessions are temporary, but mergers are forever”.¹⁰²
- *Alternative policies.* The right policy response to an industry-wide and long-lasting crisis may not be a lenient merger control policy. Governments have other instruments at their disposal. They may provide financial support to troubled industries, for example. Those policies are much more flexible than merger control. While financial support measures can be tailored to the business cycle, anticompetitive changes in market concentration cannot be quickly corrected once the industry is out of recession.

Third, when one of the merging firms is in financial distress time is of the essence. During a merger investigation, the financial position of a failing firm may quickly deteriorate. Firms which might initially

⁹⁹ See for instance: “Banks urged to bail out diamond industry”. The financial express. 7 March 2009. Available at: <http://www.financialexpress.com/news/banks-urged-to-bail-out-diamond-industry/431837/>.

¹⁰⁰ See Nigra, B.A. & J.S.Kanter. 2003. “The Effect of Market Conditions on Merger Review -- Distressed Industries, Failing Firms, and Mergers with Bankrupt Companies.” 2 ABA section of Antitrust Law, 51st annual spring meeting course materials, 736 737 (2003). Available on 26-08-2009 at: <http://www.abanet.org/antitrust/at-committees/at-telecom/pdf/distressedindustry.pdf>.

¹⁰¹ See for instance the speech by Debra A. Valentine, Deputy Director of Policy Planning of the FTC on 8 December 1995. Available at: <http://www.ftc.gov/speeches/other/dvhorizontalissues.shtml>.

¹⁰² C. Shapiro, “Competition Policy in Distressed Industries,” speech delivered at the ABA Antitrust Symposium: Competition as Public Policy, May 13 2009.

have been described as “weak competitors” or “flailing firms” may rapidly become failing firms. The rapid flux in the industry and the uncertainties raised by the crisis may make the proposed merger especially time-sensitive and render other alternative transactions irrelevant. This adds time pressure to the many challenges faced competition agencies in the context of merger control.

Fourth, financial distress may affect firms’ motivations to merge. Competition agencies should carefully investigate the reasons behind mergers involving firms in financial distress. As explained below, that requires considerable understanding of corporate finance and, in particular, of the interrelationships between capital and product markets. Companies often merge in order to benefit from deeper internal capital markets.¹⁰³ Consolidation allows companies to increase and/or better allocate the internal resources needed to fund investment and innovation plans. This merger rationale is of particular importance when internal funds are much cheaper than external capital, or when access to external capital markets is restricted, as is the case in current times. Of course, consumers benefit from increased investment and innovation. Improved access to funding also generates real efficiencies through its effects on product market competition.¹⁰⁴ For example, it may allow companies to step up investment in productive capacity. When those investments reduce marginal costs, we would expect lower prices. Similarly, a merger that increases firms’ ability to fund investments may help them to pursue dynamic pricing strategies in which early losses to build a customer base are offset by future profits. These pricing strategies are optimal in markets characterised by network effects, learning by doing and switching costs, but in the absence of external funding require deep pockets.

Consolidation may also constitute an efficient response to negative demand shocks. The decline in demand, and the consequent loss of scale, may increase firms’ unit costs. Mergers in markets experiencing reductions of demand may therefore allow firms to reduce their inflated unit fixed and variable costs. Consumers will benefit from these economies of scale provided the merged entity remains constrained by actual or potential competitors. Those benefits will be greater when the adverse shocks are persistent over time and there are no significant barriers to entry.

Fifth, the tightening of the financial markets may also make the task of finding suitable buyers for divested assets much more difficult. Those with the required traits may not be able to access the funds required to acquire the assets of the merged entity. As a result, the anticompetitive effects of mergers may not be remedied, or at least not as easily as in normal times.

3.3 *Implications of the Credit Crunch for the FFD*

As stated above, many firms are likely to find themselves in financial distress when capital markets are tight and the economy is in recession. Some of those may contemplate a merger with a competitor as the most attractive exit route and a fraction of those may evaluate the possibility of developing a failing firm defence. However, the prospects of success may be limited under the analytical framework currently used to assess such defences in the jurisdictions we have reviewed.

As explained in Section 2.5, the current framework presumes that certain but-for scenarios, such as the permanence of a trimmed down and handicapped company in the market, are necessarily superior from a competitive perspective than the merger under review. Such a presumption is not always justified. So mergers may be blocked even when they represent the least anticompetitive option. Furthermore, the assessment of a failing firm defence requires considerable time which, given that the position of firms in distress may rapidly deteriorate, may trigger inefficient liquidations. Consequently, the option of running a failing firm defence may not be available in practice.

¹⁰³ J. Stein, 1997, “Internal Capital Markets and the Competition for Corporate Resources”, *Journal of Finance*, 52, 111-133.

¹⁰⁴ See note 88 *supra*.

Of course, competition agencies can address many of these problems in practice. They can fast track those notified mergers so as to avoid the risk of costly delay. They may also invest resources in investigating the business rationale and identifying the most appropriate counterfactual without any *a priori* or preconception. Finally, they may also work together with the parties in identifying compensation measures to ensure that the proposed merger goes through with limited anticompetitive effects. These practical changes would certainly improve the outcomes of the merger control process and hence are undoubtedly justified. What would not be justified is to modify current merger policy so that it becomes tolerant with anticompetitive mergers which do not represent the least anticompetitive option realistically available to the failing firm. Such a reform would violate the fundamental principle of merger control – which establishes that an anticompetitive merger should be blocked or condition unless it can be shown to be the least anticompetitive option. That principle is as valid in the current economic and financial context as it was in the past.

3.4 *Mergers between Banks and the FFD*

The challenges faced by competition agencies analysing mergers among distressed companies in the current crises are nowhere greater than when those mergers involve banking institutions. Banks are special economic agents because of their importance for the stability of the financial system and the economy. The collapse of one bank system may cause a financial meltdown and a severe economic recession. Globalisation and increased interbank lending have made banks highly dependent on each other. Investors and businesses are also dependent on banks. This establishes a close link between the real economy and the health of the financial system. The systemic role of the banking sector explains why it may be of great importance to prevent the exit of an individual bank, and may justify a more lenient approach to bank mergers during a credit crunch.

Competition authorities should, however, distinguish between banks that suffer from structural problems and banks that are fundamentally sound but that are hampered by a temporary liquidity shortage when considering bank mergers. Mergers involving a bank with significant structural problems may do more bad than good, as the toxic assets of the failing bank may contaminate the merging partner. In that case, the merger may take the assets of the two merging parties out of the market. The restriction in output that this may cause will hurt consumers for a long period of time.

Competition agencies should also take into account the possibility of State intervention in the absence of a merger. This makes the definition of the appropriate counterfactual particularly tricky in banking mergers. Banks in financial distress – especially those that are too big to fail – may not be allowed to go under in order to avoid the systemic implications of their collapse. Governments may try to persuade healthy banks to acquire their troubled competitors but, when that is not possible, they may inject capital or provide other forms of financial support in order to avoid the systemic consequences of bank failure. In *Lloyds/HBOS*,¹⁰⁵ for example, both the merging parties and the UK OFT agreed that it was “impossible to contemplate that HBOS would have been allowed to fail” considering the disastrous effects “in terms of financial stability, in particular in terms of counterparty exposure, depositor exposure, investor confidence and general confidence in the wider economy”.¹⁰⁶ The OFT then analysed the proposed merger assuming that HBOS would remain in the market with State support.

¹⁰⁵ OFT, Anticipated acquisition by Lloyds TSB plc of HBOS plc, Report to the Secretary of State for Business Enterprise and Regulatory Reform, 24 October 2008.

¹⁰⁶ *Ibid.*, pp. 57-58.

Let us now consider the use of the failing firm defence in banking mergers under the current crisis. Three different cases must be distinguished. The simpler case is one where the merger comprises two relatively small banks whose failure is unlikely to cause systemic effects. In that case the application of the failing firm defence raises no new issues.

This is not so when the merger involves one or more systemic banks – *i.e.* banks whose collapse could generate negative spillovers on the economy as a whole. The failing firm defence cannot be applied to mergers between banks when there is a significant risk that the failing bank contaminates the acquirer. As noted above, in this case the post merger scenario is likely to produce less attractive outcomes for consumers than the exit of the troubled bank. The merger should be blocked or remedies should be imposed.

The failing firm defence cannot be applied either to mergers between systemic banks because governments would not allow systemic banks to fail. In Lloyds/HBOS, for example, the OFT concluded “that the application of the failing firm defence in this case is not appropriate given that it is not realistic to consider that HBOS would have been allowed to fail (or that its assets would have been allowed to exit the market).”¹⁰⁷

This should pose no major concern, however. If the problem faced by the distressed bank is a temporary liquidity shortage. Mergers, which are relatively permanent measures, are inferior solutions to systemic risk than government interventions, such as capital injections and/or loan guarantees, simply because it is easier to find an exit strategy with respect to the latter measures.

On the other hand, this does not mean that all such mergers necessarily cause incremental anticompetitive effects and should be banned or conditioned. It is perfectly possible that the post-merger scenario proves more competitive than the scenario with no merger and one State supported (or State owned) bank. The rescued bank will be allowed to benefit from past excessive risk taking, which will exacerbate the moral hazard problems that are common in banking. Sound banks will likely lose business at the expense of over-aggressive too-big-to-fail, bailed out banks. In addition, the rescued bank will be able to attract new depositors and borrow at a lower cost in interbank markets given the State support. It will hence be able to lend more aggressively and steal business from more prudent competitors without the State guarantee. These distortions may cause the exit of existing competitors and prevent the entry of new rivals. The harm to competition under this counterfactual scenario is thus likely to be greater than the potential anticompetitive effects of the merger.

3.5 Conclusion

The current financial and economic crisis may place a large number of firms in financial distress. Some of them may try to address their financial problems by merging with financially strong competitors. In some cases the merging parties may consider relying on the application of the failing firm defence to get their deals approved by regulators. This may prove to be an onerous and disappointing choice, however. As we saw in Section 2 above, the conditions required for accepting a failing firm defence are very strict and the burden of proof imposed on the parties very demanding. This is problematic in general but especially so in a financial crisis where capital is scarce and solvent firms in financial distress risk losing their franchises from one day to the next.

In the next Section, we consider whether firms experiencing financial distress may be better off defending their deals using standard “but for” arguments. That is, comparing the effects of the merger on competition with a realistic counterfactual scenario which reflects the external context. This pure effects-based approach is free from the many presumptions that underlie existing failing firm defence policies.

¹⁰⁷

Ibid., p. 59.

4. Assessing Current FFD Policies

In the context of merger control, competition authorities must decide whether to approve the merger, though possibly imposing some conditions (remedies) on the merging parties, or to block it. These are difficult decisions. Merger investigations are complex prospective exercises. Competition agencies attempt to correctly foresee whether the proposed merger will harm consumers with often limited and dated information about the dynamics of competition in the markets affected by the deal. Not surprisingly, their decisions may turn out to be wrong. So-called type I and type II errors may occur. Type I errors refer to prohibition decisions involving mergers that in reality would not have caused anti-competitive effects and might even have contributed to increased competition. Type II errors refer to decisions approving mergers that actually caused harm to competition. Competition agencies also make type I errors when they impose remedies that are unnecessary or disproportionate and type II errors when the remedies imposed on the parties are not capable of restoring effective competition post merger.

Ideally, competition agencies should assess the competitive effects of mergers using a set of explicit or implicit rules that (a) minimise the expected cost of error, (b) are relatively inexpensive to administer and (c) produce predictable results.

The expected cost of error is given by the likelihood of type I and type II errors and their respective costs. The cost of a type I error will be large only when the merger would have produced significant cost or demand efficiencies; otherwise, the cost will be minimal. A type II error occurs when the authorities conclude that the merger is pro-competitive and in reality the welfare loss resulting from the price increase caused by the merger offsets the cost and demand efficiencies made possible by the merger. The cost of a type II error will be large when the merger produces modest (or no) efficiencies, while it gives rise to a significant increase in market power, as reflected by a substantial price increase. Type I errors are often considered more serious than type II errors in merger control. This is because the potential anti-competitive effects of a merger may be limited via ex-post intervention, such as the prohibition on the abuse of a dominant position. That option is likely to be available only in jurisdictions like the EU, where it is possible to find a violation for excessive pricing. In other jurisdictions, the harm from the merger could go on for a long, long time, as long as there is no abusive, exclusionary conduct that maintains or extends the firms' market power.

The costs of both types of error may be particularly large when the merger under review involves a failing firm operating in the midst of a credit crunch. On the one hand, those mergers may give rise to significant efficiencies. For example, the merger may prevent the exit of the failing firm's assets from the market. It may also allow cash-constrained firms to continue investing in new products and processes. On the other, the merger may weaken the financial position of the acquirer, thus reducing its own efficiency. Or it may simply be used to consolidate a competitive market in a co-ordinated fashion and at the expense of consumers. For these reasons the costs of type I and type II errors may be considerable.

The likelihood of error when assessing failing firm mergers in a financial crisis is also likely to be high. As explained above the pre-merger scenario provides little or no guidance about the development of the market post merger or even in the absence of the merger. Competition agencies need to consider the macroeconomic conditions under which the merging parties will operate, need to audit their financial health, etc.

It is therefore important to evaluate the expected cost of the criteria used by competition agencies around the world to assess a failing firm defence in order to determine whether that cost can be minimised without increasing implementation costs or reducing the predictability of their decisions. This is the object of this Section. In what follows we seek to assess the failing firm defence approach currently used in the jurisdictions reviewed in Section 2 from the viewpoint of its *administrability* – i.e. its implementation costs

–, its *predictability* – which provides legal certainty to firms contemplating a merger –, and its *efficiency* – which is given by the likelihood and cost of their erroneous merger decisions.

4.1 *Type I and Type II Errors*

The current approach to the failing firm defence appears to be geared towards minimising type II errors. First, while it clearly applies to extreme situations of financial distress, its application to mergers involving flailing firms or weak competitors is open to question. Second, the merging parties are required to consider a large number of possible counterfactuals. They must consider the feasibility of a but-for scenario where the failing firm is able to restructure and remain in the market as a stand-alone player. They must also contemplate scenarios where the failing firm exits the market but some or all of its assets remain operational in the hands of current or potential competitors. And they must also compare and contrast their proposed merger to all other realistic merger alternatives. In fact the failing firm must demonstrate that it has made good-faith efforts to find alternative partners, where “any offer to purchase the assets of the failing firm for a price above the liquidation value of those assets (...) will be regarded as a reasonable alternative”.¹⁰⁸ Third, the existing approach presumes that some of those counterfactual scenarios are preferable to the post-merger scenario from a competition viewpoint. In particular, the current approach will reject a failing firm defence unless the merging parties can demonstrate that some of those counterfactuals are not realistic: they must show that the firm and its assets are likely to exit the market absent the proposed merger.

This bias in favour of minimising the likelihood of type II errors can be explained as follows. A lenient approach may not properly account for the anti-competitive effects of mergers involving failing firms, which could lead to long-lasting distortions of the competitive process given the irreversible nature of mergers. As noted by Professor Salop, competition agencies must be “highly sceptical of lawyers who will try to turn every temporary recession into a golden opportunity for industry cartelisation by merger.”¹⁰⁹ A lenient approach may also lead to an increase in the number of welfare-reducing merger applications. A well-functioning merger control system deters the filing of anticompetitive mergers. Competition agencies seeking to maximise the deterrent effect of merger control will bias their merging policies in the direction of minimising type II errors.

Furthermore, a lenient approach may lead to inefficient entry decisions.¹¹⁰ Entry decisions are based on an estimation of expected profits post entry. By allowing firms a cheap way out and limiting their exit costs, a lenient application of the failing firm defence may truncate the losses an entrant would expect to incur upon failure. This artificially reduces the cost of entry and, as a result, may incent entry by inefficient competitors. Furthermore, entry decisions may be skewed towards those markets where investors expect a more lenient failing firm defence, which would distort normal market functioning.¹¹¹

A lenient approach may also cause inefficient exit decisions. One of the desirable features of a well-functioning competitive process is that it leads to the exit of inefficient firms and in this way it ensures that production is conducted at the minimum possible cost. This is always important but especially in the context of a credit crunch when funding is scarce and therefore it is important that it gets channelled to the

¹⁰⁸ See note 13 *supra*, Section 5.1, footnote 39.

¹⁰⁹ Federal Trade Commission Hearings on Global and Innovation-Based Competition, (1995) (statement of Steven C. Salop, Professor of Economics and Law, Georgetown University Law Center).

¹¹⁰ Heyer, K. & S Kimmel. 2009. Merger Review of Firms in Financial Distress. Economic Analysis Group, Discussion Paper 09-1, p. 11.

¹¹¹ *Ibid.*, p. 12.

companies with greater growth opportunities. A narrow application of the failing firm defence “will help weed out weak and inefficient firms and foster long-term growth.”¹¹²

Last but not least, competition agencies may have another reason to adopt an analytical framework that is biased towards the minimisation of type II errors: such a bias may help them to resist the considerable political pressure that they are likely to receive when assessing some failing firm defence claims. Politicians care about certain mergers for industrial policy reasons or because they are interested in avoiding the loss of jobs at financially distressed companies.

The emphasis on type II errors comes at a cost: it increases the likelihood of type I errors. The current approach presumes that it is preferable from a competition standpoint to retain a handicapped failing company in the market than allowing it to merge with a competing, healthier company. As explained above this presumption is not always justified and may lead to prohibiting mergers even when they represent the least anticompetitive option. A firm in financial distress may have to reduce its investment in productive capacity. A merger which prevents those reductions in capacity may result in lower prices. Similarly, a merger that increases firms’ ability to fund investments may help them to pursue dynamic pricing strategies in which early losses to build a customer base are offset by future profits. These pricing strategies are optimal in markets characterised by network effects, learning by doing and switching costs, but in the absence of external funding require deep pockets. A merger with a healthier partner may provide the necessary funds.

An overly strict failing firm defence policy may not only cause too many erroneous decisions, it may also deter efficient mergers from being proposed, it may deter efficient new entrants by increasing the perceived risk of entry,¹¹³ and it may also induce firms in financial trouble to seek other more damaging, and possibly illegal, ways to ensure the continuation of their operations. For instance, firms may try to reach an agreement with competitors in order to increase revenue streams and profit levels. The discovery of such cartels is not easy. Alternatively, firms may demand State support. Although this is not necessarily harmful to society, a private-sector solution to financial distress may be superior to State intervention.

4.2 *An Effects-Based Alternative*

An alternative to the current failing firm defence approach would be to assess the competitive effects of mergers involving failing firms under a two stage effects-based counterfactual analysis. In the first stage, competition agencies should assess the evidence presented by the merging parties, their competitors and customers in order to determine what the most likely counterfactual scenario is without any *a priori* or presumptions. Second, competition agencies should compare the strength and vigour of competition under the post-merger and the counterfactual scenarios and approve the merger without remedies only if the post-merger scenario proves superior.

Like the current approach, this alternative is also likely to produce type I and type II errors. However, one would expect it to result in relatively fewer type I errors, because, in contrast with the current approach, it involves no presumption that the post-merger scenario is necessarily more harmful than other possible counterfactual scenarios – a presumption that is not necessarily correct. A merger will be blocked under the effects-based approach *only if* the facts show that it is likely to lessen competition relative to the level of competition that would obtain under the most likely counterfactual scenario(s). Under this approach the merging parties must prove that the target firm is in financial distress and that there is a

¹¹² Anandarajah, K., D. Lombardi & A. Mahesh Tulpule, 2009. Antitrust: Scrutiny of Mergers during Economic Downturns. Available at: <http://www.lawgazette.com.sg/2009-5/feature2.htm>.

¹¹³ Mason, R. & H. Weeds. 2002. The Failing Firm Defence: Merger Policy and Entry. CEPR Discussion Paper No. 3664, p. 30.

significant risk that it would exit the market absent the merger. They must also adduce the necessary evidence to assess the likelihood of alternative counterfactual scenarios. It corresponds to the competition authorities to decide what the relevant counterfactual is and to weigh the anticompetitive effects of the proposed merger using the counterfactual scenario as a benchmark for comparison.

On the contrary, the effects-based approach may produce relatively more type II errors than the current approach. Furthermore, it may be more difficult to administer. Gathering and analysing facts may be a complex, costly and lengthy process. It may also lead to less predictable outcomes. A case-by-case factual analysis may limit the ability of the merging parties to predict the outcome of a merger investigation pre-merger.

4.3 Conclusion

The current financial crisis represents an additional challenge for the application of the failing firm defence. A question arises as to whether the policy and its requirements should possibly be relaxed since existing failing firm defence policies may lead to many type I errors, which may be unacceptable in the context of economic and financial trouble. In this Section we have investigated the relative merits of adopting an effects-based counterfactual approach to the assessment of mergers involving firms in financial distress. This approach may reduce the frequency of type I errors but may give rise to more type II errors. It may also be more difficult to administer and may reduce legal certainty relative to the current scenario.

5. Concluding Remarks

In times of financial and economic crisis, such as the one we are currently experiencing, more firms may find themselves in financial difficulty. The current crisis has not only damaged the health of financial institutions, but has had an impact throughout the economy. Firms in financial distress will seek options to safeguard their long-term survival; one of those options is to merge with healthier partners. Competition agencies may face an increasing number of mergers involving firms in financial distress, some of which may be true failing firms while others may simply be weak competitors or flailing firms. In some of those cases, the failing firm defence may be put forward as an argument for the approval of the transaction. This paper has considered whether the failing firm defence policies of several OECD members are apt to deal with the challenge of assessing those transactions in these troubled times.

Those policies, which can be found in merger guidelines or inferred from merger decisions, involve a number of strict conditions: the allegedly failing firm and its assets must exit the market in the near future absent the merger and there must be no less anti-competitive alternative purchase than the proposed merger. It falls on the merging parties to demonstrate that those requirements are met. Not surprisingly, given the high standard of proof, there are very few cases in which the failing firm defence has been invoked successfully. And there are no reasons to believe that this will change in the current context of financial instability and economic recession.

This paper addresses the question whether this state of affairs is optimal. We have seen that the criteria used to assess failing firm defences today is geared towards minimising type II errors – *i.e.* erroneous merger clearances or insufficient remedies – and may thus result in too many type I errors – *i.e.* erroneous prohibitions or excessive remedies. We have also seen that a more effects-based approach focused on identifying the most likely counterfactual and comparing the outcomes of the post-merger scenario with those of such realistic counterfactual may lead to less type I errors though it makes type II errors more likely. An effects-based approach may also result in higher implementation costs and lengthier investigations. It may also be less predictable.

OECD member states should consider whether the bias of the current failing firm defence policies is justified. They may conclude that this is indeed the case because the defence will, in any event, only be applicable to a small percentage of mergers and is important to maintain a strict stance toward mergers that involve selling to a direct competitor. They may also consider that there are other policy instruments (*e.g.* bankruptcy law, State aid) which can be used to avoid the inefficient liquidation of financially distressed companies. Whether they decide to reconsider their current policies or not, there are some aspects of those policies that are difficult and others, such as the viability of the so-called flailing firm defence, which are unclear. Some competition agencies around the world have issued guidance on how they will analyse failing/flailing firm/division defences;¹¹⁴ we would encourage others to follow their example.

¹¹⁴

The guidance on the failing division defence usually follows the same lines of reasoning as the failing firm defence. See, *e.g.* US Department of Justice and the Federal Trade Commission Horizontal Merger Guidelines as revised April 8, 1997, p. 5.2; UK Competition Commission. 2003. Merger references: Competition Commission Guidelines. June 2003, p. 3.63; or Competition Bureau Canada. 2004. Merger Enforcement Guidelines. September 2004, Part 9 – Failing firm, p. 9.5.

NOTE DE RÉFÉRENCE¹

par le Secrétariat

1. Introduction

Les dispositions en vigueur en matière de contrôle des fusions visent à bloquer ou à soumettre à certaines conditions les opérations susceptibles d'amoindrir dans une large mesure (ou d'entraver significativement) la concurrence, en renforçant le pouvoir de marché des parties à l'opération. Les autorités de la concurrence ne peuvent bloquer ou soumettre à certaines conditions une opération de fusion que si et seulement s'il existe un strict lien de causalité entre la transaction sur laquelle elles se penchent et le préjudice anticipé pour la concurrence. L'argument de l'entreprise défaillante s'applique aux cas dans lesquels, même si l'effet anticoncurrentiel de la fusion n'est pas contesté, ce strict lien de causalité n'existe pas – à savoir, les cas engendrant une plus grande concentration et un affaiblissement important de la concurrence sur les marchés concernés par la fusion, que l'opération ait lieu ou non.

L'argument de l'entreprise défaillante est invoqué par les autorités de la concurrence du monde entier depuis les débuts des dispositifs de contrôle des fusions, mais seulement dans des cas exceptionnels. Aux États-Unis, l'argument de l'entreprise défaillante a été admis pour la première fois dans l'affaire *International Shoe* en 1930.² La charge de la preuve reposait sur l'entreprise défaillante qui a dû démontrer que ses « ressources [étaient] si réduites et ses perspectives de rétablissement si lointaines qu'elle se trouvait face à un sérieux risque de faillite. »³ Dans l'Union européenne, cet argument a été invoqué pour la première fois, sans être cependant admis, dans l'affaire *Aérospatiale-Alenia/De Havilland* en 1991, tout juste un an après le lancement du droit communautaire de contrôle des concentrations.⁴

Au fil du temps, les autorités de la concurrence ont recensé les critères précis qui doivent être remplis pour qu'une entreprise puisse recourir à l'argument de l'entreprise défaillante dans le cadre du contrôle des fusions. Le consensus général paraît être que cet argument ne peut être jugé recevable que lorsqu'il existe des éléments précis et convaincants prouvant que (a) la concurrence sera moins intense dans l'avenir et que (b) la fusion envisagée n'aura pas, de surcroît, pour effet de fausser le processus concurrentiel. Plus précisément, la plupart des autorités de la concurrence ont admis l'argument de l'entreprise défaillante lorsque l'entreprise présumée défaillante et ses actifs sont voués à disparaître du marché dans un avenir proche s'ils ne font pas l'objet d'un rachat et lorsqu'il n'existe pas d'autre solution de rachat, moins préjudiciable pour la concurrence, que la fusion proposée.

¹ Note préparée par Anne-Layne Farrar, Jorge Padilla et Henri Piffaut. Les auteurs sont économistes chez LECG Consulting. Ils souhaitent remercier Ingrid Liedorp pour son concours ainsi que Jeremy West et Joe Phillips pour leurs commentaires. La présente note ne reflète pas l'opinion de LECG ou de l'un quelconque de ses clients.

² Affaire *International Shoe c FTC*, 280 U.S. 291 (1930).

³ *Ibid.* p. 302.

⁴ Affaire IV/M.053 *Aérospatiale-Alenia/de Havilland* JO 1991, L334/42, §31.

En période de crise financière et économique, nombre d'entreprises sont susceptibles de se trouver financièrement en difficulté. Aux États-Unis, le nombre total de faillites enregistrées (faillites d'entreprises ou autres) est passé de 603 633 en 2006 à 847 141 en 2007 et 1 117 771 en 2008.⁵ Une évolution analogue a pu être constatée en Europe. Selon les estimations de Standard & Poor's (S&P), le taux global de défaillance pourrait atteindre jusqu'à 11 % en 2009, contre un taux moyen d'environ 3 % ces 15 dernières années.⁶ Au Japon également, le nombre de faillites d'entreprises était d'environ 25 % supérieur en décembre 2008 à ce qu'il était un an avant.⁷

Dans de nombreux cas, les actifs des entreprises en faillite ont plus de valeur s'ils sont conservés d'un seul tenant que s'ils sont liquidés élément par élément. Les propriétaires de ces entreprises s'efforcent de les maintenir en vie pour assurer la continuité de l'exploitation. Cela étant, ils n'ont parfois pas d'autres solutions que de vendre l'entreprise à un tiers pour éviter la liquidation lorsque leurs créanciers ne peuvent ou ne veulent pas renégocier leurs créances, ce qui est généralement le cas en période de crise du crédit. On peut donc s'attendre à une multiplication des fusions concernant des entreprises en difficulté financière dans le contexte actuel de pénurie de crédit. Ces opérations de fusion peuvent tomber sous le sens, à la fois pour les acquéreurs et pour les entreprises cibles, en période de crise financière. Reste à savoir si elles sont préjudiciables pour les consommateurs.

En temps normal, certaines de ces fusions auraient clairement été inacceptables du point de vue de la concurrence lorsque l'acquéreur et l'entreprise cible restent financièrement solides. En revanche, elles n'ont pas nécessairement d'impact réel sur l'intensité de la concurrence dès lors que l'entreprise cible se trouve en grave difficulté financière. Le cas échéant, interdire ces opérations reviendrait à appliquer à une politique de la concurrence mal inspirée. On peut se demander si les critères qui rendent recevable l'argument de l'entreprise défaillante, définis et appliqués durant la période de « grande modération », sont toujours applicables pendant la période de « grande récession » que nous traversons. La situation actuelle semble se prêter à un réexamen des modalités d'application de l'argument de l'entreprise défaillante dans le contexte du contrôle des fusions.

La grille d'analyse sous-tendant actuellement l'attitude de la plupart des pays de l'OCDE face à l'argument de l'entreprise défaillante a fait l'objet de certaines critiques. *Premièrement*, ce dispositif a été critiqué pour conduire à des enquêtes de longue haleine qui ne prennent pas en compte le fait que la situation des entreprises en difficulté peut rapidement se détériorer et qui peuvent aboutir à une liquidation contreproductive. *Deuxièmement*, il a été critiqué pour ses critères, jugés excessivement rigides notamment dans un contexte de durcissement des marchés du crédit, qui peuvent entraîner une disparition de certains actifs du marché, actifs qui peuvent être essentiels pour l'économie pour des raisons liées à l'emploi, à l'innovation, à la vigueur des exportations ou au contraire à la dépendance de l'économie vis-à-vis des exportations dans la chaîne de valeur globale d'un secteur donné.

La présente note propose un tour d'horizon des attitudes des différents pays de l'OCDE face à l'argument de l'entreprise défaillante. Elle évalue l'efficacité des politiques en vigueur et vérifie si elles permettent aux autorités de la concurrence, au cœur de la crise actuelle du crédit, de trancher efficacement

⁵ Voir les statistiques sur les faillites de l'American Bankruptcy Institute : http://www.abiworld.org/AM/Template.cfm?Section=Annual_U_S_Filings1&Template=/TaggedPage/TaggedPageDisplay.cfm&TPLID=62&ContentID=36294.

⁶ European bankruptcy laws - Out of pocket, *The Economist*, 30 décembre 2008. Téléchargeable à l'adresse suivante : http://www.economist.com/displaystory.cfm?story_id=12855376.

⁷ Voir « More firms go bankrupt in Japan ». 13 janvier 2009. Téléchargeable à l'adresse suivante : <http://news.bbc.co.uk/2/hi/business/7826009.stm>.

lorsqu'elles contrôlent des opérations de fusion. Elle examine en outre différentes options possibles en vue d'une réforme.

Nos principales conclusions sont les suivantes :

- En période de crise financière et économique, comme celle que nous traversons actuellement, de plus en plus d'entreprises peuvent se trouver en difficulté financière. Ces entreprises vont chercher à assurer leur survie à long terme en fusionnant, si possible, avec leurs concurrents directs, en meilleure santé.
- Les autorités de la concurrence peuvent donc être confrontées à un nombre croissant de fusions impliquant des entreprises en difficulté financière, certaines étant des entreprises réellement défaillantes et d'autres simplement des concurrents fragilisés ou encore des entreprises en récession. Dans certains de ces cas, l'argument de l'entreprise défaillante peut être avancé pour afin d'obtenir le feu vert pour l'opération.
- Nous avons examiné les attitudes des différents pays de l'OCDE face à l'argument de l'entreprise défaillante. Leur politique s'accompagne souvent d'un certain nombre de conditions strictes : l'entreprise présumée défaillante et ses actifs doivent être voués à disparaître du marché dans un avenir proche si la fusion n'a pas lieu et il ne doit exister aucune autre solution de rachat possible, moins préjudiciable pour la concurrence, que la fusion proposée. Il revient aux parties à l'opération de démontrer que ces conditions sont réunies. Compte tenu des preuves particulièrement solides qui sont exigées, on ne compte qu'un très petit nombre de cas dans lesquels l'argument de l'entreprise défaillante est invoqué avec succès.
- Dans la présente note, on se demandera si cet état de fait est souhaitable. Nous avons vu que les critères utilisés actuellement pour évaluer la validité de l'argument de l'entreprise défaillante sont destinés à minimiser les erreurs de type II – agrément, à tort, d'opérations de fusion ou application de mesures correctrices insuffisantes – et peuvent donc entraîner de trop nombreuses erreurs de type I – interdiction, à tort, d'opérations de fusion ou application de mesures correctrices disproportionnées. Cela est dû au fait que le cadre d'application actuel de l'argument de l'entreprise défaillante présume que certains scénarios bâtis sur un facteur déterminant, comme le maintien sur le marché d'une entreprise tronquée ou handicapée, sont nécessairement supérieurs, du point de vue de la concurrence, à l'opération de fusion faisant l'objet du contrôle. Cette présomption n'est pas toujours justifiée. Des fusions peuvent ainsi être bloquées alors même qu'elles représentent la solution la moins préjudiciable pour la concurrence.
- Nous avons également vu qu'une approche davantage fondée sur les effets, axée sur l'identification du contre-scénario le plus probable et comparant les résultats du scénario post-fusion avec ceux de ce contre-scénario réaliste peut diminuer le nombre d'erreurs de type I, mais augmenter en revanche la probabilité d'erreurs de type II. Une approche fondée sur les effets peut aussi entraîner une augmentation des coûts de mise en œuvre et un allongement de la durée des enquêtes. Elle peut être aussi avoir une issue moins prévisible.
- Les pays de l'OCDE doivent se demander si les partis pris des attitudes actuelles face à l'argument de l'entreprise défaillante sont justifiés. Qu'ils décident ou non de réexaminer ces attitudes, il n'en reste pas moins que certains de leurs aspects sont complexes et que d'autres, comme la validité de l'argument dit de « l'entreprise en récession », ne sont pas clairs. Les autorités de la concurrence du monde entier doivent sérieusement envisager de diffuser des lignes directrices sur la manière dont elles analyseront les arguments de l'entreprise ou de la division défaillante ou en récession.

Le reste de la présente note s'articule comme suit. Dans la Section 2, nous passerons en revue les attitudes d'un certain nombre de pays de l'OCDE face à l'argument de l'entreprise défaillante. Dans la Section 3, nous analyserons les conséquences éventuelles de la crise financière actuelle sur les modalités d'application de l'argument de l'entreprise défaillante dans la pratique. Dans la Section 4, nous examinerons les arguments pour ou contre l'adoption d'une approche moins rigide vis-à-vis des opérations de fusion impliquant des entreprises en difficulté. Enfin, la Section 5 conclut la présente note.

2. Attitudes face à l'argument de l'entreprise défaillante en vigueur

2.1 Introduction

Dans la section précédente, nous avons expliqué pourquoi l'argument de l'entreprise défaillante suscite un regain d'intérêt. Dans cette section, nous passons en revue les attitudes adoptées dans plusieurs pays de l'OCDE. Nous y comparons en outre les critères qui doivent être remplis dans les différents pays pour que l'argument de l'entreprise défaillante puisse être jugé recevable. Enfin, nous examinerons comment la charge de la preuve est attribuée, ainsi que la compatibilité des différentes politiques en vigueur avec les principes fondamentaux de l'analyse des fusions.

2.2 Attitudes des pays de l'OCDE face à l'argument de l'entreprise défaillante

Les pays de l'OCDE ont incorporé de différentes manières l'argument de l'entreprise défaillante à leurs politiques de contrôle des fusions. Dans certaines juridictions, cet argument est expressément analysé dans les lignes directrices relatives aux fusions. C'est notamment le cas aux États-Unis, au Japon, au Royaume-Uni et dans l'Union européenne. D'autres pays, comme l'Australie, n'incorporent pas officiellement cet argument dans leur droit de la concurrence ou dans leurs lignes directrices relatives aux fusions, mais évaluent la validité de cet argument dans le cadre du processus normal de contrôle des fusions. Cette approche au cas par cas a donné naissance à une jurisprudence qui sert, *de facto*, dans le pays concerné, de politique vis-à-vis de l'argument de l'entreprise défaillante. En ce qui concerne l'action publique, ce qui paraît importer le plus, c'est de savoir s'il existe des critères spécifiques en fonction desquels la validité de cet argument est évaluée, et non si ces critères sont inscrits dans le droit de la concurrence, dans les lignes directrices relatives aux fusions ou dans la jurisprudence. Dans les pages qui suivent, nous passons en revue les attitudes à cet égard de plusieurs pays de l'OCDE.

2.2.1 États-Unis

La Cour Suprême des États-Unis a reconnu pour la première fois la recevabilité de l'argument de l'entreprise défaillante dans l'affaire *International Shoe* en 1930.⁸ Elle a défini comme première condition d'admissibilité de l'argument le fait que l'absence de fusion pourrait entraîner la liquidation de l'entreprise. La charge de la preuve a été attribuée à l'entreprise défaillante qui a dû démontrer que ses « ressources [étaient] si réduites et ses perspectives de rétablissement si lointaines qu'elle se trouvait face à un sérieux risque de faillite. »⁹ La Cour a en outre évalué, de manière prospective, quelle serait l'intensité de la concurrence dans deux scénarios. Dans le premier scénario, l'entreprise en difficulté était rachetée par un concurrent alors que dans le second, aucune fusion n'avait lieu et les actifs de l'entreprise en difficulté étaient liquidés. La Cour a conclu que le premier scénario était l'option qui fausserait le moins la concurrence.

⁸ Voir note 2 *supra*.

⁹ *Ibid.*, § 302.

Trente ans plus tard, dans l'affaire *Philadelphia National Bank*,¹⁰ la Cour Suprême faisait remarquer que l'argument peut s'appliquer plus facilement au secteur bancaire « en raison de l'impact plus important d'une faillite bancaire par rapport à la faillite d'une entreprise ordinaire. »¹¹ Cette décision a donné à penser qu'il pouvait être important de prendre en compte les objectifs de l'argument de l'entreprise défaillante ne relevant pas de questions de concurrence. Il a fallu attendre la fin des années 60, dans l'affaire *Citizen Publishing*,¹² pour que la Cour définisse, pour la première fois, les trois conditions qui doivent être réunies pour que cet argument soit recevable : (1) l'entreprise repreneuse doit démontrer que l'entreprise cible se trouve face à un danger imminent de faillite ; (2) l'entreprise défaillante n'a pas de perspective de parvenir à se restructurer et (3) l'entreprise défaillante doit démontrer qu'elle s'est suffisamment efforcée, en toute bonne foi, de chercher un autre repreneur sans avoir réussi à trouver une autre solution de rachat susceptible d'être moins préjudiciable pour la concurrence.

Les Lignes directrices de 1997 sur les fusions horizontales [*1997 Horizontal Merger Guidelines*] publiées par le ministère américain de la Justice et la Commission fédérale du commerce admettent que :

*... une fusion n'est pas susceptible de créer ou de renforcer un pouvoir de marché, si la faillite imminente, comme définie ci-dessous, de l'une des entreprises partie à l'opération peut avoir pour effet de faire disparaître les actifs de l'entreprise en question du marché concerné. Dans ce cas, le fonctionnement du marché concerné, après la fusion, ne sera pas nécessairement moins efficace que si la fusion avait été bloquée et si les actifs avaient disparu du marché.*¹³

Les Lignes directrices énumèrent quatre conditions à la recevabilité de l'argument de l'entreprise défaillante, qui reprennent la décision rendue par la Cour Suprême dans l'affaire *Citizen Publishing* :

- l'entreprise présumée défaillante est incapable de faire face à ses obligations financières dans un avenir proche,
- elle n'est pas en mesure de réussir à se restructurer aux termes du Chapitre 11 de la Loi sur les faillites,
- elle s'est efforcée, sans succès et en toute bonne foi, de solliciter d'autres offres raisonnables de rachat de ses actifs qui auraient permis de préserver ses actifs corporels et incorporels sur le marché concerné, tout en constituant une menace moins importante pour la concurrence que la fusion proposée,
- si l'opération de rachat n'a pas lieu, les actifs de l'entreprise défaillante sont voués à disparaître du marché concerné.¹⁴

L'argument de la division défaillante

Dans certains cas, la fusion examinée implique le rachat de la division d'une entreprise. Le cas échéant, les parties à l'opération peuvent faire valoir que la division en question serait vouée à disparaître

¹⁰ Affaire *United States v Philadelphia National Bank*, 374 U.S. 321 (1963).

¹¹ Kokkoris, I. 2007. Failing firm defence under the Clayton Act. 28 *European Competition Law Review*, pp. 158-166.

¹² Affaire *Citizen Publishing Co v United States*, 394 U.S. 131, 138-139 (1969).

¹³ US Department of Justice and the Federal Trade Commission Horizontal Merger Guidelines, modifiées le 8 avril 1997, § 5.0.

¹⁴ *Ibid.*, §§ 5.1.

du marché (i) que la fusion ait concrètement lieu ou non et (ii) quelle que soit la solidité financière de société-mère. Il n'existe pas de consensus à cet égard parmi les tribunaux américains, mais les Lignes directrices de 1997 sur les fusions horizontales comportent une disposition autorisant le rachat d'une division défaillante d'une entreprise si les conditions suivantes sont réunies : (a) la division en question affiche des flux de trésorerie négatifs ; (b) il est démontré que les actifs de la division disparaîtraient du marché dans un avenir proche si l'opération de rachat n'avait pas lieu et (c) le propriétaire de la division défaillante s'est efforcé, sans succès et en toute bonne foi, de solliciter d'autres offres raisonnables d'acquisition des actifs de la division défaillante.¹⁵

L'argument de l'entreprise fragilisée

En 1974, la Cour Suprême a décidé, dans l'affaire *General Dynamics*,¹⁶ d'autoriser une fusion, faisant passer de 5 à 4 le nombre des grands intervenants du secteur, en considérant que la capacité de l'entreprise cible à affronter la concurrence dans un avenir proche était sérieusement limitée. Tout en admettant que le fait que l'entreprise ait des capacités concurrentielles limitées ne correspondait pas au niveau de preuve exigé pour que l'argument de l'entreprise défaillante soit jugé recevable, la Cour Suprême a néanmoins considéré que l'opération de rachat ne diminuerait pas significativement l'intensité de la concurrence.¹⁷ La décision rendue dans l'affaire *General Dynamics* a été appelée l'argument de l'entreprise fragilisée, de l'entreprise quasi défaillante ou de l'entreprise en récession. Cet argument a été appliqué pour la première par des tribunaux de degré inférieur dans l'affaire *US v. International Harvester Co.*,¹⁸ dans laquelle le tribunal a conclu que l'acquisition prévue n'était pas contraire au droit des fusions car l'entreprise rachetée ne disposait pas des moyens nécessaires pour exercer son activité de manière concurrentielle. L'argument de l'entreprise fragilisée s'applique lorsque l'entreprise cible, sans être en danger imminent d'insolvabilité, n'a pas la possibilité d'imposer une pression concurrentielle importante dans l'avenir en raison de la faiblesse de sa situation financière et/ou économique. Les entreprises fragilisées sont des entreprises en difficulté financière qui ne sont pas susceptibles de disparaître du marché dans un avenir proche. Leurs perspectives à long terme peuvent en fait être plutôt solides et de ce fait, on peut s'attendre à ce qu'elles soient en mesure d'exercer une pression concurrentielle dans un avenir proche, même si cette pression sera vraisemblablement plutôt faible, sur les autres participants du marché.

2.2.2 Union européenne

La Commission européenne a tenu compte pour la première fois de l'argument de l'entreprise défaillante dans l'affaire *Aérospatiale-Alenia/De Havilland*.¹⁹ Dans cette affaire, la Commission a récusé l'argument considérant que (a) De Havilland pouvait rester un concurrent indépendant et efficient sur le marché (b) qu'il pourrait y avoir d'autres repreneurs possibles pour De Havilland et que ces opérations de rachat susciteraient moins de préoccupations du point de vue de la concurrence, voire ne poseraient aucun problème.²⁰

L'argument a été invoqué pour la première fois avec succès dans l'Union européenne dans l'affaire *Kali+Salz* en 1993²¹. Dans cette affaire, la Commission a conclu qu'il n'existait pas de lien de causalité

¹⁵ *Ibid.*, §§ 5.2.

¹⁶ Affaire *United States c General Dynamics Corp.* (1974) 415 U.S. 486.

¹⁷ *Ibid.*, § 510 – 511.

¹⁸ 564 F.2d 769, 774 (7th Cir. 1977).

¹⁹ Voir note 4 *supra*.

²⁰ *Ibid.*, §§ 31.

²¹ Affaire IV/M308 *Kali + Salz/MdK/Treuhand*. JO 1994 L186/30.

strict entre la fusion proposée et la perte de concurrence anticipée sur le marché allemand, puisque des effets de même ampleur pourraient se produire si la fusion n'avait pas lieu du fait que l'entreprise cible aurait disparu du marché. La Commission a conclu que (1) l'entreprise rachetée disparaîtrait du marché dans un avenir proche si elle n'était pas rachetée par une autre entreprise ; (2) l'entreprise repreneuse absorberait en tout état de cause les parts de marché de l'entreprise rachetée si celle-ci était contrainte à quitter du marché et (3) et qu'il n'existait pas d'autre repreneur possible moins préjudiciable pour la concurrence.

Dans son appel de la décision de la Commission européenne, le gouvernement français a jugé trop restrictif le critère de l'absorption de la totalité des parts de marché de l'entreprise défaillante par l'entreprise repreneuse si la fusion n'a pas lieu. Cependant la Cour de Justice des Communautés européennes a confirmé l'analyse de la Commission sur l'argument de l'entreprise défaillante.²² Elle a fait valoir que le critère d'« absorption des parts de marché » vise à assurer qu'il n'existe pas de lien de causalité entre la dégradation de la structure concurrentielle du marché et l'opération. La Cour relevait notamment :

Dès lors, le critère de l'absorption des parts de marché, bien qu'il ne soit pas considéré par la Commission elle-même comme suffisant à lui seul pour exclure le caractère préjudiciable de l'opération de concentration pour le jeu de la concurrence, concourt à assurer la neutralité de cette opération par rapport à la dégradation de la structure concurrentielle du marché, ce qui est conforme à la notion de causalité figurant à l'article 2, paragraphe 2, du règlement.²³

La Commission a longtemps appliqué les critères retenus dans l'affaire *Kali+Salz* de manière restrictive. Ainsi, dans l'affaire *Saint-Gobain/Wacker-Chemie/NOM*, elle a conclu que Wacker-Chemie pouvait trouver des solutions de rechange et que ces solutions auraient un effet moins important sur la concurrence.²⁴ De même, dans l'affaire *Blokker/Toys "R" US (II)*, la Commission a conclu que [la condition de] l'absence de lien de causalité entre l'opération de concentration et ses effets sur le marché n'est en l'occurrence pas établie [car il] n'est pas prouvé que la totalité de la part de marché de Toys "R" Us reviendra à Blokker. »²⁵

La Commission n'a jamais admis l'argument de l'entreprise défaillante après l'affaire *Kali+Salz* jusqu'en 2001, année où elle a autorisé la fusion *BASF/Eurodiol/Pantochim*.²⁶ Cette décision a marqué une étape importante dans l'évolution de l'argument dans l'Union européenne. Le « critère de l'absorption des parts de marché » a été jugé trop restrictif. La Commission a fait valoir qu'il suffit de démontrer que les actifs de l'entreprise défaillante disparaîtraient inévitablement du marché si la fusion n'était pas réalisée et qu'il n'existe pas d'autre alternative de rachat moins dommageable pour la concurrence que la concentration notifiée.²⁷

²² Affaires jointes C-68/94 et C-30/95 République française et Société commerciale des potasses et de l'azote (SCPA) et Entreprise minière et chimique (EMC) contre Commission des Communautés européennes [1998] Rec. p. I-1375.

²³ Id. §116.

²⁴ Affaire IV/M.774 - Saint-Gobain/Wacker- Chemie/NOM. JO 1997 L247/1. Pour une analyse de cette affaire, voir Kokkoris, I. 2006. Failing firm defence in the European Union: A panacea for mergers? 27 *European Competition Law Review* 2006, pp. 494-509.

²⁵ Affaire IV/M.890 Blokker/Toys "R" US (II), JO 1998 L316/1.

²⁶ Affaire COMP/M.2314 BASF/Eurodiol/Pantochim. JO 2002 L132/45.

²⁷ *Ibid.*, §§ 142.

Les Lignes directrices sur l'appréciation des concentrations horizontales exposent la position actuelle de la Commission concernant l'argument.²⁸ Il y est précisé que la Commission « peut conclure qu'une opération de concentration, qui pose par ailleurs des problèmes de concurrence, est néanmoins compatible avec le marché commun si l'une des parties à l'opération est une entreprise défaillante. La condition fondamentale est que la détérioration de la structure de la concurrence qui se produirait après la concentration ne puisse pas être considérée comme étant causée par cette opération. »²⁹ La recevabilité de l'argument de l'entreprise défaillante exige d'établir que :

*En premier lieu, l'entreprise prétendument défaillante serait, dans un proche avenir, contrainte de quitter le marché en raison de ses difficultés financières si elle n'était pas reprise par une autre entreprise. Deuxièmement, il n'existe pas d'autre alternative de rachat moins dommageable pour la concurrence que la concentration notifiée. Troisièmement, si la concentration n'était pas réalisée, les actifs de l'entreprise défaillante disparaîtraient inévitablement du marché.*³⁰

De plus, les Lignes directrices attribuent clairement la charge de la preuve en cas d'invocation de l'argument de l'entreprise défaillante : « C'est aux parties notifiantes qu'il incombe de produire en temps voulu toutes les informations nécessaires pour démontrer que la détérioration de la structure de la concurrence qui se produira après la concentration n'est pas causée par celle-ci. »³¹

L'argument de la division défaillante

La Commission européenne a tenu compte pour la première fois de l'argument de la division défaillante dans l'affaire *Bertelsmann/Kirch/Premiere*.³² Elle a analysé l'opération de concentration en utilisant les critères appliqués aux entreprises défaillantes tout en précisant qu'il faut alors « exiger des preuves particulièrement solides. »³³ Cette approche plus restrictive a été justifiée par un certain nombre de raisons, notamment le fait que la société-mère peut utiliser des méthodes comptables créatives pour susciter l'illusion d'une défaillance de la division. Les parties à l'opération de concentration n'ont pas réussi à convaincre la Commission qu'il n'existait pas de lien de causalité entre l'opération et la dégradation de la structure concurrentielle et l'argument de la division défaillante a donc été rejeté.

L'argument de l'entreprise fragilisée

Dans l'affaire *Newscorp/Telepiu*,³⁴ la Commission a également récusé l'argument de la division défaillante invoqué. Elle a cependant autorisé l'opération de concentration en tenant compte des réalités économiques du secteur. Elle a conclu qu'il était peu probable que l'entreprise rachetée puisse constituer une menace très importante pour la concurrence dans l'avenir en raison de sa mauvaise santé financière. Cette décision est interprétée comme une définition de l'argument de l'entreprise fragilisée qui n'est guère dissemblable de celle adoptée dans l'affaire *General Dynamics* aux États-Unis.³⁵

²⁸ Lignes directrices sur l'appréciation des concentrations horizontales au regard du règlement du Conseil relatif au contrôle des concentrations entre entreprises (2004/C 31/03).

²⁹ *Ibid.*, §§ 89.

³⁰ *Ibid.*, §§ 90.

³¹ *Ibid.*, §§ 91.

³² Affaire COMP/M.993 Bertelsmann/Kirch/Premiere. JO 1999 L53/1.

³³ *Ibid.*, §§ 71.

³⁴ Affaire COMP/M.2876 Newscorp/Telepiu. JO 2004 L110/73.

³⁵ Voir Caffarra, C *et al.* 2003. Merger to Monopoly. 11 *European Competition Law Review*, p. 625.

Dans son enquête sur l'affaire *KLM/Martinair*,³⁶ la Commission a évalué les pressions concurrentielles que Martinair exercerait si l'opération de concentration avec KLM n'avait pas lieu. La Commission a admis que les services long courriers destinés au transport de passagers seraient probablement supprimés dans un avenir proche en l'absence de fusion avec KLM.³⁷ Elle a conclu que malgré les mesures de restructuration, la situation financière de Martinair semblait s'être considérablement détériorée³⁸ et qu'il pourrait être très difficile pour Maersk de trouver un autre acheteur pour sa participation de 50 % dans Martinair.³⁹ La Commission n'a pas officiellement appliqué l'argument de la division défaillante dans cette affaire. Elle a néanmoins conclu que les effets spécifiques de l'opération seraient limités :

*La situation spécifique de Martinair rend probable l'affaiblissement de la pression concurrentielle exercée par cette dernière dans un proche avenir. Il peut donc être conclu des éléments susmentionnés que les effets spécifiques de l'opération envisagée sur les activités de transport aérien des parties semblent être limités.*⁴⁰

Cette décision semble confirmer que l'argument de l'entreprise fragilisée peut être appliqué en Europe à condition de démontrer dans les faits que la fusion constitue la solution aux problèmes financiers de l'entreprise défaillante qui est la moins préjudiciable pour la concurrence.

2.2.3 Australie

L'Australie n'a pas officiellement incorporé l'argument de l'entreprise défaillante dans sa Loi sur les pratiques commerciales (Article 50) ou dans les Lignes directrices sur les fusions adoptées par la l'Australian Competition and Consumer Commission (ACCC). Cela étant, l'argument de l'entreprise défaillante peut constituer un élément essentiel de la contre-analyse dans le cadre de laquelle l'ACCC détermine ce que serait probablement la concurrence sur le marché si l'opération de fusion n'avait pas lieu⁴¹. » L'ACCC a récemment admis cet argument dans l'une des décisions qu'elle a rendue sur une opération de fusion.⁴²

2.2.4 Canada

Selon les Lignes directrices pour l'application de la Loi publiées par le Bureau de la concurrence du Canada, une entreprise est considérée comme une entreprise « en déconfiture » dans les cas suivants : (i) elle est insolvable ou le deviendra vraisemblablement ; (ii) elle a entamé ou entamera vraisemblablement une procédure de faillite volontaire ; (iii) elle a été mise sous séquestre ou en faillite, ou le sera vraisemblablement.⁴³

³⁶ Affaire COMP/M.5141 – KLM/ Martinair. JO 2009 C51/04.

³⁷ *Ibid.*, §§ 163.

³⁸ *Ibid.*, §§ 166.

³⁹ *Ibid.*, §§ 174. Les 50 % restants étaient déjà aux mains de KLM avant la fusion.

⁴⁰ M.5141, §§ 175.

⁴¹ Poddar, D. 2009. The global financial crisis – will it affect merger review? Article du cabinet de droit commercial australien Mallesons Stephan Jacques. Téléchargeable à compter du 05-08-2009 à l'adresse Internet suivante <http://www.mallesons.com/publications/2009/Jun/9918866w.htm>.

⁴² ACCC. 2009. Public competition assessment of 13 March 2009 in the case P & M Quality Smallgoods Pty Ltd - proposed acquisition of Hans Continental Smallgoods Pty Ltd.

⁴³ Bureau de la concurrence du Canada. 2004. Lignes directrices pour l'application de la Loi. Septembre 2004, Partie 9 – Déconfiture de l'entreprise.

Le Bureau de la concurrence du Canada vérifie si la faillite est imminente ou probable ; s'il existe une solution de rechange à la fusion proposée qui entraînera vraisemblablement un niveau de concurrence nettement plus élevé ; si l'entreprise qui se trouve dans une situation difficile pourrait éviter la déconfiture et survivre comme concurrent réel en réduisant l'étendue de ses activités ; si la liquidation a de grandes chances de se traduire, sur une part sensible du marché, par un niveau de concurrence nettement plus élevé que celui qui existerait si la fusion en question avait lieu.⁴⁴

Les Lignes directrices énumèrent en outre les renseignements et les documents types que le Bureau peut demander pendant le contrôle d'une opération de fusion, afin d'évaluer dans quelle mesure l'argument de l'entreprise défaillante est recevable. Ces renseignements et documents incluent les états financiers de l'entreprise, la position de l'entreprise sur le marché et ses relations avec ses créanciers et ses fournisseurs.

2.2.5 France

Dans l'affaire *Moulinex*,⁴⁵ le Conseil d'État a accepté la possibilité d'invoquer l'argument de l'entreprise défaillante si trois conditions sont réunies, autrement dit « s'il est établi en premier lieu que ces difficultés entraîneraient la disparition rapide de la société en l'absence de reprise, en deuxième lieu, qu'il n'existe pas d'autre offre de reprise moins dommageable pour la concurrence et, en troisième lieu, que la disparition de la société en difficulté ne serait pas moins dommageable pour les consommateurs que la reprise projetée ». Cette décision statuait sur l'acquisition d'une entreprise en redressement judiciaire par son concurrent direct. Le ministère des Finances avait autorisé l'opération sur la base des critères définis dans l'affaire *Kali+Salz*⁴⁶ pour invoquer l'argument de l'entreprise défaillante. Le Conseil d'État a annulé la décision d'agrément, considérant que le ministère des Finances n'avait pas de motifs suffisants pour conclure que les concurrents n'auraient pu acquérir les marques de l'entreprise liquidée ou n'aurait pu remplacer l'entreprise défaillante sur le marché si celle-ci disparaissait. Autrement dit, le Conseil d'État a conclu que les conditions (2) et (3) n'étaient pas établies.

2.2.6 Allemagne

Le Bundeskartellamt admet l'argument de l'entreprise défaillante dans le cadre d'enquêtes portant sur des fusions pour lesquelles il peut être démontré que l'opération n'est pas la cause de la dégradation anticipée de la concurrence. Les conditions suivantes doivent être réunies pour prouver que ce lien de causalité n'existe pas :

- Si l'opération n'avait pas lieu, l'entreprise disparaîtrait du marché (« Sanierungsbedürftigkeit »),⁴⁷
- Il n'existe pas d'autres repreneurs possibles pour l'entreprise défaillante qui constitueraient une menace moins sérieuse pour la concurrence (« Nachweis eines fehlenden alternativen Erwerbers »).⁴⁸

⁴⁴ *Ibid.*

⁴⁵ Décision du Conseil d'État, Section du contentieux, du 6 février 2004, N°s 249262-252297-252350-252809, SOCIÉTÉ ROYAL PHILIPS ELECTRONIC et autres.

⁴⁶ Voir note 21 *supra*.

⁴⁷ Décision du Bundeskartellamt du 06-06-2007 dans l'affaire LBK/Mariahilf, B 3 - 85111-Fa-6/07, § 235-253.

⁴⁸ *Ibid.*, § 254-261.

- Si la fusion n'a pas lieu, les parts de marché reviendront vraisemblablement, en tout état de cause, en totalité ou dans une très large mesure, au repreneur éventuel (« Verstärkung auch bei Ausscheiden »⁴⁹)

Ces conditions sont identiques à celles appliquées aux termes du droit communautaire avant la décision de la Commission européenne rendue dans l'affaire *BASF/Eurodiol/Pantochim*. Ces critères ont été récemment appliqués dans l'affaire *LBK/Mariahilf*.⁵⁰ En l'occurrence, les parties à l'opération de fusion n'ont pas pu convaincre le Bundeskartellamt que les trois critères exigés étaient réunis.

2.2.7 Irlande

Les Lignes directrices sur l'analyse des fusions, publiées par l'Irish Competition Authority examinent l'argument de l'entreprise défaillante. Les critères qui y sont énumérés sont les suivants :

- L'entreprise présumée défaillante doit être dans l'incapacité de faire face à ses obligations financières dans un avenir proche ;
- L'entreprise n'a pas la moindre possibilité de parvenir à se restructurer dans le cadre d'une procédure de redressement judiciaire ;
- L'entreprise s'est efforcée, en toute bonne foi et de manière vérifiable, à solliciter d'autres offres de reprise raisonnables qui éviteraient à ses actifs, corporels et incorporels, de disparaître du marché concerné et qui constitueraient une menace moins importante pour la concurrence que l'opération de fusion proposée [...] ;
- Si l'opération n'avait pas lieu, les actifs de l'entreprise défaillante disparaîtraient définitivement du marché.⁵¹

Les Lignes directrices précisent toutefois que ces conditions sont « rarement réunies dans la pratique. »⁵²

2.2.8 Japon

L'argument de l'entreprise défaillante est défini dans la Partie IV des Lignes directrices sur les concentrations de la Japan Fair Trade Commission (JFTC).⁵³ Ces Lignes directrices précisent que :

La possibilité qu'une concentration d'entreprises puisse avoir pour effet substantiel de réduire la concurrence dans un domaine commercial donné est généralement jugée limitée si l'une des parties à l'opération est excessivement endettée ou si elle est dans l'incapacité de financer son fonds de roulement et si elle risque de se trouver en faillite et de disparaître du marché dans un avenir proche et s'il est difficile de trouver un autre repreneur qui puisse assurer la survie de la

⁴⁹ *Ibid.*, § 262-267.

⁵⁰ *Ibid.*

⁵¹ Irish Competition Authority. 2002. Notice in respect of Guidelines for Merger Analysis. 16 décembre 2002, § 5.17.

⁵² *Ibid.*, §5.17.

⁵³ Japan Fair trade Commission. 2007. Guidelines to application of the Anti-monopoly Act concerning review of business combination [Lignes directrices relatives à l'application de la Loi anti-monopole concernant le contrôle des concentrations d'entreprises].

*partie défaillante en procédant à une opération de concentration qui aurait moins d'impact sur la concurrence que n'en aurait le repreneur effectif, autrement dit l'autre partie à l'opération.*⁵⁴

En d'autres termes, l'argument de l'entreprise défaillante est admis (a) si l'entreprise cible est vouée à disparaître du marché dans un avenir proche en raison de ses difficultés économiques (faillite ou graves problèmes financiers) ; et (b) s'il n'existe pas d'autre possibilité de reprise moins préjudiciable pour la concurrence.

2.2.9 Corée

La politique de la Korean Fair Trade Commission (KFTC) relative à l'argument de l'entreprise défaillante impose aux parties à l'opération de fusion de démontrer que les actifs de l'entreprise en question ne seront probablement plus utilisés si l'opération n'a pas lieu et qu'il est peu probable qu'une opération moins préjudiciable pour la concurrence soit possible.⁵⁵

Le rachat de Kia par Hyundai est une opération de fusion pour laquelle la doctrine de l'entreprise défaillante a été invoquée avec succès. Considérant que Kia était vouée à la faillite et dans l'incapacité de se redresser, l'opération a été approuvée.⁵⁶ En revanche, lors du rachat par SK Telecom de Shinsegi Telecom, l'argument a été invoqué par les parties à l'opération, mais la KFTC n'a pas estimé que Shinsegi serait, d'un point de vue réaliste, contrainte à quitter le marché, ni que ses actifs seraient dépréciés si la fusion avec SK Telecom n'avait pas lieu.⁵⁷

2.2.10 Royaume-Uni

L'Office of Fair Trading (OFT) et la Competition Commission (CC) reconnaissent tous deux l'argument de l'entreprise défaillante dans leurs lignes directrices actuelles sur les fusions :

*Lorsqu'il est invoqué, l'argument de l'entreprise défaillante consiste essentiellement à dire que l'entreprise cible sortira du marché si la fusion n'a pas lieu et que les éventuels préjudices à la concurrence ne doivent donc pas être imputés à la fusion.*⁵⁸

*Lorsque la CC estime qu'une des entreprises ferait faillite, il se peut que la situation sur le marché sans la fusion soit comparable à celle qui résulterait de la fusion et la fusion en soi ne saurait donc entraîner une modification de l'intensité de la concurrence sur le marché.*⁵⁹

Selon les Lignes directrices de l'OFT, pour qu'un recours à l'argument de l'entreprise défaillante soit examiné, deux conditions doivent être remplies : (a) la disparition inévitable de l'entreprise cible en l'absence de fusion et (b) le fait qu'il n'y ait aucune solution de rechange réaliste et nettement moins

⁵⁴ *Ibid.*, Part IV, (8), A-B, pp. 32-33.

⁵⁵ Yun, M. 2002. Policies to Improve Monopolistic/Oligopolistic Market Structure. Korea Institute for International Economic Policy. Téléchargeable à compter du 16-09-2009 à l'adresse Internet suivante : <http://unpan1.un.org/intradoc/groups/public/documents/APCITY/UNPAN014166.pdf>.

⁵⁶ *Ibid.*

⁵⁷ *Ibid.*

⁵⁸ Office of Fair Trading. 2008. Reformulation de la position de l'OFT concernant les acquisitions d'« entreprises défaillantes ». Décembre 2008, p. 4.

⁵⁹ Competition Commission. 2003. Merger references: Competition Commission Guidelines. Juin 2003, p. 3.61.

préjudiciable pour la concurrence.⁶⁰ L'OFT précise qu'un scénario où l'entreprise cible fait faillite et où ses actifs sont transférés aux intervenants restants du marché peut faire partie des solutions « de rechange nettement moins préjudiciable pour la concurrence ».

Les Lignes directrices de la CC précisent aussi deux conditions à remplir : (a) l'entreprise sera incapable de faire face à ses obligations financières dans un avenir proche et (b) la société est incapable de réussir sa restructuration.⁶¹ Les Lignes directrices de la CC présentent aussi des exemples de diverses circonstances que la CC prendra en compte, dont la possibilité que l'entreprise défaillante soit rachetée par une entreprise différente et l'examen de la répartition des parts de marché de l'entreprise défaillante entre les intervenants restants si elle disparaît du marché.

L'OFT et la CC reconnaissent aussi l'argument de l'entreprise défaillante dans leur projet récemment publié de lignes directrices communes sur les fusions.⁶² Ce projet définit trois conditions qui doivent être remplies pour qu'un recours à l'argument de l'entreprise défaillante soit examiné : (1) le caractère inévitable de la disparition de l'entreprise en question ; (2) le fait qu'il n'existe pas d'autre repreneur nettement moins préjudiciable pour la concurrence ; et (3) la faillite de l'entreprise n'est pas une solution nettement moins anticoncurrentielle que la fusion.⁶³

L'argument de l'entreprise défaillante a été invoqué dans le cadre de fusions sur le marché britannique, notamment dans les affaires First West Yorkshire,⁶⁴ Tesco/Kwik Save,⁶⁵ CDMG Group/Ferryways NV/Searoads Stevedores NV,⁶⁶ Homebase/Focus DIY,⁶⁷ Stagecoach/Eastbourne Buses/Cavendish Motor Services⁶⁸ et HMV/Zavvi.⁶⁹

En ce qui concerne l'affaire *HMV/Zavvi*, l'OFT a examiné l'acquisition proposée de Zavvi par HMV alors que Zavvi était déjà placé sous administration judiciaire (autrement dit, en faillite). L'OFT a conclu qu'une acquisition par HMV ne créait pas de perspective réaliste d'une diminution substantielle de la concurrence.⁷⁰ L'OFT a souligné explicitement qu'il était peu probable que Zavvi puisse éviter la faillite

⁶⁰ Voir note 58 *supra*, p. 10.

⁶¹ Voir note 59 *supra*, p. 3.62.

⁶² OFT/CC. 2009. Consultation document: Merger assessment guidelines. Avril 2009, p. 4.27.

⁶³ *Ibid.*, pp. 4.27-4.33.

⁶⁴ Décision de l'OFT du 26 mai 2005, ME/1517/05 First West Yorkshire/Black Prince Buses – Acquisition attendue par First West Yorkshire Limited de Black Prince Buses Limited.

⁶⁵ Décision de l'OFT du 11 décembre 2007, ME/3387/07 Tesco/Kwik Save – Acquisition attendue par Tesco Stores Limited de cinq anciens magasins de Kwik Save (Handforth, Coventry, Liverpool, Barrow-in-Furness et Nelson).

⁶⁶ Décision de l'OFT du 24 janvier 2008, ME/3145/07 CDMG Group/Ferryways NV/Searoads Stevedores NV – Acquisition réalisée par le groupe d'entreprises CDMG de Ferryways NV et de Searoad Stevedores NV.

⁶⁷ Décision de l'OFT du 7 août 2008, ME/3427/07 Homebase/Focus – Acquisition réalisée par Home Retail Group plc de 27 magasins de Focus (DIY) Ltd.

⁶⁸ Rapports sur les conclusions provisoires de la Competition Commission du 06-08-2009 : Les acquisitions réalisées par Stagecoach Group PLC de Eastbourne Buses Limited et de Cavendish Motor Services Limited, p. 6.3.

⁶⁹ Décisions de l'OFT du 14 mai 2009 : ME/4036/09 Acquisition attendue par HMV de 15 magasins Zavvi.

⁷⁰ *Ibid.*, § 53.

même après une réorganisation⁷¹ étant donné les « difficiles conditions économiques et commerciales actuelles et le montant prohibitif de l'investissement nécessaire pour faire redémarrer l'entreprise Zavvi. »⁷² Il a également conclu qu'il n'y avait pas d'autres acheteurs réalistes, pour les magasins Zavvi, qui soient nettement moins préjudiciables pour la concurrence malgré les efforts en termes de marketing de l'administrateur et des propriétaires respectifs.⁷³ Aucun autre détaillant exerçant ses activités sur le même marché que les parties n'avait exprimé son intérêt.⁷⁴ Pour certains magasins de Zavvi, un deuxième acheteur potentiel a été identifié. Son offre n'était toutefois pas réaliste compte tenu des conditions commerciales défavorables et de la vision à court terme de son modèle d'entreprise.⁷⁵ Enfin, l'OFT a conclu que la concurrence ne serait pas plus forte si les actifs de Zavvi disparaissaient du marché.⁷⁶

En revanche, dans le cas *Stagecoach/Eastbourne Buses/Cavendish Motor Services*, les conclusions provisoires de la CC récusent l'argument de l'entreprise défaillante invoqué par les parties, car il n'existe pas de preuve irréfutable selon laquelle les entreprises ciblées disparaîtraient du marché dans un proche avenir.⁷⁷ De plus, la CC considère que les entreprises défaillantes peuvent recourir à des mesures de restructuration leur permettant de retrouver une viabilité financière et que d'autres acheteurs que Stagecoach sont disponibles.⁷⁸

2.3 Comparaison des politiques relatives à l'argument de l'entreprise défaillante

Il ressort clairement de l'examen qui précède que les critères pour accepter l'argument de l'entreprise défaillante sont assez semblables dans les différents pays de l'OCDE. Les autorités de la concurrence demandent des preuves qu'à défaut d'une fusion, l'entreprise cible serait très probablement contrainte de quitter le marché dans un proche avenir. Elles exigent une comparaison entre les effets concurrentiels de la fusion proposée et ceux d'opérations alternatives ou d'une réorganisation interne. Elles requièrent des preuves que les actifs de l'entreprise quitteront inévitablement le marché en l'absence de fusion. Enfin, la charge de la preuve relève des parties à l'opération.

Malgré ces similitudes, cependant, il existe aussi un certain nombre de différences. Premièrement, bien que dans certaines juridictions, comme l'UE et les États-Unis, il soit explicitement précisé que la disparition de l'entreprise défaillante doit être provoquée par ses difficultés financières, la condition de la défaillance de l'entreprise cible n'est pas toujours explicitement mentionnée comme l'un des critères permettant d'invoquer ce moyen de défense avec succès. Dans un certain nombre de pays européens, il est fait référence au fait que « l'entreprise acquise disparaîtrait rapidement si elle n'était pas reprise »⁷⁹, à la « cessation des activités »⁸⁰ ou à « la disparition à court terme de l'entreprise défaillante »⁸¹, mais pas

⁷¹ Voir note 69 *supra*, p. 33.

⁷² *Ibid.*, § 36.

⁷³ *Ibid.*, § 30.

⁷⁴ *Ibid.*, § 43.

⁷⁵ *Ibid.*, § 49.

⁷⁶ *Ibid.*, § 52.

⁷⁷ Voir note 68 *supra*, p. 6.4.

⁷⁸ *Ibid.*, § 6.4-6.5.

⁷⁹ Direction générale de la concurrence, de la consommation et de la répression des fraudes (DGCCRF). 2007. Lignes directrices relatives au contrôle des concentrations ; procédure et analyse, p. 444.

⁸⁰ Politique concernant l'argument de la défaillance d'entreprise de la Commission de la concurrence grecque. Voir http://www.concurrences.com/rubrique.php?id_rubrique=626&lang=en.

explicitement aux difficultés financières comme cause sous-jacente de la disparition de l'entreprise défaillante. Une telle approche peut avoir des conséquences importantes si elle laisse entrevoir qu'il est possible de recourir avec succès à l'argument de l'entreprise défaillante dans des secteurs en perte de vitesse confrontés à des surcapacités, où des fusions n'ont pas lieu pour conserver les actifs d'entreprises connaissant des difficultés financières sur le marché, mais pour parvenir à une rationalisation ordonnée du secteur et probablement préjudiciable pour la concurrence.

Deuxièmement, il semble que des différences subtiles existent dans les analyses contrefactuelles qu'exigent les différentes juridictions. Toutes les juridictions requièrent que la fusion proposée soit comparée à un contre-scénario sans fusion et à un contre-scénario dans le cadre duquel l'entreprise défaillante est vendue à un autre acheteur. Or, certaines juridictions exigent également la démonstration explicite que les effets anticoncurrentiels de la fusion ne seront pas plus graves que ceux qui découleraient de la réorganisation ou de la restructuration de l'entreprise défaillante.⁸²

Troisièmement, des différences existent au niveau des efforts exigés des entreprises défaillantes pour attirer des offres d'acquisitions alternatives, et éventuellement moins préjudiciables pour la concurrence. Les États-Unis (« l'entreprise s'est efforcée, sans succès et en toute bonne foi »⁸³) et l'Irlande (« l'entreprise s'est efforcée, en toute bonne foi et de manière vérifiable »⁸⁴) imposent tous deux aux parties à l'opération de démontrer qu'elles ont pris des mesures raisonnables pour solliciter des solutions de rechange. D'autres pays se contentent d'enquêter sur l'existence de ces autres opérations sans exiger formellement de la part de l'entreprise défaillante qu'elle démontre qu'elle a envisagé, analysé et rejeté d'autres options. Dans la pratique, le type de preuves exigées peut être assez semblable dans différents pays, sachant que la charge de la preuve revient aux parties à la fusion.

Enfin, même si on a vu que la Commission européenne n'exige plus que la totalité des parts de marché de l'entreprise défaillante revienne à l'acquéreur en l'absence de fusion, plusieurs pays de l'UE n'ont pas intégré ce changement dans leurs principes.⁸⁵ L'évolution des principes sur la base de la jurisprudence et l'application limitée de l'argument de l'entreprise défaillante peuvent expliquer ce retard. Il semble, par conséquent, probable que ces pays mettront à jour leurs principes et tiendront compte des nouvelles exigences dès que l'argument de l'entreprise défaillante sera invoqué dans une nouvelle affaire.

2.4 Charge de la preuve

Les critères pour recourir avec succès à l'argument de l'entreprise défaillante dans toutes les juridictions examinées précédemment sont très exigeants et, par conséquent, la charge de la preuve imposée aux parties à la fusion est très contraignante. Les parties doivent montrer que les actifs de

⁸¹ Décision de la Nederlandse Mededingingsautoriteit (Nma, autorité de la concurrence néerlandaise) du 12 mai 2000 concernant l'affaire 1538 De Telegraaf – De Limburger, p. 226.

⁸² Voir par exemple les règles adoptées au Royaume-Uni (« l'entreprise est incapable de réussir sa restructuration » - Competition Commission (2003) *op. cit.* à la note 59, § 3.62), en Irlande (« Il n'existe pas de possibilité que l'entreprise réussisse sa réorganisation dans le cadre de la procédure d'Examinership [redressement judiciaire] » - Irish Competition Authority (2002) *op. cit.* à la note 51) et aux États-Unis (« elle ne serait pas capable de réussir à se réorganiser aux termes du Chapitre 11 du Bankruptcy Act [loi sur les faillites] » - Ministère de la Justice américain et FTC (1997) *op. cit.* à la note 13).

⁸³ Voir Ministère de la Justice américain et FTC (1997) *op. cit.* à la note 13.

⁸⁴ Voir Irish Competition Authority (2002) *op. cit.* à la note 51.

⁸⁵ Par exemple la Bulgarie, la Grèce, le Danemark, la Suisse et l'Italie n'ont pas encore remplacé l'ancien critère par le nouveau avancé dans la décision de la Commission dans l'affaire BASF/Eurodiol/Pantochim. Voir http://www.concurrences.com/rubrique.php3?id_rubrique=626&lang=en.

l'entreprise cible disparaîtraient du marché dans un proche avenir s'il n'y avait pas de fusion. Cela nécessite de prouver que la valeur de l'entreprise en activité est inférieure à sa valeur de liquidation. Cette comparaison donnera une bonne indication pour décider s'il vaut mieux maintenir ou non l'entreprise « en vie ». Cependant, la preuve ne peut être absolue dans la mesure où elle dépend d'un certain nombre d'hypothèses concernant les futurs flux de trésorerie, les taux d'actualisation et les taux de rendement. De plus, la valeur de l'entreprise en activité va dépendre de l'attitude des parties prenantes concernant une éventuelle restructuration financière et/ou économique. Et la valeur de liquidation de l'entreprise ne peut être déterminée sans une analyse détaillée de la santé du secteur sur lequel elle opère. Comme chacun sait, les actifs d'une entreprise ont plus de valeur quand ils sont vendus à des concurrents dans un secteur florissant que dans un secteur en perte de vitesse. Enfin, dans bien des cas, le moment de sa disparition peut être difficile à établir précisément.

Les parties doivent aussi montrer qu'il n'y a pas d'autre opération possible aux effets moins préjudiciables pour la concurrence. Cette condition est exigeante également sur le plan analytique. S'il est déjà difficile en soi de prévoir les effets d'une fusion qui sont préjudiciables pour la concurrence, la comparaison prospective des effets de deux fusions concurrentes est un exercice bien plus complexe. Dans la pratique, cela peut nécessiter des informations détaillées sur les acquéreurs potentiels dont ne dispose pas l'entreprise défaillante sauf si elle engage des négociations avec plusieurs parties à la fois. Cette démarche peut elle aussi s'avérer extrêmement complexe et longue car les alternatives potentielles sont nombreuses.

Dans l'affaire *Deloitte & Touche/Andersen*,⁸⁶ la Commission européenne a examiné un contre-scénario dans le cadre duquel les actifs d'Andersen seraient rachetés par les quatre grands cabinets d'audit et comptables (*Big Four*) restants et un deuxième scénario où il n'y aurait pas de rachat et où les clients existants d'Andersen seraient dispersés entre les quatre grands cabinets restants.⁸⁷ Le deuxième scénario comportait deux sous-scénarios différents sur l'attribution des parts de marché : (i) des parts égales du marché d'Andersen entre les quatre grands intervenants ; et (ii) une répartition des parts de marché d'Andersen en proportion des parts des quatre grands cabinets.

De plus, ce genre de contre-analyse est un exercice problématique d'un point de vue commercial. Une société en difficulté est par définition dans une situation très précaire. Exiger d'elle qu'elle s'exhibe dans un concours de beauté devant tous ses concurrents pourrait nuire à sa capacité de vente sur le marché et accélérer sa disparition. L'entreprise devra dépenser des ressources pour rechercher d'autres acquéreurs raisonnables et détourner des ressources d'activités plus productives. Il est probable que les concurrents utilisent cette recherche pour en tirer un avantage concurrentiel, dissuadant les clients de se fournir auprès d'une entreprise sur le point de quitter le marché.⁸⁸ Ces réalités commerciales doivent être prises en compte lorsque l'on vérifiera si l'entreprise défaillante a satisfait à l'exigence de rechercher des alternatives et de s'engager dans des négociations parallèles.⁸⁹

Enfin, les parties sont tenues de montrer que les actifs de l'entreprise cible disparaîtront du marché s'il n'y avait pas de fusion. Plus précisément, les parties à la fusion doivent exclure la possibilité que certains actifs de l'entreprise défaillante puissent être rachetés par des tiers en l'absence de fusion. En d'autres termes, les parties doivent fournir des preuves qu'aucun concurrent ou nouvel entrant potentiel sur les

⁸⁶ Décision de la Commission européenne du 1^{er} juillet 2002 concernant l'affaire M.2810 Deloitte & Touche/Andersen (Royaume-Uni).

⁸⁷ *Ibid.*, § 49.

⁸⁸ Shehadeh, R., J. Larson et I. Knable Gotts. The effect of financial distress on business investment: implications for merger reviews. In *Antitrust*, Printemps 2009, Vol. 23, n°2, p. 12.

⁸⁹ Voir Lignes directrices sur l'appréciation des concentrations horizontales de la CE, note 34 *supra*, p. 217.

marchés concernés par l'opération ne pourrait être intéressé par une part significative des actifs de l'entreprise défaillante.⁹⁰ Cette démarche est manifestement lourde. Pour s'en tenir strictement à cette exigence, il faudrait envisager la possibilité d'acquisitions partielles dans le cadre d'une procédure de liquidation officielle ou non. Cela exige d'identifier les actifs qui peuvent intéresser des concurrents existants ou potentiels, en évaluant la probabilité que ces actifs finissent, en cas de liquidation de l'entreprise, entre les mains d'acquéreurs qui constituaient la concurrence avant l'opération et en évaluant le temps nécessaire pour que ces transferts d'actifs se matérialisent. Cela n'est pas rien.

2.5 *Contre-analyse et argument de l'entreprise défaillante*

Pour évaluer les dommages potentiels pour la concurrence résultant d'une fusion, les autorités de la concurrence comparent généralement les effets sur la concurrence qui devraient caractériser le scénario après la fusion à ceux qui découleraient d'un « contre-scénario ». En d'autres termes, l'approche classique du contrôle d'une fusion comporte deux étapes. Premièrement, l'autorité de la concurrence chargée de l'examen de la fusion identifie le contre-scénario approprié – à savoir, la structure de marché qui devrait prévaloir en l'absence de fusion. Deuxièmement, elle compare ce contre-scénario au scénario après la fusion. On notera que la charge de la preuve dans ces deux étapes de la contre-analyse (ou analyse à partir d'un facteur déterminant) incombe aux autorités de la concurrence.

Dans le cadre de l'examen d'une fusion entre deux entreprises financièrement saines, le contre-scénario se caractérise généralement par les conditions concurrentielles en jeu dans la situation avant la fusion. Cette approche est la bonne sauf si l'on pense que les conditions seront différentes dans un proche avenir, même en l'absence de fusion. Cependant, quand une des parties à l'opération est une entreprise défaillante, il est probable que la situation concurrentielle avant la fusion ou le *statu quo* fournisse une approximation valable de la structure concurrentielle des marchés concernés en l'absence de fusion. En d'autres termes, il est probable que la menace que représente l'entreprise défaillante pour la concurrence sur les marchés avant la fusion exagère les pressions concurrentielles que l'entreprise serait en mesure d'exercer à terme en l'absence de fusion. Cela rend encore plus difficile l'exercice qui consiste à choisir un contre-scénario. En fait, il pourrait y avoir plus d'un contre-scénario pertinent quand l'une des parties à l'opération est en difficulté financière et le choix du scénario le plus approprié selon chaque cas particulier est loin d'être simple.

Un des divers contre-scénarios potentiels qui pourrait être comparé au scénario après la fusion lors de l'évaluation de l'argument de l'entreprise défaillante est celui de la disparition du marché de tous les actifs de l'entreprise défaillante. Un autre scénario possible serait que tous ces actifs soient rachetés par une entreprise existante et un autre encore serait que l'acheteur soit un entrant potentiel. D'autres contre-scénarios possibles pourraient faire intervenir la restructuration et la réduction du périmètre des activités de l'entreprise et la cession de certains de ses actifs à des entreprises existantes et/ou entrantes.

Pour comprendre le ou les scénarios les plus pertinents selon le cas, il faut examiner les diverses options ouvertes à l'entreprise défaillante pour déterminer lesquelles représentent de réelles possibilités. Mais la tâche sera très probablement difficile, car les diverses options possibles doivent être analysées sur la base d'informations assez limitées, compte tenu des risques commerciaux liés à une analyse publique de multiples alternatives de fusion et/ou de restructuration quand une entreprise est en difficulté financière.

Or, le choix d'un contre-scénario plutôt qu'un autre peut avoir des conséquences considérables. On le comprendra si l'on examine un projet de fusion impliquant deux entreprises en place, dans le cadre de laquelle l'entreprise cible est en difficulté financière. Si le bon contre-scénario prévoit la disparition de

⁹⁰ Voir note 45 *supra*.

tous les actifs de l'entreprise défaillante, la fusion ne risque guère de fausser la concurrence par rapport au contre-scénario. Par contre, l'entité issue de la fusion peut conserver une part significative des actifs de l'entreprise défaillante et la fusion peut donc entraîner une réduction moins prononcée de l'offre que dans le contre-scénario de disparition des actifs. Dans ce cas, la fusion devrait obtenir le feu vert, car elle aura un effet moins préjudiciable pour la concurrence que celui qu'aurait eu la disparition de l'entreprise défaillante.

Si, d'un autre côté, le bon contre-scénario est celui où les actifs de l'entreprise défaillante sont achetés par un ou plusieurs nouveaux entrants,⁹¹ la fusion a alors peu de chance d'être approuvée car son impact risque d'être plus préjudiciable pour la concurrence que celui d'une ou plusieurs opérations alternatives. Les parties à la fusion pourraient défendre l'intérêt relatif de leur projet et obtenir que leur opération puisse se faire, cependant, si elles pouvaient démontrer que leur fusion donnerait lieu à des économies d'échelle et de gamme ou à des efficacités du côté de la demande que les nouveaux entrants ne seraient pas en mesure d'égaler, ou bien encore que les nouveaux entrants n'ont pas d'expérience sur le marché et ne sont intéressés que par le démantèlement des actifs de l'entreprise défaillante pour que l'entreprise défaillante ne soit pas en mesure d'affronter efficacement la concurrence quand elle passera dans d'autres mains.

Imaginons, en revanche, que le bon contre-scénario fasse intervenir la cession de l'entreprise défaillante à une entreprise exerçant déjà ses activités sur le marché. Dans ce cas, une évaluation convenable du projet de fusion nécessite de comparer les conséquences des deux différentes fusions : le projet de fusion, lorsque la partie acheteuse est déjà présente sur le marché (sinon, il n'y aura pas besoin de recourir à l'argument de l'entreprise défaillante), et une fusion avec une autre entreprise présente sur le marché. Si cette tâche n'est pas impossible, il faut tout de même reconnaître qu'il s'agit nécessairement d'un exercice bien plus compliqué que l'analyse classique où la fusion est comparée au *statu quo*. Les résultats de cette comparaison complexe peuvent en principe tout aussi bien être favorables ou non aux parties à l'opération.

On pourrait aussi conclure qu'en l'absence de fusion, l'entreprise défaillante ne quittera pas le marché à court terme. Les entreprises confrontées à des coûts irréversibles élevés peuvent être particulièrement réticentes à quitter le marché.⁹² Elles peuvent aussi être maintenues en vie par des codes des faillites indulgents. Ou elles peuvent renégocier leur dette et restructurer leurs activités. Un contre-scénario selon lequel l'entreprise défaillante parvient à rester sur le marché soit sous la forme d'un « zombie », soit sous une forme réduite par rapport à ce qu'elle était auparavant, n'a pas forcément d'effets plus favorables à la concurrence que le scénario après la fusion. Les entreprises zombies peuvent générer des distorsions importantes : sous le couvert de la responsabilité limitée ou grâce à des dispositions de sursis automatique aux termes du code des faillites du pays, l'entreprise défaillante peut se livrer à des pratiques de tarification ou de non-tarification inefficaces qui ne sont que des paris opportunistes sur leur résurrection. Les inefficacités résultant de telles pratiques devraient être comparées aux effets d'une accentuation de la concentration après la fusion proposée. Les entreprises ayant fait l'objet d'une rationalisation peuvent s'avérer incapables d'affronter la concurrence efficacement ou au moins aussi efficacement que l'entité issue de la fusion ne serait en mesure de le faire.

⁹¹ Un contre-scénario dans le cadre duquel plusieurs entreprises rachètent les actifs de l'entreprise défaillante peut avoir un effet plus concurrentiel que celui où il n'existe qu'un seul acheteur. Cependant, l'écart d'acquisition attaché à l'entreprise défaillante peut disparaître lorsque les actifs sont tellement morcelés que la possibilité de faire concurrence à ces acheteurs est sérieusement menacée. Voir Oxera. 2009. « Failing, or just flailing? The failing firm defence in mergers. » Oxera Agenda, mars 2009. Disponible le 26-08-2009 à l'adresse : http://www.oxera.com/cmsDocs/Agenda_Mar_Failing_firm_defence.pdf.

⁹² Voir O'Brien, J. & T.Folta. 2009. « Sunk costs, uncertainty and market exit: A real options perspective. » Oxford Journal Industrial and Corporate Change. Disponible le 22-09-2009 à l'adresse : <http://icc.oxfordjournals.org/cgi/content/abstract/dtp014>.

Les attitudes face à l'argument de l'entreprise défaillante examinées dans la section 2.1 ne suivent pas le processus en deux étapes qui caractérise la politique classique de contrôle des fusions. L'argument de l'entreprise défaillante habituel est, en revanche, structuré comme suit :

- Premièrement, les parties à l'opération et les autorités de la concurrence concluent que la fusion va fausser la concurrence en comparant le scénario après la fusion au scénario avant la fusion ;
- Deuxièmement, les parties à l'opération doivent montrer que l'entreprise défaillante va quitter le marché si la fusion n'a pas lieu. Sinon, la fusion sera bloquée ou des mesures correctrices seront exigées ;
- Troisièmement, les parties à l'opération doivent aussi démontrer qu'il n'y a pas de possibilité de fusion moins préjudiciable pour la concurrence. Autrement dit, elles doivent déterminer si d'autres fusions sont possibles, puis comparer ces scénarios de fusion à leur projet de fusion ;
- Quatrièmement, les parties à l'opération doivent aussi démontrer que tous les actifs de l'entreprise défaillante disparaîtront du marché si la fusion n'a pas lieu. Sinon, la fusion sera bloquée ou soumise à certaines conditions.

Cette structure est problématique : une fusion impliquant une entreprise défaillante peut être bloquée (ou des mesures correctrices peuvent être exigées) si elle ne satisfait pas aux conditions précédemment citées, même lorsqu'il s'agit de la solution aux problèmes financiers de l'entreprise défaillante la moins préjudiciable pour la concurrence. Afin de comprendre pourquoi, examinons chacune des quatre conditions séparément.

La première condition suppose de comparer le scénario après la fusion au scénario avant la fusion, mais cette comparaison n'est pertinente que si le scénario avant la fusion permet vraiment de se faire une idée de la structure du marché en l'absence de fusion, ce qui est peu probable si l'entreprise cible est en difficulté financière. Mais surtout, cette comparaison détermine l'attribution de la charge de la preuve ; la charge de la preuve ne relève plus des autorités mais des parties quand le scénario après la fusion est moins concurrentiel que le scénario avant la fusion.

La deuxième condition part du présupposé que la présence d'une entreprise en difficulté financière sur le marché, misant peut-être sur sa résurrection ou handicapée après une restructuration, vaut mieux pour les consommateurs que le projet de fusion. Ce présupposé n'est pas justifié : la présence d'une entreprise handicapée, en difficulté financière, sur le marché risque de fausser l'efficacité productive et peut évincer des entreprises relativement efficaces au détriment, en définitive, du bien-être à long terme des consommateurs.

La troisième condition est cohérente avec le processus classique en deux étapes de contrôle des fusions. Cependant, il appartient aux parties à la fusion de démontrer qu'il n'existe pas d'alternatives moins préjudiciables pour la concurrence, or celles-ci sont moins bien équipées pour se lancer dans le type d'analyses que les autorités de la concurrence réalisent habituellement, qui concernent des fusions entre entreprises dont les finances se portent bien et qui sont nettement plus simples. Mais surtout, les parties ne peuvent obtenir autant d'informations auprès de tiers que les autorités sont généralement en mesure de le faire. L'inversion de la charge de la preuve peut donc aboutir à des décisions erronées.

La quatrième condition part du présupposé que la structure du marché qui va résulter de la fusion sera nécessairement moins concurrentielle qu'une structure de marché où les actifs de l'entreprise défaillante sont partagés entre un certain nombre de concurrents existants et/ou potentiels. Mais ce n'est pas nécessairement le cas : un marché comportant quelques gros intervenants symétriques et de multiples

entreprises de petite envergure peut être moins concurrentiel qu'un marché avec moins d'entreprises de petite envergure si les gros intervenants deviennent moins symétriques.

En résumé, une fusion concernant une entreprise défaillante peut être bloquée (ou faire l'objet de mesures correctrices) si elle ne satisfait pas aux conditions précédemment citées, même si elle représente la solution la moins anticoncurrentielle pour les problèmes financiers de l'entreprise défaillante. Cela peut être le cas dans un certain nombre de circonstances. Par exemple, telle serait l'issue de l'évaluation de l'argument de l'entreprise défaillante si une restructuration est possible mais extrêmement inefficace, ou s'il existe des acheteurs potentiels pour les actifs de l'entreprise défaillante mais que ces acheteurs risquent de ne pas utiliser ces actifs de façon efficace, ou lorsqu'il existe un autre acheteur pour les activités de l'entreprise défaillante qui est cependant moins susceptible d'affronter efficacement la concurrence sur le marché, et que les parties à l'opération estiment qu'il leur est trop difficile de s'acquitter de la charge de la preuve.

2.6 Conclusions

Les critères définis dans les différentes juridictions pour évaluer l'invocation de l'argument de l'entreprise défaillante lors du contrôle d'une fusion horizontale sont très semblables. Ils imposent aux parties à la fusion de démontrer que l'entreprise présumée défaillante et ses actifs disparaîtraient du marché dans un proche avenir s'ils n'étaient pas rachetés et qu'il n'existe pas d'autre solution de rachat moins préjudiciable pour la concurrence que la fusion proposée. Ces exigences sont très rigoureuses. On ne s'étonnera donc pas que le nombre de cas où l'argument de l'entreprise défaillante a été invoqué avec succès soit très limité. Par exemple, au Royaume-Uni, l'OFT n'a donné son feu vert que pour cinq fusions en invoquant l'argument de l'entreprise défaillante depuis 2003, date à laquelle ont été publiées les lignes directrices sur les fusions de l'OFT.⁹³ Le nombre de cas de fusion dans lesquels les autorités de la concurrence ou les tribunaux d'autres pays ont jugé cet argument recevable est également très limité.

Les parties qui fusionnent et envisagent de recourir à l'argument de l'entreprise défaillante risquent d'être dissuadées par l'extrême rigueur des critères appliqués à ce type de prétentions. Même quand cet argument est jugé recevable, ce n'est généralement qu'après un examen approfondi et, dans certains cas, l'application d'importantes mesures correctrices.⁹⁴ En outre, invoquer l'argument de l'entreprise défaillante suppose d'admettre que la fusion proposée est anticoncurrentielle. Tout compte fait, l'argument de l'entreprise défaillante repose sur l'affirmation que la fusion, même si elle est préjudiciable à la concurrence, est un moindre mal. Les parties à l'opération peuvent être réticentes à l'admettre.

⁹³ OFT. 2003. Mergers - Substantive assessment guidance. OFT 516, publié en mai 2003. Ces fusions étaient les suivantes : (i) ME/1517/05 First West Yorkshire/Black Prince Buses – Acquisition attendue par First West Yorkshire Limited de Black Prince Buses Limited, décision de l'OFT, 26 mai 2005 ; (ii) ME/3387/07 Tesco/Kwik Save – Acquisition attendue par Tesco Stores Limited de cinq anciens magasins Kwik Save (Handforth, Coventry, Liverpool, Barrow-in-Furness et Nelson), décision de l'OFT, 11 décembre 2007 ; (iii) ME/3145/07 CDMG Group / Ferryways NV / Searoads Stevedores NV – Acquisition réalisée par le groupe CDMG d'entreprises de Ferryways NV et Searoad Stevedores NV, décision de l'OFT, 24 janvier 2008 ; et (iv) ME/3427/07 Homebase/Focus – Acquisition réalisée par Home Retail Group plc de 27 magasins auprès de Focus (DIY) Ltd, décisions de l'OFT, 7 août 2008 ; et (v) décisions de l'OFT du 14 mai 2009 : ME/4036/09 Acquisition attendue par HMV de 15 magasins Zavvi.

⁹⁴ Par exemple en 2001, l'Australian Competition and Consumer Commission (ACCC) a imposé des conditions pour approuver l'acquisition d'Impulse Airlines par Qantas Airways. Qantas a dû accorder l'accès à des créneaux horaires de pointe à l'aéroport de Sydney Airport et proposer certains créneaux horaires à d'autres transporteurs. Voir Bnet. 2001. ACCC approuve l'accord commercial entre Qantas Airways et Impulse Airlines. Disponible le 18-08-2009 à l'adresse : http://findarticles.com/p/articles/mi_m0CWU/is_2001_May_21/ai_74807690/.

Enfin, et cet aspect est tout aussi important, aux termes des critères actuels, l'examen d'une fusion en tenant compte de l'argument de l'entreprise défaillante peut donner lieu à des interdictions injustifiées trop nombreuses ou à l'application de mesures correctrices disproportionnées. Une fusion ne devrait être bloquée ou soumise à des conditions que si le scénario après la fusion est moins favorable à la concurrence qu'un contre-scénario convenablement élaboré. Le contre-scénario doit refléter la structure du marché censée exister en l'absence de fusion. Comme on l'a vu, l'application stricte des critères de l'argument de l'entreprise défaillante dans toutes les juridictions que nous avons passées en revue peut aboutir à des conclusions concernant la fusion proposée qui sont différentes de celles qui résulteraient d'une contre-analyse convenable.

3. Contrôle des fusions et argument de l'entreprise défaillante lors d'une crise du crédit

3.1 Introduction

La crise actuelle a commencé dans le secteur financier et on peut la faire remonter à l'effondrement du marché des crédits aux emprunteurs à risque (*subprime*) durant l'été 2007. Du fait de l'effondrement de ce marché, les banques ont cessé d'accorder des crédits, ce qui a eu des répercussions négatives sur l'économie réelle. Les économies de marché développées et émergentes sont toutes entrées dans une récession due à l'accès limité des entreprises aux financements à court terme. Même si les politiques monétaires des principales économies dans le monde ont apporté un volume de liquidités considérable aux marchés de capitaux mondiaux et que les programmes de relance coordonnés de ces économies ont stimulé la demande partout dans le monde, la crise est loin d'être terminée.

Dans le contexte de la crise financière actuelle, les entreprises sont plus nombreuses à se retrouver confrontées à des difficultés financières. Comme on l'a vu dans la section 1, les dépôts de bilan ont augmenté en flèche ces derniers mois partout dans le monde.⁹⁵ Bon nombre de PME et de grandes entreprises n'ont pu échapper aux effets de la crise. Des entreprises comme General Growth Properties (GGP), deuxième société d'investissement immobilier et exploitant de centres commerciaux aux États-Unis, ou encore les constructeurs automobiles Chrysler et General Motors et le promoteur immobilier japonais Zephyr, pour n'en citer que quelques unes, se sont toutes récemment placées sous la protection de la loi sur les faillites.

Les problèmes financiers de ces entreprises peuvent être résolus par une fusion avec des partenaires en meilleure santé financière. La réussite de l'opération de fusion évitera la faillite de l'entreprise défaillante et maintiendra les actifs de l'entreprise sur le marché, ce qui peut être rentable à titre privé non seulement pour les parties prenantes de l'entreprise défaillante mais aussi pour les actionnaires de la société acheteuse, et bénéfique au processus concurrentiel et au bien-être des consommateurs. Il est par conséquent possible que, dans les mois ou les années à venir, les autorités de la concurrence soient confrontées à un nombre croissant d'affaires dans lesquelles l'argument de l'entreprise défaillante ou de l'entreprise fragilisée sera invoqué comme moyen de défense. Le cas échéant, cela dépendra de facteurs extérieurs – comme la profondeur et la durée de la crise du crédit et de la récession – ainsi que de facteurs internes – comme la nature des réactions des autorités de la concurrence à ces moyens de défense. Cette section examine si les attitudes actuelles face à l'argument de l'entreprise défaillante permettent aux autorités de la concurrence, en pleine crise du crédit, de trancher efficacement lorsqu'elles contrôlent des opérations de fusion impliquant des entreprises défaillantes/fragilisées.

⁹⁵ Voir <http://www.fastupfront.com/blog/business/21-famous-corporate-bankruptcies-from-2001-2009/> et également <http://news.bbc.co.uk/2/hi/business/8091298.stm>.

3.2 *Contrôle des fusions et crise du crédit*

La crise financière et la récession économique actuelles posent un certain nombre de problèmes concernant le contrôle des fusions.

Premièrement, pendant une crise du crédit, les entreprises en difficulté financière ne sont pas forcément inefficaces en termes de coûts et leurs produits ne sont pas forcément confrontés à une demande insuffisante. Des entreprises en bonne santé peuvent se retrouver en difficulté. En effet, en raison de la pénurie de crédit, il leur est impossible d'obtenir le fonds de roulement nécessaire pour maintenir leurs activités. Laisser une entreprise efficace proposant des produits pour lesquels il existe une demande significative quitter les marchés sur lesquels elle opère en raison du dysfonctionnement des marchés de capitaux n'est pas dans le meilleur intérêt des consommateurs. Cela engendre plutôt une défaillance supplémentaire du marché : une augmentation du pouvoir de marché. La concurrence s'en trouvera réduite et les consommateurs en pâtiront. Dans ces circonstances, il peut être préférable de laisser des concurrents en difficulté financière fusionner, même si cela peut soulever des problèmes de concurrence, car une telle initiative peut leur permettre de dégager les synergies réelles et financières nécessaires pour rester en activité sur leurs marchés traditionnels. Il est donc d'une importance primordiale que le régime de l'argument de l'entreprise défaillante ne verrouille pas cette possibilité sauf s'il apparaît clairement qu'il existe des options moins préjudiciables pour la concurrence et que ces options sont réalistes. Cela étant, pour les raisons exposées dans la section 2.5, compte tenu des conditions actuelles d'application de l'argument de l'entreprise défaillante dans les juridictions que nous avons examinées, le risque existe qu'une fusion impliquant une cible en difficulté puisse être bloquée (ou soumise à des mesures correctrices), alors même que cette fusion représente la solution aux problèmes financiers de l'entreprise défaillante la moins préjudiciable pour la concurrence.

Deuxièmement, pendant une crise du crédit de l'ampleur de celle qu'on connaît actuellement, des secteurs entiers peuvent se retrouver en difficulté financière. Le secteur bancaire en est une illustration évidente. Le secteur de l'automobile, le secteur du charbon,⁹⁶ le secteur de l'hôtellerie aux États-Unis,⁹⁷ le secteur de la presse⁹⁸ et le secteur du diamant⁹⁹ en constituent d'autres exemples. Tout le problème pour les autorités de la concurrence procédant au contrôle d'une fusion dans un de ces secteurs en proie à des difficultés est de définir le contre-scénario convenable, sachant que la situation avant la fusion ou le *statu quo* n'a guère de chance de fournir une approximation valable de la structure du marché à laquelle on pourrait s'attendre dans un proche avenir en l'absence de fusion. Le secteur risque de devenir bien plus concentré, même en l'absence de la fusion proposée, car l'une des parties à l'opération ou les deux peuvent être vouées de disparaître si la fusion n'a pas lieu. Plusieurs opérations de fusion peuvent aussi avoir lieu simultanément, chaque intervenant du secteur pouvant tenter de fusionner pour éviter la faillite.

⁹⁶ Voir par exemple : « Steel production to decline by 10% in 2009, say analysts ». 29 décembre 2008. Disponible à l'adresse : <http://www.irishtimes.com/newspaper/finance/2008/12/29/1229728603954.html> et « Now, US steel industry asks for government bailout ». 2 janvier 2009. Disponible à l'adresse : http://www.domain-b.com/economy/worldconomy/20090102_us_steel_industry.html.

⁹⁷ Voir par exemple : « More distress on the horizon for U.S. hotels ». 23 juillet 2009. Disponible à l'adresse : http://www.hotelmarketing.com/index.php/content/article/more_distress_on_the_horizon_for_us_hotels/.

⁹⁸ Voir par exemple : Bandyk, M. 2009. « Newspaper Bailout Seriously Considered ». 25 March 2009. Disponible à l'adresse : <http://www.usnews.com/blogs/risky-business/2009/03/25/newspaper-bailout-seriously-considered.html>.

⁹⁹ Voir par exemple : « Banks urged to bail out diamond industry ». The financial express. 7 mars 2009. Disponible à l'adresse : <http://www.financialexpress.com/news/banks-urged-to-bail-out-diamond-industry/431837/>.

Cela peut donner à penser que le contrôle des fusions doit être relativement plus indulgent pour les secteurs en difficulté. Cependant, plusieurs facteurs semblent indiquer le contraire. On notera, en particulier, que l'entrée peut être beaucoup plus difficile dans un contexte de crise du crédit, car les nouveaux entrants ont un accès limité, voire nul, au crédit¹⁰⁰. Les entrants peuvent avoir des idées mais ne pas disposer du financement leur permettant de s'introduire sur le marché. De plus, dans un secteur en difficulté, les fusions peuvent se succéder puisque les entreprises défaillantes se regroupent pour éviter la faillite. L'analyse de chaque fusion doit par conséquent prendre en compte la possibilité de fusions en série. En d'autres termes, quand tout un secteur est en difficulté, le contre-scénario peut avoir à prendre en compte toutes les futures fusions attendues. L'impact de la fusion en cours sur la concurrence et le bien-être des consommateurs risque bien plus d'être négatif quand d'autres fusions sont aussi attendues dans un proche avenir. De même, les conséquences d'une fusion donnée seront forcément encore plus défavorables si certains concurrents quittent le marché dans un proche avenir parce qu'ils n'ont pas pu obtenir de crédits.

De plus, deux autres facteurs doivent être examinés avant d'adopter une approche plus souple face à des fusions dans des secteurs en proie à des difficultés financières :

- *Confusion entre le déclin d'un secteur et des ralentissements de courte durée.* Il est très difficile de distinguer si un secteur risque de s'effondrer ou s'il est seulement confronté à un ralentissement de courte durée.¹⁰¹ Cette distinction est extrêmement importante dans la mesure où une modification de la structure de marché peut avoir un impact négatif à long terme sur le bien-être des consommateurs. Les autorités de la concurrence devraient donc veiller à ne pas sur-réagir au cycle de l'activité en approuvant des fusions qui seraient préjudiciables à long terme pour les consommateurs : « les récessions sont temporaires, mais les fusions sont éternelles. »¹⁰²
- *Autres politiques.* La bonne réaction stratégique face à la crise prolongée de tout un secteur n'est pas forcément d'appliquer une politique de contrôle des fusions indulgente. Les pouvoirs publics ont d'autres instruments à leur disposition. Ils peuvent apporter un soutien financier à des secteurs en difficulté, par exemple. Ces politiques sont bien plus flexibles qu'un contrôle des fusions. Si des mesures de soutien financier peuvent être adaptées en fonction du cycle de l'activité, une évolution anticoncurrentielle de la concentration du marché ne peut être corrigée rapidement une fois que le secteur est sorti de la récession.

Troisièmement, quand l'une des sociétés parties à la fusion est en difficulté financière, le temps est un facteur fondamental. Pendant que les autorités examinent une fusion, la situation financière de l'entreprise défaillante peut se détériorer rapidement. Les entreprises que l'on aurait pu initialement qualifier de « concurrents fragiles » ou d'« entreprises en récession » peuvent rapidement devenir des entreprises défaillantes. La rapidité des flux dans le secteur et les incertitudes soulevées par la crise peuvent faire que la fusion proposée soit particulièrement sensible au facteur temps et que des transactions alternatives deviennent sans intérêt. De ce fait les pressions dues aux délais sont l'un des nombreux problèmes auxquels les autorités de la concurrence sont confrontées dans le cadre du contrôle des fusions.

¹⁰⁰ Voir Nigra, B.A. & J.S.Kanter. 2003. « The Effect of Market Conditions on Merger Review -- Distressed Industries, Failing Firms, and Mergers with Bankrupt Companies. » 2 ABA section of Antitrust Law, 51st annual spring meeting course materials, 736 737 (2003). Disponible le 26-08-2009 à l'adresse : <http://www.abanet.org/antitrust/at-committees/at-telecom/pdf/distressedindustry.pdf>.

¹⁰¹ Voir par exemple le discours de Debra A. Valentine, directeur adjoint de la planification des politiques de la FTC du 8 décembre 1995. Disponible à l'adresse : http://www.ftc.gov/speech_dvhoriz_lissues.shtm.

¹⁰² C. Shapiro, « Competition Policy in Distressed Industries », discours prononcé à l'occasion de l'ABA Antitrust Symposium: Competition as Public Policy, 13 mai 2009.

Quatrièmement, les difficultés financières peuvent affecter les motivations qu'ont les entreprises pour fusionner. Les autorités de la concurrence doivent examiner attentivement les raisons incitant les entreprises en difficulté financière à fusionner. Comme on l'a vu, cela nécessite une excellente connaissance de la situation financière des entreprises et, en particulier, de l'interdépendance entre les marchés du capital et des produits. Souvent, les entreprises fusionnent pour bénéficier de marchés internes du capital plus profonds.¹⁰³ Un regroupement permet aux entreprises d'augmenter et/ou de mieux répartir les ressources internes nécessaires pour financer les projets d'investissement et d'innovation. Cette logique des fusions est particulièrement importante quand les fonds internes sont bien moins coûteux que les capitaux externes, ou quand l'accès aux marchés externes du capital est restreint, comme c'est le cas actuellement. Bien entendu, les consommateurs tirent parti d'une augmentation de l'investissement et de l'innovation. Un meilleur accès au financement génère également des efficacités réelles à travers son impact sur la concurrence sur les marchés de produits.¹⁰⁴ Par exemple, il peut permettre aux entreprises de renforcer leurs investissements productifs. Quand ces investissements réduisent les coûts marginaux, on peut s'attendre à une baisse des prix. De même, une fusion qui augmente les capacités des entreprises à financer des investissements peut les aider à mener des stratégies dynamiques de détermination des prix dans le cadre desquelles les pertes initiales encourues pour se constituer une clientèle sont compensées par les futurs bénéfices. Ces stratégies de détermination des prix sont optimales sur les marchés qui se caractérisent par des effets de réseau, un apprentissage par la pratique et des coûts de transfert mais qui, en l'absence de financement externe, exigent de disposer de trésors de guerre.

Le regroupement peut aussi constituer une réaction efficace à des chocs négatifs du côté de la demande. Une baisse de la demande, et la perte du volume d'activité qui en résulte, peuvent faire grimper les coûts unitaires des entreprises. Les fusions sur des marchés en proie à des contractions de la demande peuvent donc permettre aux entreprises de réduire des coûts unitaires trop élevés. Les consommateurs profiteront de ces économies d'échelle sous réserve que l'entité issue de la fusion continue à subir la pression de concurrents existants ou potentiels. Ces avantages seront d'autant plus grands que les chocs négatifs perdurent et qu'il n'existe pas d'obstacles majeurs à l'entrée.

Cinquièmement, le durcissement des conditions sur les marchés du capital peuvent aussi rendre bien plus difficile la tâche qui consiste à trouver des acheteurs convenables pour les actifs à vendre. Ceux qui présentent le profil requis peuvent ne pas être en mesure d'accéder au financement nécessaire pour acquérir les actifs de l'entité ayant fait l'objet de la fusion. En conséquence, il est impossible de remédier, ou du moins pas aussi facilement qu'en temps normal, aux effets anticoncurrentiels des fusions.

3.3 *Conséquences de la crise du crédit pour l'argument de l'entreprise défaillante*

Comme on l'a vu, de nombreuses entreprises sont susceptibles de connaître des difficultés financières quand les conditions sur les marchés du capital sont strictes et que l'économie traverse une récession. Certaines d'entre elles peuvent envisager une fusion avec un concurrent comme l'issue la plus attrayante et une partie de ces dernières peut évaluer la possibilité de recourir à l'argument de défense de l'entreprise défaillante. Cela étant, les perspectives de réussite sont sans doute limitées compte tenu de la grille d'analyse utilisée actuellement pour évaluer ces moyens de défense dans les juridictions que nous avons examinées.

Comme on l'a expliqué dans la section 2.5, le dispositif actuel présume que certains scénarios bâtis sur un facteur déterminant, comme le maintien sur le marché d'une entreprise dont l'activité a été tronquée ou amputée, sont nécessairement supérieurs, du point de vue de la concurrence, à l'opération de fusion

¹⁰³ J. Stein, 1997, « Internal Capital Markets and the Competition for Corporate Resources », *Journal of Finance*, 52, 111-133.

¹⁰⁴ Voir note 88 *supra*.

examinée. Une telle présomption n'est pas toujours justifiée. Des fusions peuvent donc être bloquées même alors même qu'elles représentent l'option la moins préjudiciable. De plus, évaluer la validité de l'argument de l'entreprise défaillante demande beaucoup de temps, ce qui, sachant que la situation des entreprises en difficulté peut se détériorer rapidement, peut aboutir à une liquidation contreproductive. En conséquence, l'option consistant à invoquer l'argument de l'entreprise défaillante peut ne pas être envisageable dans la pratique.

Bien entendu, les autorités de la concurrence peuvent résoudre bon nombre de ces problèmes dans la pratique. Elles peuvent faire suivre une procédure accélérée à ces fusions annoncées pour éviter le risque de retards coûteux. Elles peuvent aussi investir des ressources pour examiner la logique commerciale et identifier le contre-scénario le plus approprié sans aucun *a priori* ou idée préconçue. Enfin, elles peuvent également collaborer avec les parties pour définir des mesures compensatoires afin de s'assurer que la fusion proposée se fera en produisant des effets anticoncurrentiels limités. Ces changements d'ordre pratique amélioreraient certainement les résultats des processus de contrôle des fusions et seraient donc sans aucun doute justifiés. Ce qui ne serait pas justifié serait de modifier la politique actuelle concernant les fusions pour qu'elle devienne plus tolérante vis-à-vis de fusions anticoncurrentielles qui ne constituent pas la solution la moins anticoncurrentielle que peut choisir de façon réaliste l'entreprise défaillante. Une telle réforme serait contraire au principe fondamental du contrôle des fusions, selon lequel une fusion anticoncurrentielle doit être bloquée ou soumise à des conditions sauf s'il peut être démontré qu'il s'agit de l'option la moins préjudiciable pour la concurrence. Ce principe est aussi valable dans le contexte économique et financier actuel qu'il l'était par le passé.

3.4 *Fusions entre banques et argument de l'entreprise défaillante*

Les problèmes auxquels sont confrontées les autorités de la concurrence quand elles analysent les fusions entre sociétés en difficulté durant les crises actuelles ne sont jamais aussi complexes que lorsque ces fusions impliquent des établissements bancaires. Les banques sont des agents économiques particuliers du fait de leur importance pour la stabilité du système financier et de l'économie. L'effondrement d'un système bancaire peut entraîner une débâcle financière et une grave récession économique. La mondialisation et la multiplication des prêts interbancaires ont rendu les banques extrêmement interdépendantes. Les investisseurs et les entreprises dépendent aussi des banques. Cela crée un lien étroit entre l'économie réelle et la santé du système financier. Le rôle systémique du secteur bancaire explique pourquoi il peut être très important d'éviter la disparition d'une banque donnée et peut justifier une approche plus tolérante vis-à-vis des fusions bancaires lors d'une crise du crédit.

Les autorités de la concurrence doivent cependant, lorsqu'elles examinent les fusions bancaires, établir une distinction entre les banques qui sont en proie à des problèmes structurels et les banques qui sont fondamentalement en bonne santé mais sont gênées par une pénurie temporaire de liquidités. Une fusion portant sur une banque qui a des problèmes structurels majeurs peut faire plus de mal que de bien, les actifs toxiques de la banque défaillante pouvant contaminer le partenaire avec lequel elle fusionne. Dans ce cas, la fusion peut faire disparaître du marché les actifs des deux parties à l'opération. La restriction en termes d'offre qui peut en découler fera du tort aux consommateurs pendant longtemps.

Les autorités de la concurrence doivent aussi prendre en compte la possibilité d'une intervention de l'État en l'absence de fusion. Cela complique singulièrement la définition d'un contre-scénario approprié dans le cas des fusions bancaires. Il se peut qu'on refuse de laisser sombrer des banques en difficulté financière – surtout celles qui sont trop grosses pour faire faillite – afin d'éviter les conséquences systémiques de leur effondrement. Les pouvoirs publics peuvent essayer de persuader des banques en bonne santé de racheter leurs concurrentes en difficulté mais, quand cela est impossible, ils peuvent injecter des capitaux ou apporter d'autres formes de soutien financier afin d'éviter les conséquences

systémiques de la faillite de ces banques. Dans l'affaire *Lloyds/HBOS*,¹⁰⁵ par exemple, les deux parties qui fusionnaient et l'OFT, l'autorité de la concurrence britannique, ont convenu qu'il était « impossible d'envisager que l'on puisse laisser HBOS faire faillite » compte tenu des conséquences désastreuses « en termes de stabilité financière, en particulier compte tenu de l'exposition des contreparties, de l'exposition des déposants, de la confiance des investisseurs et de la confiance générale de l'économie au sens large. »¹⁰⁶ L'OFT a ensuite analysé la fusion proposée en partant du principe que HBOS resterait sur le marché avec le soutien de l'État.

Examinons à présent le recours à l'argument de l'entreprise défaillante dans le cadre des fusions bancaires pendant la crise actuelle. Il faut distinguer trois cas différents. Le cas le plus simple est celui où la fusion porte sur deux banques relativement petites dont la faillite ne risque pas de provoquer des effets systémiques. Dans ce cas, l'application de l'argument de l'entreprise défaillante ne soulève pas de nouveaux problèmes.

Il en va autrement quand la fusion concerne une ou plusieurs banques systémiques, à savoir des banques dont la faillite pourrait entraîner des conséquences négatives sur l'économie dans son ensemble. L'argument de l'entreprise défaillante ne peut s'appliquer aux fusions entre des banques quand il existe un risque significatif que la banque défaillante contamine l'acquéreur. Comme on l'a souligné plus haut, dans ce cas le scénario après la fusion est susceptible de donner lieu à une offre moins intéressante pour les consommateurs que si la banque en difficulté disparaît du marché. La fusion doit alors être bloquée ou des mesures correctrices imposées.

L'argument de l'entreprise défaillante ne peut pas non plus s'appliquer à des fusions entre des banques systémiques car les pouvoirs publics ne permettraient pas que les banques systémiques fassent faillite. Dans l'affaire *Lloyds/HBOS*, par exemple, l'OFT a conclu « que l'application de l'argument de l'entreprise défaillante dans ce cas n'est pas appropriée, étant donné qu'il n'est pas réaliste d'envisager que l'on ait laissé HBOS faire faillite (ou que l'on ait laissé ses actifs disparaître du marché). »¹⁰⁷

Cela ne devrait cependant pas susciter de préoccupation majeure si le problème auquel est confrontée une banque en difficulté est une pénurie temporaire de liquidités. Face à un risque systémique, les fusions, qui sont des mesures relativement permanentes, sont des solutions moins bonnes que les interventions de l'État, comme des injections de capitaux et/ou des garanties de crédit, simplement parce qu'il est plus facile de trouver une stratégie de sortie concernant ces dernières mesures.

En revanche, cela ne signifie pas que toutes les fusions de ce type provoquent nécessairement des effets anticoncurrentiels supplémentaires et devraient être interdites ou soumises à des conditions. Il est tout à fait possible que le scénario après la fusion s'avère plus favorable à la concurrence que le scénario sans fusion avec une banque soutenue (ou contrôlée) par l'État. En effet, la banque ayant fait l'objet du plan de sauvetage va pouvoir profiter des risques excessifs qu'elle aura pris par le passé, ce qui exacerbera les problèmes d'aléa moral, fréquents dans le secteur bancaire. Les banques en bonne santé verront probablement leur volume d'activité diminuer au profit de banques très agressives, trop grosses pour faire faillite et qui ont fait l'objet d'un plan de sauvetage. De plus, ces banques renflouées pourront attirer de nouveaux déposants et emprunter à un coût inférieur sur les marchés interbancaires compte tenu du soutien de l'État. Elles pourront donc prêter de façon plus agressive et détourner les clients de concurrentes plus prudentes qui ne bénéficient pas de la garantie de l'État. Ces distorsions peuvent provoquer la disparition

¹⁰⁵ OFT, Aquisition anticipée par Lloyds TSB plc de HBOS plc, rapport du Secretary of State for Business Enterprise and Regulatory Reform, 24 octobre 2008.

¹⁰⁶ *Ibid.*, § 57-58.

¹⁰⁷ *Ibid.*, § 59.

de concurrents en place et empêcher l'entrée de nouveaux concurrents. Le préjudice pour la concurrence selon ce contre-scénario sera donc sans doute plus grand que les effets anticoncurrentiels potentiels de la fusion.

3.5 Conclusion

La crise financière et économique actuelle peut mettre un grand nombre d'entreprises en difficulté financière. Certaines d'entre elles peuvent essayer de régler leurs difficultés en fusionnant avec des concurrentes plus solides financièrement. Dans certains cas, les parties à l'opération peuvent envisager de recourir à l'argument de l'entreprise défaillante pour que leur fusion soit approuvée par les autorités de tutelle. Ce choix peut se révéler coûteux et décevant, cependant. Comme on l'a vu dans la section 2, les conditions requises pour que l'argument de l'entreprise défaillante soit jugé recevable sont très strictes et la charge de la preuve imposée aux parties très exigeante. Cet aspect pose un problème général, mais d'autant plus lors d'une crise financière où les capitaux sont rares et les entreprises solvables en difficulté financière risquent de perdre leur position sur le marché du jour au lendemain.

La section qui suit examine si les entreprises en difficulté financière peuvent mieux s'en sortir si elles utilisent pour défendre l'opération de fusion envisagée les arguments classiques bâtis sur « un facteur déterminant ». Autrement dit, il s'agit de comparer les effets de la fusion sur la concurrence par rapport à un contre-scénario réaliste qui reflète le contexte extérieur. Cette approche purement fondée sur les effets n'est pas entravée par les nombreuses présuppositions qui sous-tendent les attitudes actuelles face à l'argument de l'entreprise défaillante.

4. Évaluation des attitudes actuelles face à l'argument de l'entreprise défaillante

Dans le contexte du contrôle des fusions, les autorités de la concurrence doivent décider ou non d'approuver la fusion, étant entendu qu'elles peuvent éventuellement imposer certaines conditions (mesures correctrices) aux parties à l'opération, ou bloquer l'opération. Ces décisions sont difficiles à prendre. Le contrôle des fusions est un exercice prospectif complexe. Les autorités de la concurrence tentent de prévoir correctement si la fusion proposée va nuire aux consommateurs sur la base d'informations souvent limitées et datées concernant la dynamique de concurrence sur les marchés concernés par l'opération. Aussi rien d'étonnant à ce que leurs décisions puissent parfois être mal inspirées. Des erreurs dites de type I et de type II peuvent se produire. Les erreurs de type I se réfèrent à des décisions d'interdire des fusions qui en réalité n'auraient pas produits d'effets anticoncurrentiels et auraient même pu contribuer à renforcer la concurrence. Les erreurs de type II se réfèrent à des décisions d'approuver des fusions qui sont en fait préjudiciables pour la concurrence. Les autorités de la concurrence font aussi des erreurs de type I quand elles imposent des mesures correctrices qui sont inutiles ou disproportionnées et des erreurs de type II quand les mesures correctrices imposées aux parties ne permettent pas de rétablir une concurrence effective après la fusion.

Idéalement, les autorités de la concurrence devraient évaluer les effets concurrentiels des fusions en recourant à un ensemble de règles explicites ou implicites qui (a) minimisent le coût attendu de l'erreur, (b) requièrent une administration relativement peu coûteuse et (c) donnent des résultats prévisibles.

Le coût de l'erreur attendue correspond à la probabilité des erreurs de type I et de type II et à leurs coûts respectifs. Le coût d'une erreur de type I ne sera élevé que dans le cas où la fusion aurait induit des efficacités importantes en termes de coût ou de demande ; autrement, le coût sera minime. Une erreur de type II se produit quand les autorités concluent que la fusion est favorable à la concurrence et qu'en réalité le coût pour le bien-être résultant de l'augmentation des prix provoquée par la fusion réduit à néant les efficacités en termes de coût et de demande rendues possibles par la fusion. Le coût d'une erreur de type II sera élevé si la fusion génère peu d'efficacités (voire aucune), ce qui donne lieu à une forte augmentation

du pouvoir de marché, reflétée par une nette augmentation des prix. Les erreurs de type I sont souvent jugées plus graves que les erreurs de type II lors de contrôles de fusions. Cela vient du fait que les effets anticoncurrentiels potentiels d'une fusion peuvent être limités par une intervention *ex post*, comme l'interdiction de l'abus de position dominante. Ce recours ne peut exister que dans des juridictions comme l'UE, où des entreprises peuvent être mises en cause pour pratique de prix excessifs. Dans d'autres juridictions, le préjudice provoqué par la fusion peut perdurer extrêmement longtemps, tant qu'il n'y a pas de conduite abusive, exclusive, qui maintient ou étend le pouvoir de marché des entreprises.

Les coûts de ces deux types d'erreurs peuvent être particulièrement élevés quand la fusion faisant l'objet du contrôle implique une entreprise défaillante exerçant ses activités en pleine crise du crédit. D'un côté, ces fusions peuvent donner lieu à d'importantes efficiences. Par exemple, une fusion peut éviter la disparition du marché des actifs de l'entreprise défaillante. Elle peut aussi permettre aux entreprises ayant des difficultés de trésorerie de continuer à investir dans des nouveaux produits et processus. D'un autre côté, la fusion peut affaiblir la position financière de l'acquéreur, réduisant ainsi sa propre efficacité. Ou elle peut simplement servir à consolider un marché concurrentiel de façon coordonnée et aux dépens de consommateurs. Aussi les coûts des erreurs de type I et de type II peuvent-ils être considérables.

La probabilité d'erreurs lors de l'évaluation des fusions concernant des entreprises défaillantes en période de crise financière risque aussi d'être élevée. Comme on l'a expliqué plus haut, le scénario avant la fusion donne peu d'indications, voire aucune, sur le développement du marché après la fusion ou même en l'absence de fusion. Les autorités de la concurrence doivent examiner les conditions macroéconomiques dans lesquelles les parties à l'opération vont exercer leur activité, elles doivent procéder à un audit de leur situation financière, etc.

Il est donc important d'évaluer le coût attendu des critères utilisés par les autorités de la concurrence partout dans le monde pour examiner l'argument de l'entreprise défaillante afin de déterminer si ce coût peut être minimisé sans augmenter le coût de mise en œuvre ou réduire la prévisibilité de leurs décisions. La présente section traitera de ce sujet. Dans ce qui suit, on cherchera à évaluer l'approche actuellement utilisée concernant l'argument de l'entreprise défaillante dans les juridictions examinées dans la section 2 du point de vue de son *administrabilité* – à savoir son coût de mise en œuvre –, de sa *prévisibilité* – qui donne aux entreprises envisageant une fusion une certitude légale –, et de son *efficacité* – qui correspond à la probabilité de décisions erronées en matière de fusion de leur part et au coût de telles décisions.

4.1 Erreurs de type I et de type II

L'approche actuelle vis-à-vis de l'argument de l'entreprise défaillante semble être axée sur une minimisation des erreurs de type II. Premièrement, bien qu'elle s'applique manifestement à des situations extrêmes où l'entreprise est en difficulté financière, on peut s'interroger sur sa mise en œuvre dans le cas de fusions portant sur des entreprises en récession ou des concurrents fragilisés. Deuxièmement, les parties à l'opération sont tenues d'examiner un grand nombre de contre-scénarios possibles. Elles doivent considérer la faisabilité d'un scénario bâti sur un facteur déterminant dans lequel l'entreprise défaillante est en mesure de se restructurer et de rester sur le marché en tant qu'intervenant autonome. Elles doivent aussi envisager des scénarios où l'entreprise défaillante quitte le marché, mais où tout ou partie de ses actifs restent opérationnels entre les mains de concurrents existants ou potentiels. Et elles doivent également comparer et mettre en regard la fusion qu'elles proposent et toutes les autres solutions réalistes de fusion. En fait, l'entreprise défaillante doit démontrer qu'elle a réalisé en toute bonne foi des efforts pour trouver d'autres partenaires, sachant que « toute offre d'achat des actifs de l'entreprise défaillante à un prix supérieur à la valeur de liquidation de ces actifs (...) sera considérée comme une alternative raisonnable. »¹⁰⁸ Troisièmement, l'approche existante suppose que certains de ces contre-scénarios sont

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Voir note 13 *supra*, section 5.1, note 39.

préférables au scénario après la fusion du point de vue de la concurrence. En particulier, l'approche actuelle rejettera l'argument de l'entreprise défaillante sauf si les parties à l'opération peuvent démontrer que certains de ces contre-scénarios ne sont pas réalistes : elles doivent montrer que l'entreprise et ses actifs sont susceptibles de disparaître du marché si la fusion proposée n'a pas lieu.

Ce parti pris en faveur d'une minimisation de la probabilité des erreurs de type II peut être interprété de la manière suivante. Une approche tolérante ne peut expliquer de façon satisfaisante les effets anticoncurrentiels des fusions concernant les entreprises défaillantes, qui pourraient fausser durablement le processus concurrentiel compte tenu de la nature irréversible des fusions. Comme l'a souligné le professeur Salop, les autorités de la concurrence doivent être « extrêmement sceptiques vis-à-vis des juristes qui vont s'efforcer de transformer toute récession temporaire en une occasion en or pour procéder à une cartellisation du secteur au moyen de fusion. »¹⁰⁹ Une approche tolérante peut aussi entraîner une augmentation du nombre de demandes concernant des fusions qui réduisent le bien-être. Un système efficace de contrôle des fusions dissuade les demandes de fusions anticoncurrentielles. Les autorités de la concurrence cherchant à maximiser les effets dissuasifs du contrôle des fusions vont orienter leurs politiques en matière de fusion dans le sens d'une minimisation des erreurs de type II.

De plus, une approche tolérante peut entraîner des décisions inefficaces sur le plan des entrées.¹¹⁰ Les décisions relatives aux entrées se fondent sur une estimation des bénéfices attendus après l'entrée. En donnant aux entreprises la possibilité de sortir à peu de frais, en limitant leurs coûts de sortie, une application tolérante de l'argument de l'entreprise défaillante risque de donner une vision tronquée des pertes qu'un entrant peut s'attendre à subir en cas de faillite. Cela réduit artificiellement le coût d'une entrée et, de ce fait, peut favoriser l'entrée de concurrents inefficaces. En outre, les décisions en matière d'entrée peuvent être biaisées en faveur des marchés où les investisseurs s'attendent à une plus grande tolérance concernant l'argument de l'entreprise défaillante, ce qui fausserait le fonctionnement normal du marché.¹¹¹

Une approche tolérante peut aussi donner lieu à des décisions de sortie inefficaces. Une des caractéristiques souhaitables d'un processus concurrentiel fonctionnant bien est qu'il provoque la sortie d'entreprises inefficaces et assure ainsi que la production s'effectue au coût le plus bas possible. Cette caractéristique, toujours importante, l'est d'autant plus dans le contexte d'une crise du crédit où le financement est rare et où il est essentiel de le canaliser vers les entreprises dotées de meilleures possibilités de croissance. Une application stricte de l'argument de l'entreprise défaillante « aidera à éliminer les entreprises fragiles et inefficaces et à générer une croissance de long terme. »¹¹²

Enfin, il importe de souligner un autre aspect. Les autorités de la concurrence peuvent avoir une autre raison d'adopter une grille d'analyse qui cherche plutôt à minimiser les erreurs de type II : ce type de parti pris peut les aider à résister aux pressions politiques considérables qu'elles risquent de subir quand elles évaluent certains recours fondés sur l'argument de l'entreprise défaillante. Les milieux politiques s'intéressent à certaines fusions pour des raisons de politique industrielle ou parce qu'ils cherchent à éviter des pertes d'emplois dans des entreprises en difficulté financière.

¹⁰⁹ Auditions de la Federal Trade Commission concernant la concurrence mondiale et basée sur l'innovation, (1995) (déclaration de Steven C. Salop, professeur d'économie et de droit, Georgetown University Law Center).

¹¹⁰ Heyer, K. & S Kimmel. 2009. Merger Review of Firms in Financial Distress. Economic Analysis Group, document de travail 09-1, p. 11.

¹¹¹ *Ibid.*, p. 12.

¹¹² Anandarajah, K., D. Lombardi & A. Mahesh Tulpule. 2009. Antitrust: Scrutiny of Mergers during Economic Downturns. Disponible à l'adresse : <http://www.lawgazette.com.sg/2009-5/feature2.htm>.

L'importance accordée aux erreurs de type II a un prix : elle augmente la probabilité des erreurs de type I. L'approche actuelle suppose qu'il est préférable du point de vue de la concurrence de garder une entreprise défaillante handicapée sur le marché plutôt que de l'autoriser à fusionner avec une entreprise concurrente en meilleure santé. Comme on l'a vu, cette présupposition n'est pas toujours justifiée et peut conduire à l'interdiction de fusions alors même qu'elles représentent la solution la moins préjudiciable pour la concurrence. Une entreprise en difficulté financière peut avoir à réduire ses investissements productifs. Une fusion qui empêche ces réductions de capacités peut entraîner une baisse des prix. De même, une fusion qui renforce les possibilités qu'ont les entreprises de financer des investissements peut les aider à mener des stratégies dynamiques de détermination des prix dans le cadre desquelles les pertes initiales encourues pour se constituer une clientèle sont compensées par les futurs bénéfices. Ces stratégies de détermination des prix sont optimales sur les marchés qui se caractérisent par des effets de réseau, l'apprentissage par la pratique et les coûts de transfert mais qui, en l'absence de financement externe, exige de disposer de trésors de guerre. Une fusion avec un partenaire en meilleure santé peut apporter les fonds nécessaires.

Un traitement trop strict de l'argument de l'entreprise défaillante peut non seulement engendrer de nombreuses décisions mal inspirées, mais aussi dissuader la proposition de fusions efficaces, dissuader les nouveaux entrants efficaces en accentuant la perception d'un risque à l'entrée¹¹³ et aussi inciter les entreprises en difficulté financière à rechercher d'autres moyens plus préjudiciables, et éventuellement illégaux, de s'assurer de la poursuite de leurs activités. Par exemple, les entreprises peuvent essayer de parvenir à un accord avec leurs concurrents pour augmenter leurs flux de recettes et leurs bénéfices. Il n'est pas facile de mettre au jour de telles ententes. Autrement, les entreprises peuvent demander le soutien de l'État. Bien que cela ne soit pas forcément préjudiciable au corps social, une solution du secteur privé aux difficultés financières d'une entreprise peut être préférable à une intervention de l'État.

4.2 *Une alternative fondée sur les effets*

Une alternative à l'approche actuelle concernant l'argument de l'entreprise défaillante serait d'évaluer les effets concurrentiels des fusions concernant des entreprises défaillantes dans le cadre d'une contre-analyse en deux étapes fondée sur les effets. Durant la première étape, les autorités de la concurrence évalueraient les éléments présentés par les parties à l'opération, leurs concurrents et les clients afin de déterminer quel est le contre-scénario le plus probable sans a priori ou présuppositions. Durant la deuxième étape, les autorités de la concurrence compareraient l'ampleur et la vigueur de la concurrence selon les scénarios après la fusion et contrefactuels et elles n'approuveraient la fusion, sans imposer de mesures correctrices, que si le scénario après la fusion s'avère meilleur.

Comme l'approche actuelle, cette alternative peut aussi donner lieu à des erreurs de type I et de type II. Cela étant, on peut penser qu'elle engendrera relativement moins d'erreurs de type I car, contrairement à l'approche actuelle, elle ne présuppose pas que le scénario après la fusion est nécessairement plus préjudiciable que les autres contre-scénarios possibles – une supposition qui n'est pas forcément juste. Une fusion sera bloquée selon l'approche fondée sur les effets *seulement si* les faits montrent qu'elle risque de réduire la concurrence par rapport à l'intensité de la concurrence obtenue dans le cadre du ou des contre-scénarios les plus probables. Selon cette approche, les parties à l'opération doivent prouver que l'entreprise cible est en difficulté financière et qu'il existe un risque significatif qu'elle quitte le marché en l'absence de fusion. Elles doivent aussi présenter les preuves nécessaires permettant d'évaluer la probabilité des autres contre-scénarios. C'est aux autorités de la concurrence qu'il incombe de décider du contre-scénario pertinent et de prendre la mesure des effets anticoncurrentiels de la fusion proposée en utilisant le contre-scénario comme point de comparaison.

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Mason, R. & H. Weeds. 2002. The Failing Firm Defence: Merger Policy and Entry. Document de travail du CEPR n° 3664, p. 30.

Par contre, l'approche fondée sur les effets peut aboutir à des erreurs de type II plus nombreuses, que l'approche actuelle. De plus, elle risque d'être plus difficile à gérer. La collecte et l'analyse des éléments factuels peuvent être un processus complexe, coûteux et long. Elle peut aussi donner des résultats moins prévisibles. Une analyse factuelle au cas par cas peut limiter la capacité des parties à l'opération à prévoir, avant la fusion, l'issue qu'aura le contrôle de la fusion.

4.3 Conclusion

La crise financière actuelle pose un problème supplémentaire pour l'application de l'argument de l'entreprise défaillante. On peut se demander si la politique suivie et ses exigences devraient être assouplies, les attitudes actuelles face à l'argument de l'entreprise défaillante pouvant donner lieu à de nombreuses erreurs de type I, qui risquent d'être inacceptables dans un contexte de difficultés économiques et financières. Cette section a examiné l'intérêt relatif de l'adoption d'une approche fondée sur les effets pour évaluer les fusions concernant des entreprises en difficulté financière. Cette approche peut réduire la fréquence des erreurs de type I mais elle peut provoquer davantage d'erreurs de type II. Elle peut aussi être plus difficile à gérer et réduire la certitude légale par rapport au scénario actuel.

5. Conclusion générale

En des temps de crise financière et économique, comme ceux que nous traversons actuellement, les entreprises sont plus nombreuses à connaître des difficultés financières. La crise actuelle a non seulement affaibli les institutions financières, mais elle a aussi eu un impact sur toute l'économie. Les entreprises en difficulté financière chercheront des solutions pour assurer leur survie à long terme ; une de ces solutions est de fusionner avec des partenaires en meilleure santé. Les autorités de la concurrence peuvent être confrontées à un nombre croissant de fusions impliquant des entreprises en difficulté financière, certaines étant des entreprises réellement défaillantes et d'autres simplement des concurrents fragilisés ou encore des entreprises en récession. Dans certains de ces cas, l'argument de l'entreprise défaillante peut être avancé afin d'obtenir le feu vert pour l'opération. Le présent rapport a examiné si les attitudes de plusieurs membres de l'OCDE face à l'argument de l'entreprise défaillante permettent de relever le défi que constitue l'évaluation de ces opérations en ces temps difficiles.

Ces politiques, qui sont exposées dans des lignes directrices sur les fusions ou que l'on peut déduire des décisions concernant les fusions, s'articulent autour d'un certain nombre de conditions strictes : l'entreprise présumée défaillante et ses actifs doivent disparaître du marché dans un proche avenir si la fusion n'a pas lieu et il ne doit pas exister d'autre solution de rachat, moins préjudiciable pour la concurrence, que la fusion proposée. Il incombe aux parties à l'opération de démontrer que ces exigences sont respectées. On ne s'étonnera pas, du fait des preuves particulièrement solides qui sont exigées, que très peu de cas où l'argument de l'entreprise défaillante a été invoqué aient abouti. Et rien ne permet de croire que cet état de fait va changer dans le contexte actuel d'instabilité financière et de récession économique.

La présente note se demande si cet état de fait est optimal. On a pu constater que les critères actuellement utilisés pour évaluer l'argument de l'entreprise défaillante sont axés sur la minimisation des erreurs de type II – agrément, à tort, d'opérations de fusion ou application de mesures correctrices insuffisantes – et peuvent donc entraîner de trop nombreuses erreurs de type I – interdiction à tort d'opérations de fusion ou application de mesures correctrices disproportionnées. On a vu également qu'une approche davantage fondée sur les effets qui cherche prioritairement à identifier le contre-scénario le plus probable et à comparer les résultats du scénario post-fusion avec ceux d'un tel contre-scénario réaliste peut diminuer le nombre d'erreurs de type I, mais augmenter en revanche la probabilité d'erreurs de type II. Une approche fondée sur les effets peut aussi entraîner une augmentation des coûts de mise en œuvre et un allongement de la durée des enquêtes. L'issue peut en outre en être moins prévisible.

Les pays de l'OCDE devraient se demander si les partis pris des attitudes actuelles face à l'argument de l'entreprise défaillante se justifient. Ils peuvent conclure que c'est effectivement le cas, car ce moyen de défense est, en tout état de cause, seulement applicable à un petit pourcentage de fusions et il est important de conserver un point de vue rigoureux vis-à-vis de fusions dans le cadre desquelles une entreprise est cédée à un concurrent direct. Ils peuvent aussi considérer qu'il existe d'autres instruments d'action publique (par exemple, la loi sur les faillites, les aides de l'État) pour éviter la liquidation inefficace d'entreprises en difficulté financière. Qu'ils décident ou non de réexaminer ces politiques, il n'en reste pas moins que certains aspects de ces politiques sont complexes et que d'autres, comme la validité de l'argument dit de « l'entreprise en récession », ne sont pas clairs. Certaines autorités de la concurrence dans le monde ont publié des lignes directrices sur les modalités d'analyse de l'argument de l'entreprise ou de la division défaillante ou en récession qu'elles appliquent ;¹¹⁴ nous encourageons les autres à suivre leur exemple.

¹¹⁴ Les lignes directrices relatives à l'argument de la division défaillante s'appuient généralement sur le même type de raisonnement que l'argument de l'entreprise défaillante. Voir par exemple les Horizontal Merger Guidelines [Lignes directrices sur les fusions horizontales] du ministère américain de la Justice et de la Federal Trade Commission, modifiées le 8 avril 1997, §5.2 ; UK Competition Commission. 2003. Merger references: Competition Commission Guidelines. Juin 2003, § 3.63 ; ou Bureau de la concurrence du Canada. 2004. Fusions - Lignes directrices sur l'application de la Loi. Septembre 2004, Partie 9 – Déconfiture de l'entreprise, §9.5.

BELGIUM

1. Definition of the FFD

There is as yet no case law in Belgium applying (or refusing to apply) the failing firm defence.

2. Type and Quantum of Evidence

As indicated in response to the previous question, we cannot (yet) refer to case law. We suggest, however, the following approach:

2.1 *What kind of evidence – and how much of it – is necessary to satisfy a court or an agency that a firm is actually ‘failing’?*

We expect that a Court will require that the company accounts, and where relevant the management plans of the parent company, show beyond reasonable doubt that bankruptcy or closure was to be expected/was the most likely outcome, or in other terms that a market exit was to be expected.

2.2 *What counterfactual scenarios should be examined: should the only alternative to be examined be the one of exit from the market or should it encompass a loss of competitive constraint on the part of the target (for example, poor enough performance so as to prevent outside financing at affordable rates), other possible transactions, etc.*

We expect that a Court, unless EU precedents or guidelines point in another direction, will require that the counterfactual scenario be exit from the market. Also, the OECD report 1995 refers to failing as ‘a situation where it is virtually certain that, absent a merger, the failing firm will be forced to liquidate’.

However, in economic terms, it is very hard to establish when a firm will be very likely to be forced to liquidate. Accounting ratios that may indicate that a firm is in a financially difficult situation. Nevertheless, a recovery of the firm’s activity and financial health is not excluded even if the accounting data point to a very difficult situation. A more formal proof failing might be when a firm is under an official pre-bankruptcy regime. But even in that case, a temporary protection against creditors may help to solve the financial difficulties of firms and do not offer certainty that a firm will exit the market if the merger is blocked. This is demonstrated by many cases in which firms attempt to improve their business situation while under a regime of the U.S. Chapter 11 (as opposed to Chapter 7). Financial difficulties can also be caused by temporary problems or phases in business cycles. Consequently, the structural characteristic and underlying cause of the financial distress should be evaluated. The track record of accounting data can only offer a partial answer to this issue. And financial difficulties can be caused by managerial inefficiency. In that case, other alternatives could solve the difficulties.

We consider moreover that there is a good case to argue that effective competition is not impeded significantly when a firm ceases to compete independently in case (1) that firm was no longer able to exercise competitive constraint on the relevant market and (2) other competitors will continue to be able to exercise sufficient competitive constraints after the transaction.

We consider that the impact of the acquired capacity in relation to the remaining competitive constraints is more significant than the question whether the counterfactual scenario is a market exit or not.

2.3 *What should be the depth of the analysis to gauge the potential impact on competition of each of the alternative scenarios? Under what circumstances should an enforcement agency or court be satisfied that an otherwise anticompetitive merger is the best known alternative?*

The agency should not oppose a transaction in case the remaining competitors, or the competitors of whom market entry is sufficiently likely, will continue to be able to exercise sufficient competitive constraints without undue impact on them (the balancing of effects with emphasis on the assessment of constraints).

2.4 *Failing Divisions. What should be done when the failing “firm” is a division of a larger, viable company? In other words, should a “failing division” defence be allowed? If so, why? What kind of evidence should be required to establish it?*

It makes in our opinion in principle no difference whether the ‘failing firm’ is an independent company or part of a larger group or a larger viable company. We see nevertheless some specific issues in respect of failing divisions or subsidiaries:

- In case a transaction could be authorised in the light of the benefits of a soft landing scenario for the failing firm, the soft landing defence is less likely to be convincing in case the failing firm is a division of a larger healthy company or a subsidiary; and
- One should also be aware of the risk that accounting techniques may have been used to show a subsidiary and especially a division as more failing than it actually is, thus abusing the failing division defence.

3. *Market context*

3.1 *Declining Industry. Should it matter to the analysis that the failing firm is part of a declining industry?*

In case the transaction affects competition in a declining industry, the competitive constraints exercised by substituting products or industries may be more relevant than the competition by direct competitors.

It will also be relevant for the assessment of transactions whether they can be seen as part of a credible soft landing scenario for the declining industry. In that respect the nature of the market and the competitive structure needs to be assessed. Is there excess capacity because of declining demand or because too large a number of players? Is the decline only a local phenomenon because of a delocalisation of the market? In that case a merger with a competitor may be necessary in order to create a world-wide important player. And also, is the decline a consequence of a temporary downward movement in a business cycle: in other words, does the specific industry offer sufficient opportunities to make a financially distressed company viable in the longer term.

3.2 *Nature of competitive interaction. Should the type of competition in the market(s) affected by the transaction matter in the assessment of the FFD? In particular, should court and agencies be more lenient when firms compete for the market through investment and innovation?*

If a market is characterised by a high investment and innovation activity, the expected margins will usually be high. But if they are not (or will no longer be in case of an increased number of competitors), entry to such markets by new players is often difficult:

- A merger between a failing firm and an incumbent might be used by the incumbent to further hamper entry to the market. This approach advocates extra caution when evaluating this type of mergers. A trade-off has to be made with the loss of expertise and production capacity (and *e.g.* consequences for the supply of a market) when a merger is blocked and the failing firm exits the market; and
- A merger between a new player and a failing firm leads to important benefits for the entrant as knowledge, experience and production infrastructure are available with a minimum of effort.

3.3 *Small economy. What role, if any, does the size/extent of the local market play in the evaluation, as opposed to the size of any trans-border or global market? What role, if any, does the industry's importance to the local economy play when assessing an FFD defence?*

Competition must be assessed on the relevant market. The fact whether or not the relevant geographic market is small, will inevitably impact on the assessment.

We must, however be very prudent with regard to the impact of the size of the economy on the assessment. FFD may be a way to safeguard locally important industries. Exit of firms means job losses, losses for shareholders and creditors and exits of closely linked firms. Nevertheless, FFD cannot be a way to safeguard industries that are not viable on long terms. In this sense, the size of the economy and the importance of the industry should not be a criterion to evaluate FFD, but rather the size of the market, which could be trans-national, and the consequences for competition.

But this prudence should not exclude a degree of understanding for realistic soft landing scenarios.

3.4 *Capital markets. Should the assessment of the FFD take into account possible limitations in the availability of external funds (debt and equity) resulting from the particular characteristics of the industry in which the merging parties operate or more general macroeconomic conditions?*

The availability of external funds in general, or for a specific industry, will inevitably impact on the assessment of the viability of firms and of the competitive constraints they can be expected to exercise.

If a concentrated market has a lack of funding because of its particular characteristics, a merger of a failing firm with a dominant player will enforce the latter's position. Absence of viable alternatives because of a lack of funds should not be a reason to allow unconditionally mergers of failing firms.

4. *Should the FFD Analysis Be Changed During Economic Crises? Because of the current global economic crisis, we may expect to hear that the FFD should be made easier to invoke. It may be argued, for example, that maintaining the traditionally high hurdles for the FFD will get in the way of much-needed rationalisation of the over-capacity that now exists in many industries. Or some might argue that mergers should be encouraged in order to strengthen weakened industries. Alternatively, some might point out that because the availability of capital is now much lower than usual, authorities cannot afford to be so selective in approving buyers. Otherwise, it may take too long to find a buyer who presents few or no competitive concerns and who can actually raise the necessary financing to acquire the (failing) target firm. Do these or any other arguments justify a more lenient approach?*

Subject to the issue of financial institutions, we do not think that the FFD should be made easier to invoke. But there are likely to be more failing firms.

We suspect that the FFD may even be rather more difficult to invoke because it is more difficult to determine the relevant counterfactuals in case firms are failing due to the credit crisis.

5. **Mergers between Financial Institutions. Do any special issues arise when the FFD is invoked in a merger between financial institutions (during a financial crisis)? If so, what are they and how should they be handled? What should be the relative weight attributed to competition and prudential objectives in the assessment of mergers between financial institutions?**

As indicated during the Roundtables on competition and financial markets (17 and 18 February 2009) we consider that mergers in the financial sector in times of crisis should not only be assessed in the light of their impact on the structure of relevant markets. They should also be assessed in the light of the probability that the transaction will help to avoid bankruptcies in the financial sector beyond the boundaries of the directly affected relevant markets, and of the impact bankruptcies of financial institutions have on public finance.

6. **Interplay with other policy instruments. How should a more lenient approach to FFD be articulated with other aspects of competition policy such as the review of agreements or the assessment of State Aids (where applicable)?**

We only argue in favour of a more lenient approach to FFD in respect of financial institutions. This has had during the last year no impact on our substantial assessment of agreements or market behaviour but it may have had an influence on the decision to prefer an informal approach to a formal investigation.

The Belgian Competition Authority has no powers in respect of state aids.

CANADA

Despite continued uncertainty regarding the extent of the current economic downturn, governments face significant pressures to implement measures that will facilitate rapid recovery. The collapse of once-venerable financial institutions¹ and other established businesses has sparked debate over the most appropriate manner of addressing the economic hardships brought about by the crisis, including the propriety of relaxing competition laws to allow for fewer regulatory barriers to the restructuring of industries under pressure.

Although some may argue that competition principles should be subordinated to broader economic concerns, the Competition Bureau (the “Bureau”) remains of the view that the principled and undiluted continued enforcement of competition laws will contribute to speedier recovery from an economic downturn. Canada’s competition framework has proven flexible enough to accommodate both ordinary and extraordinary market conditions, and times of crisis should not prompt any retreat from this framework.

This flexibility to Canada’s regime is evident in the Bureau’s *Merger Enforcement Guidelines* (the “MEGs”),² which mandate a consideration of factors that are clearly sufficiently broad to account for a variety of prevailing economic conditions, including those associated with a contraction or recession. For example, as to barriers to entry, an inability to secure financing in current capital markets may suggest that entry is less likely. Similarly, market shares in the current economic climate may not accurately reflect firms’ competitive significance. Other factors, including a consideration of the financial viability of a firm (or the “failing firm factor”) in merger review, can assume greater significance in difficult economic times than they otherwise would in times of prosperity.

In all environments, sensitivity to the economic realities of the marketplace should not only be accommodated by the Bureau’s analytical framework itself, but also addressed by the manner in which the framework is implemented. In this regard, the economic crisis challenges the Bureau to identify all possible means of achieving greater procedural and organisational efficiencies to expedite the merger review process.

1. The “Failing Firm” Factor in Canadian Merger Review

In times of economic hardship, it is not unreasonable to expect an increase in the number of mergers involving firms in financial distress. The financial viability of a firm (the “failing firm factor”) is one of a number of factors enumerated in section 93 of Canada’s *Competition Act* (the “Act”) that are considered in the analysis of a merger’s competitive effects. In particular, subsection 93(b) states:

¹ High-profile examples include the bankruptcy of Lehman Brothers Holdings Inc. and subsequent acquisition in part by Barclays PLC and Nomura Holdings, Inc.; the acquisition of Merrill Lynch & Co., Inc. by Bank of America Corporation; the acquisitions of Washington Mutual Bank and The Bear Stearns Companies Inc. by J.P. Morgan Chase & Co.; and the acquisition of Wachovia Corporation by Wells Fargo & Company.

² Available online: Competition Bureau [http://www.competitionbureau.gc.ca/eic/site/cbbc.nsf/vwapj/2004%20MEGs.Final.pdf/\\$file/2004%20MEGs.Final.pdf](http://www.competitionbureau.gc.ca/eic/site/cbbc.nsf/vwapj/2004%20MEGs.Final.pdf/$file/2004%20MEGs.Final.pdf).

In determining, for the purposes of section 92, whether or not a merger or proposed merger prevents or lessens, or is likely to prevent or lessen, competition substantially, the Tribunal may have regard to the following factors:

(...)

(b) whether the business, or a part of the business, of a party to the merger or proposed merger has failed or is likely to fail.

Under the Act, failing firm claims are not treated as a defence to an otherwise anti-competitive merger, but are assessed within, and as part of, the competitive effects analysis of a proposed transaction. The Bureau's analytical approach to the assessment of claims made pursuant to subsection 93(b) is outlined in the MEGs. In particular, the MEGs recognise that the loss of the actual or future competitive influence of a failing firm should not be attributed to a proposed merger involving that firm if imminent failure is probable and, in the absence of a merger, the assets of the firm would be likely to exit the relevant market.³

Pursuant to the MEGs, the Bureau will assess the financial state of the allegedly failing firm to determine whether: it is insolvent or is likely to become insolvent; it has initiated or is likely to initiate voluntary bankruptcy proceedings; or, it has been, or is likely to be, petitioned into bankruptcy or receivership. In considering these issues, the Bureau may retain third-party financial experts to review, for example, the firm's most recent audited financial statements, projected cash flows and other forms of financial data described in the MEGs.

In addition to assessing the firm's financial condition, the Bureau will also consider whether alternatives exist to the proposed merger that would result in a materially greater level of competition than if the proposed merger proceeds. One such alternative involves an assessment of whether the firm might be acquired by a competitively preferable third party. Such a third party must be willing to pay a price that, net of the costs associated with making the sale, would be greater than the proceeds that would flow from liquidation, less the costs associated with such liquidation ("net price above liquidation value").⁴ The firm must also demonstrate to the Bureau that an appropriate "shop" has been conducted for alternative purchasers. In this regard, the Bureau will review documents provided by the parties with respect to the nature and extent of the shop process, and engage in conversations with bidders and alleged bidders to ensure, among other things, that they were given a fair opportunity to bid for the claimant's business. Where necessary, the Bureau has, in the past, secured orders to obtain documents relating to the shop process from a third party investment dealer, trustee or broker who conducted the shop on behalf of the claimant.

Other alternatives to the merger that are considered by the Bureau include whether retrenchment or restructuring would prevent the firm's failure and enable it to survive as a meaningful competitor, and whether the claimant's liquidation might constitute a preferable course of action. In each case, the Bureau examines whether the alternative would result in a materially higher level of competition in a substantial part of the market than if the merger in question were to proceed.

Notably, the failing firm analysis conducted pursuant to the MEGs does not require consideration of matters unrelated to competition, including the social ramifications of a firm's potential bankruptcy or insolvency (such as significant loss of employment or loss of shareholder value). In difficult economic times, pressures to consider these issues tend to increase, but they are generally outside the scope of the

³ *Ibid.* at para. 9.2.

⁴ *Ibid.* at para. 9.8.

Bureau's mandate. In carrying out its assessment of a proposed merger (whether involving a failing firm or otherwise), the Bureau's analysis is directed at determining whether the merger is likely to result in a substantial lessening or prevention of competition, and to resolve these concerns accordingly. The failing firm factor in Canadian merger review is not a mechanism to balance broad social interests against any lessening of competition associated with the proposed merger.

Perhaps because of the practical implications for a claimant in asserting that it is failing (including, for example, possible freezing of the supply of necessary inputs and sources of credit), failing firm claims have arisen relatively infrequently in the Bureau's reviews. Yet, where such claims are made, each element of the framework is assessed as part of a thorough analysis of the competitive effects of the proposed transaction. For example, in *Canada (Director of Investigation and Research) v. Canadian Pacific Ltd.*, the Notice of Application⁵ filed with the Competition Tribunal reviewed each of the alternatives to the merger as mandated by the MEGs, concluding that the anti-competitive effects of the proposed merger could have been avoided through one of those alternatives.

2. Example of a Case involving Failing Firm Considerations

In mid-2009, the Bureau engaged in a detailed review of a proposed transaction in which the parties relied heavily on a failing firm claim. An analysis of the acquiree's financial statements, interviews with suppliers and creditors, and discussions with an accounting expert specialising in insolvency led the Bureau to conclude that failure was, indeed, likely and imminent. However, the Bureau did not believe that an appropriate "shop" of the business had been conducted to determine whether a competitively preferable purchaser existed.

In particular, the Bureau determined that there existed a third party whose purchase of the acquiree was likely to result in a materially higher level of competition in a substantial part of the market. This third party purchaser was willing and able to offer a net price above liquidation value. In the view of the Bureau, this indicated that, in the absence of the proposed transaction, the acquiree was not likely to exit the market in the face of a desirable alternative to liquidation. The alternative purchaser in question constituted a new entrant into the relevant markets, whereas the acquiree's proposed transaction contemplated a merger of competitors that raised serious competition concerns.

The Bureau conducted extensive interviews with all stakeholders, including the competitively preferable purchaser and the acquiree's secured lender, and determined that adequate time remained to assess whether the competitively preferable purchaser was still willing to purchase the business at a net price above liquidation value and to provide an offer capable of acceptance by the failing firm and its secured creditor. This position was communicated to the acquiree, who ultimately consummated the transaction with the competitively preferable purchaser.

3. Achieving Improved Procedural Efficiency in Merger Review

The failing firm factor and other aspects of the analytical framework described in the MEGs promote a principled approach to the assessment of mergers that is equally applicable in ordinary and extraordinary market conditions. At the same time, the Bureau recognises that its processes for the implementation of this analytical framework must be applied in a manner that maximises procedural efficiency while accounting for prevailing economic conditions.

Mergers involving failing firm claims give rise to considerations of timeliness and efficiency that pose challenges even in ordinary economic times. Accordingly, the Bureau is committed to exploring all means

⁵ (20 December 1996), CT-1996/002 (Comp. Trib.) at 35 – 38.

of expediting these reviews. For example, the Bureau has devoted resources to identify industries where there have been indications that failing firm claims may be likely. Also, where the merging parties have asserted that the failing firm factor was applicable, the Bureau has conducted a focused analysis of this issue in priority to a full assessment of the potential competitive effects of a transaction, including using tailored investigatory orders designed to determine whether the failing firm framework was satisfied. This assumes that the failing firm argument is submitted early in the process. For example, acquirees should not wait for the Bureau to express concern about the competitive impact of the proposed transaction before submitting a proper failing firm submission.

A similar commitment to expedition is reflected in the Bureau's approach generally to supplementary information requests ("SIRs") issued pursuant to the Bureau's two-stage merger review process. The Act establishes an initial 30-day waiting period during which the vast majority of notified mergers are cleared. For those few transactions that give rise to potentially significant issues, the Bureau may issue a SIR for additional relevant information. The issuance of a SIR to one or more notifying parties triggers a second 30-day waiting period, which commences when the Commissioner receives from each recipient a complete response to all information requests set out in the SIR. In all investigations, including SIR processes, the Bureau seeks to isolate potentially seriously problematic issues and to narrow and front-end load information requests.

In the context of a failing firm submission, during the initial 30-day waiting period, the Bureau engages in discussions with the parties regarding any failing firm submission and, if applicable, prepares a SIR for issuance to the parties. All questions relating to failing firm claims or the financial viability of the allegedly failing firm can be prioritised and addressed first by the parties. The parties' responses to these questions, in combination with other evidence that may be required to complete a preliminary assessment of the competitive effects of the transaction, could serve to reduce and expedite the Bureau's review. Again, the Bureau has been clear that parties need not wait to advise the Bureau of failing firm submissions until a formal merger notification has been submitted, and are encouraged to provide a failing firm submission at the earliest possible opportunity.

Further, the Bureau makes a particular effort in the failing firm context to be clear with the parties as to what is, or is not, required. Although the analytical framework set out in the MEGs requires that valid failing firm claims establish that "imminent failure is probable", merging parties are not required to establish that the firm has actually failed. Accordingly, the Bureau has provided guidance to firms under severe financial distress as to whether they are likely to satisfy the failing firm criteria in the MEGs and, where applicable, the Bureau has outlined the types of information and other steps that would be required from the allegedly failing firm to satisfy these criteria.

In addition to its assessments of failing firms *per se*, the Bureau has also provided guidance in a related context; namely, in merger transactions involving the acquisition of assets from a "failed" firm, such as a business that is in liquidation, receivership or bankruptcy. Such transactions could give rise to particular analytical challenges that must be resolved on a case-by-case basis. For example, the notion of an "operating business" is important to determine whether a proposed transaction is subject to notification under Canada's competition regime. Where a firm has failed and has permanently closed, the firm likely will not constitute an "operating business" as defined pursuant to the notifiable transactions provisions of the Act. However, a business is not considered defunct by reason only that its assets have vested in a trustee in bankruptcy pursuant to Canada's *Bankruptcy and Insolvency Act*, or that its assets have been placed in receivership. Indeed, if a trustee or receiver is carrying on a business undertaking with a view to disposing of the business as a going concern or to reorganising its affairs, the business undertaking may still be considered an "operating business". Where the operating business cannot be carried on or sold as a

going concern, and the trustee or receiver takes steps to liquidate the assets on a piece meal basis, the undertaking may no longer be an “operating business”.⁶

Concerns with respect to timeliness and efficiency of merger reviews involving failing firm-related claims can also assume greater urgency in a multi-jurisdictional context. Importantly, at least superficially, the definition and application of the failing firm concept varies among jurisdictions. However, a comparative assessment of failing firm frameworks of other jurisdictions reveals that many of the considerations reviewed by applicable competition authorities, including, for example, those of the United States⁷ and the United Kingdom,⁸ are fundamentally equivalent to the considerations reviewed by the Bureau. To the extent that such consistencies exist, it would be beneficial for competition authorities to align their respective frameworks for analyses by communicating with one another regarding the details of their failing firm assessments and preliminary conclusions as they are reached. Sharing conclusions regarding alternatives to the merger, including determinations of competitively preferable third party purchasers, the propriety of liquidation and the potential for restructuring, would save all agencies resources and shorten review timelines. Notably, this type of alignment initiative may depend upon the merging parties’ willingness to supply waivers to competition authorities who require them before they can share information with other competition authorities.⁹ The parties’ timeliness in providing such waivers will assist greatly in realising the benefits of international co-ordination.

4. Conclusion

In assessing the impact of the economic crisis and co-ordinating an appropriate response, competition law enforcement and policy should be regarded as key components to any successful strategy for economic

⁶ For further discussion of what constitutes an operating business for purposes of Canadian competition law, please see the Bureau’s *Interpretation Guideline No. 1*, online: <http://strategis.ic.gc.ca/pics/ct/nt-interpret-e2.pdf>.

⁷ The U.S. Department of Justice’s (“DOJ”) *Horizontal Merger Guidelines*, state at page 33 that the DOJ’s failing firm analysis will consider whether: 1) the allegedly failing firm would be unable to meet its financial obligations in the near future; 2) it would not be able to reorganize successfully under Chapter 11 of the *Bankruptcy Act*; 3) it has made unsuccessful good-faith efforts to elicit reasonable alternative offers of acquisition of the assets of the failing firm that would both keep its tangible and intangible assets in the relevant market and pose a less severe danger to competition than does the proposed merger; and 4) absent the acquisition, the assets of the failing firm would exit the relevant market. See DOJ’s *Horizontal Merger Guidelines*, online: <http://www.usdoj.gov/atr/public/guidelines/hmg.pdf>.

⁸ The U.K. Office of Fair Trading’s (“OFT”) *Restatement of OFT’s position regarding acquisitions of “failing firms”* indicates that the following conditions must be met in order to establish the failing firm defence: (i) inevitable exit of the target business absent the merger (the target business would inevitably have exited the market in the near future; having demonstrably explored such options, there is no serious prospect of the target business being reorganised); and (ii) no realistic and substantially less anti-competitive alternative (there are no other realistic purchasers whose acquisition of the target business would produce a substantially better outcome for competition. Even if such a purchaser may not pay the seller as high a purchase price or otherwise benefit the target business, the OFT will take into account any realistic prospect of alternative offers above liquidation value; alternatively, in some cases it may also be better for competition that the target business fails and the remaining players compete for its market share and assets rather than being transferred wholesale to a single purchaser). See the OFT’s *Restatement of OFT’s position regarding acquisitions of “failing firms”* online: OFT <http://www.oft.gov.uk/shared_of/business_leaflets/general/oft1047.pdf>

⁹ Note that the Bureau does not require waivers to share information with foreign enforcement authorities. Section 29 of the Act provides the Bureau with discretion to disclose information “for the purposes of the administration and enforcement of the Act”.

recovery. Canada's competition framework has proven flexible enough to accommodate both ordinary and extraordinary market conditions, and times of crisis should not prompt any compromise to this framework.

The Bureau will continue to identify all possible means of achieving greater procedural and organisational efficiencies in the merger review process, including devoting additional resources to expedite the review, where possible, when firms are under severe financial distress, prioritising the analysis of the failing firm factor in the review of the overall competitive effects of a transaction and providing guidance to allegedly failing firms as to whether they are likely to satisfy the failing firm criteria in the MEGs.

CHILE

1. Introduction

Under economic recession, the failing firm defence becomes more relevant and pressuring on competition authorities, whose policies and decisions are compelled to consider changing market conditions and global consequences of a more uncertain economic environment.

From the competition authorities' view, merger analysis assesses the impact of a transaction, based upon a hypothetical comparison of the likely future state of competition on the affected relevant markets if the transaction goes on (*i.e.* the factual scenario) against the likely state of competition if it does not (*i.e.* the counterfactual scenario). In this assessment, the “failing firm defence” is sometimes used by merging parties to argue that the merger should be approved as the acquisition of a “failing firm” that otherwise would be forced to leave the market in the short term.

Under the failing firm defence criterion, a merger does not rise a substantial lessening of competition in cases in which the merged or acquired business will anyway exit the market. Hence, any substantial lessening of competition identified in the analysis of the operation is not directly attributable to the merger.

The Chilean experience on merger assessment is somehow determined by the fact that the Chilean Competition Act, enacted in 1973, does not consider mandatory notification provisions for mergers and acquisitions, in the sense that this restricts the number of cases that have been reviewed by the authorities. Perhaps for this reason, it is possible to find only one case law, in the early 80s – *Comercial Huechuraba Ltda.*, on the alcoholic beverage and beer's elaboration market – where the failing firm defence was argued by the involved parties and was fully considered by the Antitrust Commission to base on its final ruling.

2. Case Law on Failing Firm Defence in the Breweries Market

In January 1981, *Comercial Huechuraba Ltda.* acquired 95% of the equities of *Cervecería del Pacífico S.A.* As stated in the case, the acquirer was owned by the controllers of *Cervecerías Unidas S.A.* (CCU), the leading domestic beer company, a clear dominant player in the market.

Once the *Comisión Preventiva Central* (CPC¹) reviewed the facts, they determined that the transaction should have previously been consulted, since this company could have represented a competitive alternative for CCU in the alcoholic beverage and the beer market.² Accordingly, the CPC's instructed the *Fiscalía Nacional Económica*³ to investigate the case, and to pursue a fine for the companies since they did not consult the operation.

¹ Administrative body in charge of the issuance of preventive injunctions and recommendations on competition matters. They existed until the 2004 amendments to the DL 211.

² Decision No 275 / 1981, May.

³ Competition Agency responsible for investigating competition cases.

The acquirer challenged this decision by submitting an appeal to the *Comisión Resolutiva*⁴ (Antitrust Commission), based on the argument that the Competition Act had no provision on mandatory consultation for any conduct.

The Antitrust Commission decided⁵ to accept the claim grounded on the fact that there was no provision requiring consultation to buy shares of an insolvent company by a competitor since, under such conditions, it does not mean eliminating an effective or a potential competitor. In addition, its ruling also established that the **disappearance of a competitor in bankruptcy or insolvency, whose market share has been very weak, does not seriously affect competition in the affected market.**

Among the information available to the Antitrust Commission was the fact that:

- **Market share:** *Cervecera del Pacífico* reached a monthly share of 7,500 hectolitres (just 5% of the whole domestic market) and an installed capacity of 30 thousand hectolitres per month (*i.e.* 20% of the domestic beer market);
- **Financial reports:** Towards the end of 1980, according to their financial statements (audited by an external firm), *Cervecera del Pacífico* had lost over 70% of its capital and reserves, results that were confirmed by a second audited statement in June 1981;
- **Liquidity:** when the firm decided to sell, it required US\$ 8 million to avoid bankruptcy, an amount it could neither reach with its owners nor rise from financial markets;
- **Alternatives:** Due to the bad image of the firm, which eroded even the brand value, there were no alternative buyers.

Thus, although the ruling did not explicitly mention the failing firm defence criterion, the Antitrust Commission took into consideration that (1) it was foreseeable that *Cervecera del Pacífico* would have exited the market had not the operation gone ahead; and (2) there was no realistic less anti-competitive alternative to the acquisition; concluding that any consequent loss of competition was, therefore, attributable to the predictable failure rather than to the acquisition itself.

3. Competition Authority's Horizontal Guidelines

Historically, since the first Competition Act was enacted in 1973,⁶ Chile has no mandatory notification provision for merger and acquisitions (M&A), but a voluntary consultation system. Since the 2004's amendments to the Competition Act,⁷ M&A may be reviewed by the Competition Tribunal (*Tribunal de Defensa de la Libre Competencia*, TDLC⁸) if, according to an interested party or to the FNE, such merger may prevent, restrain or obstruct free competition as established under the Competition Act, article 3. In accordance with Competition Act, although mergers are not *per se* reproachable, they are susceptible to be blocked or conditioned following competition criteria. Nevertheless, the Competition Act does not contain specific rules on merger assessment.

⁴ A quasi-judicial body that decided on antitrust matters with adjudicative powers, until the 2004 amendments to the DL 211 by which the TDLC was created.

⁵ Ruling No 125/1982, November.

⁶ Decree Law No. 211, 1973.

⁷ The amendments to the Competition Act enacted in Law No. 19911 / 2004 introduced structural changes for the Competition System, mainly the creation of a Competition Tribunal. Recently, the last amendments enacted by Law No. 20361/2009, increases FNE's powers to deal with cartels and collusive agreements.

⁸ The Competition Tribunal, which decides on antitrust matters with adjudicative powers. It is integrated by five judges -three lawyers and two economists.

On October 2006, the FNE issued a guideline for the assessment of horizontal mergers (the “*Guía interna para el análisis de operaciones de concentración horizontal*”,⁹ hereinafter, ‘the Guide’). This Guide is an internal working tool providing useful information and orientation for firms and interested parties, concerning the main aspects, procedures and methodology employed by the FNE when analysing a horizontal merger, though its content is not mandatory for the TDLC or private parties. The Guide reflects the FNE’s understanding that the assessment of M&A is aimed at weighing up the risks of carrying out anticompetitive conducts by the resulting merger entity due to the increased concentration in the relevant market, *vis-à-vis* the resulting efficiency improvements.

The Guide focuses on relevant market definition, concentration levels, entrance conditions, risks resulting from the M&A and the expected efficiencies involved in the operation. In the Guide, the failing firm defence criterion is explicit. Thus, while assessing any M&A operation leading to horizontal concentration, the FNE considers whether the conditions to the failing firm defence are met.

Notwithstanding, since the issuance of the Guide there has been no consultation on M&A fencing the criterion of the failing firm. Moreover, of the 30 decisions -in non adversarial cases- rendered by the TDLC since its creation in 2004, only 5 have been related to M&A,¹⁰ none of which has been related to failing firms.

4. Conclusions

To prevent the pressures on competition authorities in times of economic slowdown, in order to provide excessive consideration to failing firm arguments, it is advisable that authorities commit *ex ante* to the criteria they shall take into consideration when analysing M&A. Guidelines seem to be powerful and useful tools in this sense.

Parties invoking the failing firm defence have to prove that the deterioration in the market competitive structure, following an M&A operation, is not caused by the operation itself. Defining clearly what constitutes adequate evidence that a firm is actually failing, and avoiding policy changes in regard to economic cycle seem to be key requirements for a consistent analysis and decisions by competition authorities.

In addition to adequate evidence on failure, before issuing their decision competition authorities should thoroughly examine two key aspects of the case. First, whether the failing firm can be acquired by an alternative buyer in such a way that market competition is not lessened (it is often the case that it can actually be enhanced), and finally examine whether the failure of the firm is not the result of anticompetitive conduct, which clearly rise a series of practical matters.

The FNE is currently assessing its respective Guide to reflect recent experiences in its application, changes in the legal framework and new procedural regulations issued by the TDLC.

⁹ The Guide was issued in May 2006 when the FNE uploaded a first draft of the document on its Website, in order to receive comments. Three months later the FNE released the final version of the Guide, which tenets have been followed by the FNE in concentration analysis ever since. A Spanish version of the Guide is publicly available at its Website, or linking http://www.fne.cl/?content=guia_concentracion.

¹⁰ These operations were: Resolution No 1/2004; about the merger between the two main Chilean cable television operators (*VTR-Metropolis*); Resolution No 2/2005; about the takeover of *BellSouth* by *Telefonica Movil*, in the mobile phone industry; Resolution No 20/2007, about the acquisition of a series of radio broadcast licenses by the subsidiary of an important radio conglomerate (*Prisa*); Resolution No 23/2008, about the merger between two pension and retirement plan administrators (*ING AFP Santa Maria* and *AFP Bansander*); and Resolution No 24/2008, rejecting the proposed merger between one of the main Chilean retail companies, *Falabella*, and the most important supermarket chain, *D&S*.

DENMARK

1. Introduction

This paper contains the views of the Danish Competition Authority (hereinafter: the DCA) on the topic of failing firm defence in merger cases.

Merger control was not introduced in Denmark until October 1st, 2000. The merger review thresholds with respect to the turnover of the merging companies are higher than in most other OECD countries. The Danish threshold for the combined turnover of the merging companies is at approximately 2.4% of GDP (2005). Similar figures for comparable countries such as the Netherlands, Norway and Sweden are all less than 0.5% of GDP. Consequently, the DCA investigates around 10 merger cases per year. Only a few of these enter into a phase II type investigation. The Danish merger thresholds are expected to be lowered significantly after a planned revision of the Danish Competition Act in 2010.

The low number of merger cases combined with the late introduction of merger control in Denmark limits the scope of the DCA's experience with merger control and, in particular, with failing firm defence. The views in this paper are based on legal provisions and considerations within the DCA in the wake of the ongoing economic crisis as well as the experience of the DCA with failing firm defence.

2. Specific Questions and Issues for Discussion

2.1 *Definition of the Failing Firm Defence*

How is the failing firm defence defined in your jurisdiction? Please refer to your jurisdiction's applicable court decisions, statutes, or competition agency guidelines. In particular, what criteria need to be met and what elements of proof are required in your jurisdiction to invoke the failing firm defence successfully?

The DCA has not yet based a merger approval on a failing firm defence, and only in one case have the merging parties invoked a failing firm defence, see paragraph 7 through 9. As a result only very limited jurisprudence can be derived from Danish case law. In 2007 the DCA issued guidelines on procedural issues in merger control, but the guidelines did not cover substantive issues such as failing firm defence. However, some jurisprudence may be derived from the explanatory notes to the Danish Competition Act.

According to the explanatory notes to the Danish Competition Act the test used to evaluate mergers, the SIEC test, is to be interpreted in accordance with the definition used in the EC Merger Regulation and in the Guidelines on the Assessment of Horizontal Mergers and Non-Horizontal Mergers as well as in accordance with decisions from the European Commission and judgments from the Community Courts. This congruence with EC merger regulation and case law also extends to the matter of failing firm defence.

Specifically, it is stated in the explanatory notes to the Danish Competition Act that a problematic merger need not be prohibited or made subject to remedies if the so-called 'failing firm defence principle' can be applied. The failing firm defence principle is described as the idea that an anti-competitive merger may be approved if the alternative, *i.e.* the failure of one or more of the merging companies, is equally or

more anti-competitive. Three cumulative conditions essential in the assessment of whether or not the failing firm defence principle can be applied are set out in the explanatory notes to the Danish Competition Act. The conditions are similar to those of the EU Horizontal Merger Guidelines, which are that:

- The allegedly failing firm would in the near future be forced out of the market because of financial difficulties if not taken over by another undertaking;
- There is no less anti-competitive alternative purchase than the notified merger; and
- In the absence of a merger, the assets of the failing firm would inevitably exit the market.

As mentioned, no decision in a Danish merger case has ever been based on a failing firm defence. In fact, the DCA has only once handled a merger case where the merging parties invoked a failing firm defence. However, in that particular case the failing firm defence was dismissed. In 2001 Steff-Houlberg, a Danish slaughterhouse and meat wholesaler, which was organised as a co-operative society, found itself in financial difficulties as society members, *i.e.* farmers, wanted to leave the society. In December 2001 Steff-Houlberg and competitor Danish Crown notified the European Commission of their intention to merge. The case was later referred to the DCA which examined the failing firm defence proposed by the merging parties. The DCA found that a failing firm defence was not applicable, as none of the conditions mentioned above were satisfied.

With respect to the first condition the DCA found it unsubstantiated by the merging parties that the migration of society members from Steff-Houlberg was severe enough to force Steff-Houlberg out of the market. Furthermore, the DCA saw the fact that Steff-Houlberg had made a profit as recently as in 2000 as an indication that Steff-Houlberg's financial difficulties might be only temporary. With respect to the second condition the DCA found that it could not be ruled out that a buyer other than Danish Crown could be found. The DCA noted that Steff-Houlberg had never been up for sale and concluded that given Steff-Houlberg's significant market share in Denmark other potential buyers, most likely from abroad, could exist. With respect to the third condition the DCA found it improbable that all society members of Steff-Houlberg would, in the event of Steff-Houlberg being forced out of the market, either join Danish Crown or leave the market altogether. Instead it was considered inevitable that a non-trivial share of the society members of Steff-Houlberg would join other smaller competitors.

On this basis the DCA rejected the failing firm defence invoked by Danish Crown and Steff-Houlberg. Ultimately, in April 2002 the merger was approved subject to remedies. This was the result after a standard assessment of the competitive effects of the horizontal merger.

In conclusion, the DCA found that the failing firm defence invoked by the parties in the Danish Crown/Steff-Houlberg merger could not satisfy the conditions set out in paragraph 6. Furthermore, the lack of other Danish merger cases where the parties have invoked a failing firm defence may, in part, be due to the very restrictive nature of those conditions.

2.2 *Type and Quantum of Evidence*

How can the elements you identify in response to the previous question be established? For example:

What kind of evidence – and how much of it – is necessary to satisfy a court or an agency that a firm is actually 'failing'?

What counterfactual scenarios should be examined: should the only alternative to be examined be the one of exit from the market or should it encompass a loss of competitive constraint on the part of the target

(for example, poor enough performance so as to prevent outside financing at affordable rates), other possible transactions, etc.

What should be the depth of the analysis to gauge the potential impact on competition of each of the alternative scenarios? Under what circumstances should an enforcement agency or court be satisfied that an otherwise anticompetitive merger is the best known alternative?

Failing Divisions. What should be done when the failing “firm” is a division of a larger, viable company? In other words, should a “failing division” defence be allowed? If so, why? What kind of evidence should be required to establish it?

As already mentioned the DCA has very limited experience with the failing firm defence and has no guidelines on the matter. However, from the Danish Crown/Steff Houlberg merger, see paragraph 7 to 9, it is clear that the DCA will evaluate the three conditions essential in the assessment of a failing firm defence, see paragraph 6, and will scrutinise any claim of impending failure by merging companies. It is also clear that a failing firm defence is unlikely to be accepted if the financial difficulties are only temporary.

With regards to counterfactual scenarios it is the view of the DCA that a number of outcomes as for the fate of the allegedly failing firm should be examined. This includes the two extreme outcomes, *i.e.* (1) imminent failure as well as (2) profitable future operation for the allegedly failing firm, but it may also include different degrees of down-sizing, divestitures, and loss of competitive power. In the end the relevant counterfactual should be constructed as the most likely outcome or set of outcomes. It should, of course, be noted that a failing firm defence is no longer applicable if the relevant counterfactual does not include the allegedly failing firm being forced out of the market in the near future. For example, a relevant counterfactual to a merger involving an allegedly failing company could be that the company alleged to be failing would remain in operation, but lose market share and competitive power. Such a counterfactual should be included in the standard merger assessment and could, given a thorough examination of the long term effects, count in favour of an approval, with or without remedies, though not with as much weight as a validated failing firm defence could have done.

2.3 *Harmonisation and Evolution*

Are you aware of approaches to the FFD that are different from the one used in your jurisdiction? If so, is the approach in your jurisdiction better? Why? Would it be sensible to try to harmonise the approach to the FFD across jurisdictions?

Has your own approach to the FFD evolved over the years and if yes, how and why?

Due to the very limited Danish case experience with respect to the failing firm defence the DCA can give no substantive answers to the questions above.

2.4 *Market Context*

Declining Industry. Should it matter to the analysis that the failing firm is part of a declining industry?

Nature of competitive interaction. Should the type of competition in the market(s) affected by the transaction matter in the assessment of the FFD? In particular, should court and agencies be more lenient when firms compete for the market through investment and innovation?

Small economy. What role, if any, does the size/extent of the local market play in the evaluation, as opposed to the size of any trans-border or global market? What role, if any, does the industry's importance to the local economy play when assessing an FFD defence?

Capital markets. Should the assessment of the FFD take into account possible limitations in the availability of external funds (debt and equity) resulting from the particular characteristics of the industry in which the merging parties operate or more general macroeconomic conditions?

With respect to market characteristics such as the availability of capital, the size of the market, the nature of the competitive interaction, and the potential decline of the industry it is the view of the DCA that such factors are already included in the evaluation of the three conditions essential to the assessment of a failing firm defence, see paragraph 6.

For example, a constrained capital market or a general decline of the industry would, all other things being equal, increase the likelihood of a company being forced out of the market in the near future and thus make that particular company a more eligible candidate for a failing firm defence. However, if an evaluation of the three conditions mentioned above leads to the rejection of a proposed failing firm defence, even when specific market characteristics such as the ones mentioned above are considered, the failing firm defence should be rejected. In other words, the standard of proof should remain the same regardless of the nature of the competitive interaction and whether the industry is in decline, the economy is small or capital is scarce.

It is the view of the DCA that any support for a local industry or market should be given in accordance with the EC Treaty provisions on state aid to avoid distortion of competition. This implies that any subsidies given to a local industry or market should be temporary, objective, transparent, necessary, non-discriminatory and proportionate. However, this should not be done through a more lenient approach to failing firm defence which could lead to inefficiency and long term anti-competitive effects stretching beyond the local economy or market.

2.5 *Should the Failing Firm Defence Analysis be changed During Economic Crises?*

Because of the current global economic crisis, we may expect to hear that the FFD should be made easier to invoke. It may be argued, for example, that maintaining the traditionally high hurdles for the FFD will get in the way of much-needed rationalisation of the over-capacity that now exists in many industries. Or some might argue that mergers should be encouraged in order to strengthen weakened industries. Alternatively, some might point out that because the availability of capital is now much lower than usual, authorities cannot afford to be so selective in approving buyers. Otherwise, it may take too long to find a buyer who presents few or no competitive concerns and who can actually raise the necessary financing to acquire the (failing) target firm. Do these or any other arguments justify a more lenient approach?

It is the opinion of the DCA that the approach to failing firm defence should not be more lenient during economic crises. However, the DCA does recognise that during an economic crisis more merging companies are potentially likely to be eligible for a failing firm defence, because more companies are likely to fulfil the three conditions essential in the assessment of a failing firm defence. However, the standard of proof required for a failing firm defence should remain unchanged during an economic crisis.

With respect to excess capacity, weakened industries, and scarcity of capital it is the view of the DCA that such market characteristics would already be taken into account if a failing firm defence was invoked by a set of merging companies. But this would be done in an indirect manner as all three characteristics might contribute to the likelihood of one or more of the three conditions essential in the assessment of a failing firm defence being met. This applies whether or not the characteristics mentioned are the result of

an economic crisis. As for the point about excess capacity it is interesting to note that ‘high hurdles’ for the failing firm defence may well put a stop to the kind rationalisation of over-capacity which can be achieved through mergers, but may also lead to a more abrupt re-scaling of capacity through company failures.

It is, however, not the view of the DCA that market characteristics such as excess capacity, weakened industries, and scarcity of capital, even if they are the result of an economic crisis, should, so to speak, be taken into account more than once. In other words if the three conditions essential in the assessment of a failing firm defence cannot be satisfied, even with contingencies caused by an economic crisis taken into account, then no further significance should be assigned to such contingencies.

It is important to emphasise that the DCA does not dismiss the idea that an economic crisis may create disruption, *e.g.* in the form of financial instability, so severe that government intervention is warranted. This may be the case even if such intervention harms competition in the short term. Nevertheless, it is also the view of the DCA that government intervention would be ill-suited to alleviate such disruption, if it came in the form of a more lenient approach to failing firm defence. A more lenient approach to failing firm defence would (1) fail to address the fundamental issue, *i.e.* the economic crisis, (2) be inherently random, and (3) potentially lead to permanent anti-competitive effects reaching beyond the economic crisis. Instead government intervention during an economic crisis could be aimed directly at preventing companies from failing, as has been the case with recent stimulus packages in many OECD countries, and thus at preventing the need for anti-competitive mergers.

In conclusion, it is the view of the DCA that the failing firm defence is included in the Danish merger control regime for the sole purpose of avoiding loss of valuable assets belonging to failing firms, if the sale of such assets does not harm competition. The purpose is not, however, to conduct interventionist policies to dampen the effects of economic crises.

2.6 Mergers between Financial Institutions

Do any special issues arise when the FFD is invoked in a merger between financial institutions (during a financial crisis)? If so, what are they and how should they be handled? What should be the relative weight attributed to competition and prudential objectives in the assessment of mergers between financial institutions?

Several mergers have been notified to the DCA in the wake of the ongoing economic crisis, and most of these cases have involved distressed companies primarily in the financial sector. As noted earlier the DCA has not yet based a decision in a merger case on a failing firm defence. In fact, all the mergers notified to the DCA in the wake of the crisis have been approved without remedies, since no significant impediments to competition were identified. That is not to say that the companies involved were not about to fail. On the contrary, some cases have involved financial institutions which could not meet the solvency requirements of the Danish Financial Services Authority. Consequently, for some of the merging companies it proved vital that the DCA was able to handle the merger cases more quickly than under normal non-crisis circumstances.

The issue of time span between notification and approval is important when it comes to the failing firm defence. Reaching a decision sooner rather than later may be very difficult, or even impossible, if that decision is to be based on a failing firm defence. This is due to the complex analyses required to evaluate the three conditions essential to the assessment of a failing firm defence, see paragraph 6. Reaching a decision quickly may be particularly important with merger cases involving distressed companies in the financial sector; as such companies are especially vulnerable to prolonged periods of uncertainty due to the risk of bank runs.

Finally, it is important to emphasise that it may be especially difficult to validate a failing firm defence, if the proposed merger involves companies in the financial sector. This is due to the third condition essential to the assessment of a failing firm defence which is that in the absence of a merger, the assets of the failing firm would inevitably exit the market. The assets of a financial company are made up, primarily, of a portfolio of debtors. The idea that an entire portfolio of debtors would inevitably exit the market appears to make little sense.

An alternative interpretation of the third condition is suggested in the EU Horizontal Merger Guidelines, *i.e.* that the market share of the failing company would in any event accrue to the other merging party, see footnote 111 of the Guidelines. However, even the alternative interpretation may be impossible to fulfil in the financial sector. This is due to the fact that debtors are; typically, free to transfer their engagements to any company which will accept them. Additionally, it cannot be ruled out that even failing financial companies may have in their portfolio a non-trivial amount of healthy assets, *i.e.* debtors who can repay their loans and would be accepted by most other financial companies. In conclusion, it may be relevant to ask: Is the failing firm defence unlikely to be inapplicable to mergers in the financial sector, because the third condition essential to the assessment of a failing firm defence cannot be validated, or should the third condition be interpreted differently for mergers in the financial sector?

2.7 *Interplay with other Policy Instruments*

How should a more lenient approach to FFD be articulated with other aspects of competition policy such as the review of agreements or the assessment of State Aids (where applicable)?

For the purpose of countervailing the effects of the ongoing or future economic crises it is the view of the DCA that a more lenient approach to the failing firm defence is not warranted. A more lenient approach to failing firm defence would (1) fail to address the fundamental issue, *i.e.* the economic crisis, (2) be inherently random, and (3) potentially lead to permanent anti-competitive effects reaching beyond the economic crisis. Instead the effects of economic crises should be addressed by more traditional policies such as the recent stimulus packages seen in many OECD countries.

FRANCE

Introduction

L'Autorité de la concurrence (ci-après l'« Autorité »), qui a succédé au Conseil de la concurrence (ci-après le « Conseil ») le 2 mars 2009 et est, depuis cette date, compétente pour appliquer les règles relatives au contrôle des concentrations¹ en France, est très attentive aux problèmes spécifiques aux entreprises en difficulté. Une annexe est consacrée à ce sujet dans les lignes directrices sur le contrôle des concentrations publiées depuis 2005².

Ainsi, la possibilité de demander une dérogation à l'interdiction de réaliser une opération avant l'accord de l'Autorité est ainsi régulièrement utilisée par les entreprises dans le cadre d'offres de reprise d'entreprises en difficulté déposées devant les tribunaux de commerce.³ Elle est rarement refusée, à la condition que la réalisation anticipée de l'opération ne préempte pas la décision de l'Autorité.

De la même façon, la pratique décisionnelle de l'Autorité s'inspire de la jurisprudence de la Cour de justice des Communautés européennes (arrêt « Kali et Salz » du 31 mars 1998⁴), selon laquelle en cas de reprise, par un concurrent, d'une entreprise en difficulté, l'opération peut être autorisée sans être assortie de prescriptions lorsqu'il apparaît que les effets de l'opération ne seraient pas plus défavorables que ceux qui résulteraient de la disparition de l'entreprise en difficulté.

Les trois critères cumulatifs définis par la Cour dans cet arrêt ont du reste été repris par le Conseil d'État, dans une décision du 6 février 2004.⁵ Il peut, selon la jurisprudence, être considéré que les effets d'une opération ne seraient pas plus dommageables pour la concurrence que la disparition de l'entreprise en difficulté lorsque :

- ces difficultés entraîneraient la disparition rapide de la société en l'absence de reprise,
- il n'existe pas d'autre offre de reprise moins dommageable pour la concurrence, portant sur la totalité ou une partie substantielle de l'entreprise,
- la disparition de la société en difficulté ne serait pas moins dommageable pour les consommateurs que la reprise projetée.

¹ Articles L. 430-1 à L. 430-10 issus de la loi sur les nouvelles régulations économiques du 15 mai 2001 et modifiés notamment par la loi de modernisation de l'économie du 4 août 2008.

² Ces lignes directrices publiées par la DGCCRF ont fait l'objet d'une actualisation au regard de la récente réforme du contrôle des concentrations en France (loi sur la modernisation de l'économie n°2008-776 du 4 août 2008). Une consultation publique sur ce projet a été lancée par l'Autorité de la concurrence le 9 juillet 2009.

³ Article L. 430-4 du code de commerce.

⁴ Arrêt de la CJCE du 31 mars 1998, « Kali et Salz », aff. 68/94 et 30/95, Rec. p. I-1375.

⁵ Arrêt du Conseil d'Etat du 6 février 2004 relatif à la concentration SEB / Moulinex (Société royal Philips Electronic et autres c/ Ministre de l'Economie), n° 249267.

L'exception de l'entreprise défaillante est cependant rarement invoquée par les entreprises notificantes – et n'est alors pas toujours admise par les autorités de contrôle. Dans l'affaire Seb-Moulinex citée ci-dessus, le Conseil d'État a considéré que la troisième condition n'était pas remplie. S'agissant de l'acquisition de plusieurs titres de presse par le groupe Ouest France,⁶ le Conseil a, de son côté, estimé qu'aucune des sociétés cibles n'apparaissait comme étant en cessation de paiement. En revanche, s'agissant de l'acquisition par la société Alliance Santé de la société ORP, deux répartiteurs pharmaceutiques, le Conseil a admis l'exception de l'entreprise défaillante à titre subsidiaire – l'opération n'étant, selon lui, en tout état de cause pas susceptible de porter atteinte à la concurrence.⁷

La présente note détaille la mise en œuvre des trois conditions ci-dessous dans la pratique décisionnelle et la jurisprudence françaises.

1. La disparition certaine de l'entreprise

A titre principal, ce critère est considéré comme satisfait que lorsque les sociétés cibles sont en cessation des paiements et font l'objet d'une procédure collective devant le tribunal de commerce. Dans l'affaire SEB/Moulinex,⁸ la cessation de paiement de la société et l'ouverture d'une procédure de redressement judiciaire avaient été prononcées par le tribunal de commerce de Nanterre, le 7 septembre 2001, et les deux administrateurs judiciaires chargés de dresser le bilan économique et social de l'entreprise, avaient écarté la faisabilité d'un plan de continuation au profit d'un plan de cession. On peut également noter que, dans cette affaire de dimension communautaire mais renvoyée partiellement à la France en application de l'article 9 du règlement n° 4064/89, applicable à l'époque, la Commission avait accordé le 27 septembre 2001 une dérogation à l'effet suspensif telle que prévue à l'article 7, paragraphe 4, du règlement n° 4064/89.

De la même façon, dans l'affaire ORP/ASD, la cible était en cessation de paiement.

Cependant, dans l'opération EBSCO/Rowecom France,⁹ bien que le tribunal de commerce ait prononcé la levée de la cessation des paiements de la cible, le ministre a considéré que le premier critère était bien rempli en raison de la dégradation de la situation financière de la cible postérieure à la décision du tribunal, et du fait que la maison mère de la cible était en faillite aux États Unis entraînant, en France, le retrait par certaines banques de crédits accordés à la cible et le refus de fournisseur de livrer les produits non payés.

Dans une affaire relative à la reprise par le groupe de presse Ouest France de trois titres de presse,¹⁰ dont l'un d'entre eux avait un compte d'exploitation négatif, mais dont aucun n'était en cessation de paiement ou ne faisait l'objet d'une procédure collective, la partie notificante soutenait que la défaillance devait être appréciée au regard des sociétés composant le pôle Ouest considérées ensemble, celles-ci constituant une seule entreprise au sens du droit de la concurrence et la cession séparée des titres étant une hypothèse économiquement irréaliste. Le Conseil a examiné *in concreto* le mode d'organisation des

⁶ Avis du Conseil de la concurrence n°05-A-18 du 11 octobre 2005 relatif à l'acquisition du Pôle Ouest de la société Socpresse et de fonds de commerce de la SEMIF par la société SIPA.

⁷ Avis du Conseil de la concurrence n°02-A-15.

⁸ Avis n°02-A-07 du 15 mai 2007, lettre du ministre de l'économie, des finances et de l'industrie du 5 juillet 2002 ; décision de la commission européenne n°COMP/M.2621.

⁹ Lettre du ministre de l'économie, des finances et de l'industrie du 25 avril 2003 aux conseils de la société EBSCO Industrie Inc. relative à une concentration dans le secteur des agences d'abonnements, C2003-45, BOCCRF n° 2003-13 du 28 octobre 2003.

¹⁰ Avis du Conseil de la concurrence n°05-A-18 du 11 octobre 2005.

entreprises concernées pour apprécier leur degré d'autonomie vis-à-vis l'une de l'autre et l'effet que pourrait avoir la défaillance de l'une sur les autres. Cet examen n'a cependant pas confirmé les affirmations de la partie notifiante et le Conseil a d'ailleurs constaté que la vente séparée de certains titres avait été envisagée. Il a donc considéré que la condition de la défaillance devait être appréciée au regard de chacune des entreprises prise isolément et que, en l'espèce, elle n'était pas remplie. Les difficultés des titres de presse (résultat d'exploitation déficitaire d'un des titres, obsolescence d'une partie de l'outil de production, irrégularité de la distribution) ont toutefois été notées par le Conseil et prises en compte dans le cadre de l'examen des gains d'efficacité susceptibles d'être apportés par l'opération.

2. L'absence d'offre alternative

Plusieurs questions sont susceptibles d'être posées lors de l'examen de cette condition. Premièrement, il faut que les repreneurs éventuellement intéressés aient eu connaissance de l'opportunité constituée par les difficultés de l'entreprise cible. De ce point de vue, les procédures collectives menées sous la juridiction des tribunaux de commerce garantissent une certaine publicité.

En deuxième lieu, une offre ne peut être considérée comme une alternative que si elle est crédible. Une offre déposée devant un tribunal de commerce dans les formes requises apparaît crédible, alors que de simples déclarations à la presse d'intérêt pour la reprise de l'entreprise en difficulté ne le sont pas.

En troisième lieu, se pose la question de la comparabilité des offres en ce qui concerne le champ des activités reprises, le prix, l'impact sur l'emploi, etc. A priori, les offres portant sur un champ plus restreint que celui de l'offre retenue ne sont pas considérées comme des alternatives.

Enfin, il pourrait être envisagé que l'impact de l'opération sur la concurrence soit pris en compte pour comparer et hiérarchiser les différentes offres, voire qu'une pesée soit effectuée entre des critères tels que ceux listés ci-dessus (champ des activités reprises, le prix, l'impact sur l'emploi, etc.) et l'impact sur la structure concurrentielle des marchés. Les autorités de concurrence ont, dans le cadre de ces affaires, souligné à plusieurs reprises la nécessaire coordination des procédures collectives avec le contrôle des concentrations.

Dans l'affaire Boiron / Dolisos¹¹ relative à une fusion dans le secteur des médicaments homéopathiques, le Conseil a considéré qu'il n'était pas possible de s'assurer que la deuxième condition était satisfaite, « *des possibilités de reprise par un opérateur tiers ne [pouvant] pas être exclues* ». Le Conseil a rappelé dans son avis qu'« en l'absence de procédure collective avec appel public à repreneur, il appartient aux parties de démontrer, par tout moyen, qu'il n'existait pas d'autre alternative d'achat des laboratoires Dolisos ». Les éléments fournis par les parties se sont cependant avérés insuffisants pour démontrer la satisfaction de cette condition. De plus, la société étrangère avait déclaré son intérêt à pénétrer le marché français, Dolisos constituant une cible d'acquisition possible. Enfin, il existait de nombreux concurrents étrangers susceptibles d'être intéressés, même s'ils ne s'étaient pas déclarés.

En revanche, s'agissant de l'opération Alliance Santé/ORP, précitée, le Conseil a considéré que des déclarations d'intérêt pour la reprise d'ORP, émanant respectivement d'un avocat pour le compte de clients non identifiés, des Editions Quo Vadis, représentant un fonds d'investissement, et de la société Phoenix Pharma qui a demandé communication des comptes « afin de préparer une offre », qui n'avaient été suivies d'aucune offre de reprise ou de continuation, ne constituaient pas des alternatives crédibles à l'offre d'Alliance Santé.

¹¹ Avis du Conseil de la concurrence n° 05-A-01 du 7 janvier 2005 relatif à l'acquisition de la société Laboratoires Dolisos par la société Boiron (point 140).

De même, dans l'affaire SEB/Moulinex précitée, aucune des autres offres déposées devant le tribunal de commerce n'a été considérée par le Conseil comme une alternative crédible à l'offre de SEB. D'une part, certaines d'entre elles ont été analysées comme de simples manifestations d'intérêt, ne pouvant être retenues, compte tenu des conditions posées par l'article L. 621-83 du code de commerce selon lequel la cession a pour but d'assurer le maintien d'activités susceptibles d'exploitation autonome, de tout ou partie des emplois qui y sont attachés, et d'apurer le passif. Or, les offres présentées par Philips, Electrolux, Arcelik, Babyliiss, Saeco, Sunbeam, Taurus, TTI, ne portaient que sur certains actifs du groupe sans reprise d'emplois ni apurement du passif. De surcroît, ces différentes propositions n'avaient pas évolué après leur dépôt, bien que les administrateurs judiciaires aient fait valoir leur non-conformité à l'article L. 621-83 du code de commerce et aient reporté à plusieurs reprises la date limite de dépôt des offres pour laisser aux candidats intéressés un délai suffisant pour modifier ou finaliser leurs offres de reprise. D'autre part, les offres de reprise totale ou partielle des actifs de Moulinex (Euroland et Société Participation industrielle) n'ont pas été considérées comme une solution substituable à celle de SEB, faute de garanties financières suffisantes pour justifier de leur faisabilité, et faute de levée, à la date de l'audience, des conditions suspensives dont elles étaient assorties.

De même, le Conseil a considéré que l'éventualité d'une reprise d'actifs dans l'hypothèse d'une liquidation judiciaire de Moulinex ne pouvait être envisagée avec suffisamment de certitude. Du fait de l'absence de matérialité et de sérieux des offres déposées devant le tribunal de commerce, il était loin d'être certain qu'elles auraient été renouvelées dans l'hypothèse d'une liquidation de Moulinex. En tout état de cause, les deux dernières offres qui comportaient un prix (Sunbeam, Conair) ne concernaient que la marque Krups qui n'occupait qu'une très faible position en France et ne concernait que le marché des « expresso ». Aucune de ces offres ne portait sur la marque Moulinex, ou sur un actif corporel du groupe. Une offre postérieure à la décision du tribunal de commerce de la société Conair/Babyliiss a été considérée comme non sérieuse, le Conseil en ne pouvant donc servir d'élément de comparaison dans l'analyse concurrentielle.

L'appréciation de l'autorité de concurrence dans cette affaire rejoint de fait celle du tribunal de commerce de Nanterre qui indiquait que [l'offre] *« présentée par la société Seb reste donc en réalité la seule subsistant (...). Que, si elle ne porte que sur une partie des sites, elle a le mérite de sauvegarder malgré tout plus du tiers des contrats de travail. »* Cette analyse avait été validée par la cour d'appel de Versailles.

Cependant, lorsqu'elle apprécie cette deuxième condition, l'autorité de contrôle des concentrations n'est pas liée par l'appréciation des offres concurrentes faite par le tribunal de commerce.

Le Conseil ajoutait par ailleurs que « le fait que les offres concurrentes n'étaient ni réelles, ni sérieuses, aurait empêché d'en apprécier l'impact sur le fonctionnement de la concurrence sur les marchés concernés, quand bien même ce critère d'analyse aurait été mis au premier plan par le tribunal de commerce ».

Les préoccupations de concurrence ne sont donc pas absentes dans l'appréciation par l'autorité de concurrence de cette deuxième condition tenant à l'absence d'alternatives. Néanmoins, aucun des cas examinés n'a donné lieu, à ce stade de l'analyse, à une comparaison des mérites respectifs des différents repreneurs potentiels du point de vue de l'effet sur l'opération sur la concurrence.

3. Neutralité pour les consommateurs

La vérification de cette condition demande en principe une analyse prospective sur ce que deviendrait la situation concurrentielle des marchés concernés dans l'hypothèse de la disparition de l'entreprise concernée. Dans les faits, cette vérification recoupe en grande partie l'analyse concurrentielle à laquelle il a

été procédé, dans un premier temps, afin d'examiner si l'opération est de nature à porter atteinte à la concurrence. Les autorités de contrôle doivent donc veiller à la cohérence des deux analyses. Le Conseil d'État a ainsi, dans une décision du 6 février 2004, annulé l'autorisation donnée à la réalisation de l'acquisition de certains actifs de la société Moulinex par la société SEB, certains arguments avancés dans la décision pour démontrer que la disparition de l'entreprise emporterait des conséquences au moins aussi dommageables pour la concurrence que l'opération étant contradictoires par rapport à ceux qui démontraient, dans un premier temps, que l'opération portait atteinte à la concurrence.

Dans cette affaire, le Conseil de la concurrence avait, dans l'avis rendu au ministre, considéré que l'arrêt brutal de l'activité industrielle et commerciale de Moulinex, à la suite des difficultés de cette entreprise, pendant les quelques mois précédant sa reprise, pouvait être assimilé à une simulation des effets d'une disparition pure et simple des moyens de production de l'entreprise ainsi que de la marque. Or, le transfert des parts de marché constaté sur cette période entre Moulinex et SEB laissait penser que, en cas de retrait du marché des produits Moulinex, les parts de marché détenues par le groupe SEB n'auraient pas été très différentes de celles résultant de l'opération.

Cette approche reprend celle de la jurisprudence communautaire pour considérer que la concentration n'est pas la cause du renforcement des parts de marché de l'entreprise qui a acquis l'entreprise en difficulté et que l'opération est donc neutre quant à son impact sur la concurrence. S'agissant des transferts de parts de marché, la Cour a en effet considéré que : *« En fait, l'introduction de ce critère vise à assurer que l'existence d'un lien de causalité entre la concentration et la détérioration de la structure concurrentielle du marché ne peut être exclue qu'au cas où la détérioration de la structure concurrentielle du marché, faisant suite à l'opération de concentration, se produirait pareillement même en l'absence de cette opération. Dès lors, le critère de l'absorption des parts de marché, bien qu'il ne soit pas considéré par la Commission elle-même comme suffisant à lui seul pour exclure le caractère préjudiciable de l'opération de concentration pour le jeu de la concurrence, concourt à assurer la neutralité de cette opération par rapport à la dégradation de la structure concurrentielle du marché, ce qui est conforme à la notion de causalité figurant à l'article 2, paragraphe 2, du règlement. »*¹²

La décision du ministre a retenu une autre approche, à savoir que, du fait de l'existence de fabricants concurrents du repreneur et de la cible, le report de marché n'avait pas été total, les concurrents ayant récupéré une partie des ventes perdues du fait de l'arrêt de l'activité de Moulinex. Elle a donc recherché si d'autres éléments permettaient de conclure que l'opération n'auraient pas été plus dommageable pour la concurrence que la disparition pure et simple de Moulinex et a noté que l'absence de reprise de Moulinex entraînerait très certainement une détérioration importante des conditions de fonctionnement de plusieurs marchés du petit électroménager, au détriment des consommateurs (une raréfaction de l'offre de nature à favoriser une offre des prix, problèmes de service après-vente).

Le Conseil d'État a cependant jugé qu'en évaluant les effets de la disparition de Moulinex sur l'offre globale de produits dans le secteur du petit électroménager, le ministre de l'économie avait omis de prendre en compte l'existence de capacités disponibles chez les concurrents et leurs sous-traitants. Il a de plus relevé que cette analyse s'appuyait largement sur l'argument selon laquelle la marque Moulinex disparaîtrait, faute d'offres de reprise crédible, alors que l'importance des marques sur ce marché, et particulièrement de la marque Moulinex, avait par ailleurs été mis en avant par le ministre dans l'analyse concurrentielle. Il a donc annulé la décision en jugeant que les motifs invoqués par ce dernier ne suffisaient pas à justifier qu'était remplie la troisième des conditions exigées pour le recours à l'exception de l'entreprise défaillante. Il ressort donc de cet arrêt que l'autorité de contrôle ne doit pas se limiter à envisager la disparition complète de l'entreprise en difficulté mais doit aussi établir un scénario prospectif

¹²

Arrêt Kali et Salz, précité.

dans lequel seuls certains actifs de l'entreprise seraient repris par d'autres repreneurs que celui notifiant l'opération.

Dans la seconde décision du ministre,¹³ l'exception de l'entreprise défaillante n'a plus été évoquée, l'analyse du marché faite par le Conseil de la concurrence deux ans après la reprise de Moulinex par SEB ayant démontré que la part des ventes de Moulinex récupérée par les concurrents à la suite de l'opération était comparable à celle qu'ils détenaient sur le marché avant l'opération. Il a donc été conclu que l'opération considérée n'était pas de nature à porter atteinte à la concurrence.

Dans l'affaire Alliance Santé Distribution (ASD) / Ouest Répartition Pharmaceutique (ORP),¹⁴ deux entreprises actives sur le marché de la répartition pharmaceutique, a également été conduite une analyse du critère de « *neutralité sur la concurrence* », mettant en balance, en termes de conséquences sur la concurrence, la concentration et la disparition d'ORP. Les risques d'atteinte à la concurrence étaient liés au caractère oligopolistique du marché, dominé par trois grands répartiteurs, dont Alliance Santé, et à la spécificité de la cible, qui pratiquait des prix plus bas pour une offre moins étendue. Le Ministre soulignait que, de ce fait, « *ORP, adossé à ASD, avec des moyens financiers importants, pourrait être utilisé pour déstabiliser les petits opérateurs du marché et les en évincer en quelques mois, compte tenu, ainsi que l'a relevé le Conseil, de l'impact très sensible d'une perte même limitée de clientèle, s'agissant de structures caractérisées par des coûts fixes importants* ». Il a cependant considéré que, « *même en l'absence de l'opération, une telle stratégie d'éviction des petits opérateurs pourrait être mise en place par les membres de l'oligopole, qui pourraient aisément créer un short-liner ciblant son activité dans les zones où les petits opérateurs sont actifs* ».

4. Conclusion

La crise économique de 2008 a entraîné une baisse des notifications reçues par l'autorité de contrôle des concentrations. L'Autorité de la concurrence n'a toutefois pas constaté, depuis sa création en mars 2009, un recours plus important par les entreprises à l'argument de l'entreprise défaillante en défense des opérations. Un certain nombre d'opérations ont pourtant été notifiées dans le cadre de procédures collectives de mise en redressement ou en liquidation d'entreprises mais la position concurrentielle des entreprises concernées sur les marchés n'était pas de nature à faire naître des préoccupations de concurrence.

En conséquence, les questions qui ont été débattues depuis le début de la crise, relatives à un éventuel assouplissement des conditions dans lesquelles les autorités de concurrence acceptent l'exception de l'entreprise défaillante, n'ont pour le moment pas trouvé de champ d'application concret. Cependant, on peut rappeler que même si l'objectif poursuivi par les autorités de contrôle avec l'exception de l'entreprise défaillante est de ne pas décourager le sauvetage d'entreprises en difficulté, et notamment des emplois concernés, au nom d'effets sur la structure concurrentielle des marchés qui résultent en fait des difficultés de l'entreprise, pour autant, l'analyse reste assise sur des critères de concurrence sur les marchés. L'Autorité de la concurrence reste soucieuse de ne pas leur substituer des critères autres, tels que la défense de l'emploi ou la compétitivité des entreprises nationales, au risque d'autoriser des opérations qui auraient des effets dommageables et durables sur la structure concurrentielle des marchés.

¹³ Lettre du ministre d'État, ministre de l'économie, des finances et de l'industrie, en date du 16 août 2004, aux conseils de la société Seb, relative à une concentration dans le secteur de la fabrication et de la vente de petit électroménager, BOCCRF n° 2005-01 du 25 janvier 2005.

¹⁴ Lettre du ministre de l'économie, des finances et de l'industrie du 20 janvier 2003, au conseil de la société Alliance Santé Distribution, relative à une concentration dans le secteur des grossistes répartiteurs pharmaceutiques, C2002-21.

GERMANY

1. Introduction

The OECD Competition Committee debated the failing firm defence in merger review in May 1995.¹ The following submission seeks to further contribute to the discussion, building on the German submission from 1995.²

The main goal of German merger control is to safeguard the competitive structure of markets against the potential anticompetitive effects of mergers. Consequently, according to Section 36 (1) of the German Act against Restraints of Competition (*Gesetz gegen Wettbewerbsbeschränkungen*; hereinafter: ARC), any merger that creates or strengthens a dominant position has to be prohibited by the *Bundeskartellamt*. An exception to this rule applies if one party to the transaction is a struggling company that will likely fail in the imminent future. However, the failing firm defence (*Sanierungsfusion*), as this exception is called, has very stringent requirements.

In German competition enforcement practice, the failing firm defence has predominantly been invoked in times of economic crisis. This holds true in particular for the period following German unification (early 1990s).³ Since then the failing firm defence has only rarely been invoked and – even more rarely – granted.⁴ However, it has recently gained attention and practical relevance in enforcement practice.⁵

This submission seeks – from a German perspective – to contribute to the clarification of the requirements of the failing firm defence.

2. Statutory Provisions and Relevant Enforcement practice

The German competition act ARC does not contain any specific provisions regarding the failing firm defence. The German legislature has deliberately decided not to introduce such provisions.⁶ In a competition-based market economy, the market exit risk is a basic feature of the market process. Consequently, from a competition point of view, the market exit of any company is not to be seen in a

¹ See OECD, Failing Firm Defence, Paris, 2006, Doc. OCDE/GD(96)23.

² *Ibid.*, page 55/56.

³ See for example BKartA, Tätigkeitsbericht 1989/1990, page 113 – *Lufthansa/Interflug* (merger clearance denied); BKartA WuW 1992, 317 – *Schott Glaswerke/Fernsehglass Tschernitz* (merger clearance granted based on failing firm defence); BKartA WuW 1992, 496 – *Vereinigte Schmiedewerke/Radsatzfabrik Ilseburg* (merger clearance granted based on failing firm defence); BKartA WuW 1992, 606 – *Suhler Verlagsgesellschaft / Südthüringer Verlag* (merger clearance granted based on failing firm defence).

⁴ Cases, in which merger clearance was granted based on the failing firm defence include, for example, BKartA, Tätigkeitsbericht 1997/1998, page 88/89 – *DuMont Schauberg/Kölnische Rundschau*; BKartA WuW/E DE-V 848 – *Imation/EMTEC* (2003) and BKartA WuW/E DE-V 1226 – *RTL/n-tv* (2006).

⁵ See, for example, BKartA B6 – 67/09 (*Eberbacher Zeitung/Rhein-Neckar-Zeitung*) (not published; German case summary available at <http://www.bundeskartellamt.de/wDeutsch/download/pdf/Fusion/Fusion09/Kurzberichte/B6-67-09-Fallbeschreibung.pdf?navid=47>).

⁶ See the official rationale for the relevant laws (Begr. RegE 2. GWB-Novelle, BT-Drucks. VI/2520, page 29); see also *Schmidt*, Die Sanierungsfusion im Zielkonflikt zwischen Unternehmenserhaltung und Wettbewerbssicherung, in: Die Aktiengesellschaft, 1982, page 169 (170).

more unfavourable light than a takeover. Mergers where at least one of the undertakings involved would otherwise exit the market are therefore subject to the same legal provisions as all other mergers. In spite of the fact that they need to be dealt with speedily, the general procedural and material requirements apply to them as to all other merger cases.

According to Section 36 (1) ARC, any merger that creates or strengthens a dominant position has to be prohibited by the *Bundeskartellamt*. However, the prerequisites for a prohibition are only met if the dominant position is created or strengthened explicitly through the merger. In other words, there has to be a causal link (*Kausalität*) between the merger and the creation or strengthening of the dominant position. In failing firm scenarios, this causal link might be missing, as the competitive situation in the market absent the proposed merger – in case of the insolvency and/or market exit of the failing firm (*i.e.* the relevant “counterfactual”) – may not differ from the competitive situation following the merger. Against this background, the failing firm defence can generally be dealt with as a case of missing causality. The relevant prerequisites have been shaped by past enforcement practice and are explained in more detail below.

The failing firm defence can principally also be dealt with under the balancing clause (*Abwägungsklausel*) of Section 36 (1) clause 2 ARC and under the provisions for a ministerial authorisation (*Ministererlaubnis*), Section 42 ARC. However, for reasons explained in more detail below, both the balancing clause and the ministerial authorisation have – at least for the last 20 years – not played a significant role in the evaluation of failing firm cases. Consequently, the subsequent analysis will focus primarily on the “causal link criterion”.

2.1 Causal Link (*Kausalität*)

The prerequisites for the failing firm defence have taken shape during the past enforcement practice of the *Bundeskartellamt*.⁷ They were also laid down in the “Principles of Interpretation of Market Dominance in German Merger Control” issued by the *Bundeskartellamt* in 2005 (*Auslegungsgrundsätze zur Prüfung von Marktbeherrschung in der deutschen Fusionskontrolle*; hereinafter: Interpretation Principles).⁸ According to the prerequisites, a merger that invokes the failing firm defence can be cleared, if the following conditions are cumulatively met:

- a) One of the merging parties would – absent the merger – likely fail in the imminent future;
- b) There is no alternative merger to the proposed merger between the failing and the acquiring firm; and
- c) It is to be expected that the market shares of the failing firm would fully accrue to the acquiring firm even absent the proposed merger (*i.e.* in case of a market exit by the failing firm).

The burden of proof regarding the fulfilment of all these prerequisites rests with the merging entities.⁹ The *Bundeskartellamt* sets the level of proof to be provided by the merging entities quite high. It has in

⁷ Recent enforcement practice that has taken up the following prerequisites includes, for example, BKartA WuW/E DE-V 695 (704/705) – *Tagesspiegel/Berliner Zeitung* (2002); BKartA WuW/E DE-V 777 (784) – *Ajinomoto/Orsan* (2003); BKartA WuW/E DE-V 848 (852) – *Imation/EMTEC* (2003); BKartA WuW/E DE-V 1087 (1102/1103) – *Rhön/Grabfeld* (2005); BKartA WuW/E DE-V 1226 (1233) – *RTL/n-tv* (2006); BKartA WuW/E DE-V 1407 (1421/1422) – *LBK Hamburg/Mariahilf* (2007).

⁸ Please note that the Interpretation Principles are currently under review and have been taken from the *Bundeskartellamt*’s homepage.

⁹ However, the *Bundeskartellamt* has in some cases – without any legal obligation to do so – initiated research on its own (see, *e.g.* BKartA DE-V 1407 (1421) – *LBK Hamburg/Mariahilf* (2007)).

particular emphasised that a mere assertion about the fulfilment of the prerequisites was not sufficient. Instead, it has pointed out that all prerequisites have to be proven with “appropriate documents”.

Regarding prerequisite (a), appropriate documents may in particular include accounting documents (e.g. annual reports).¹⁰ In assessing whether these documents sufficiently prove that one of the merging parties would – absent the merger – likely fail in the imminent future, the *Bundeskartellamt* has in the past not established general evaluative criteria. In contrast, it has put emphasis on the specific circumstances of each individual case. Recently, it has held in an individual case that it was sufficient, if the documents showed that the failing company had for more than 10 years almost consistently incurred a deficit and that there were no serious prospects of reorganisation.¹¹

As far as prerequisite (b) is concerned, the merging parties have to provide evidence that the failing firm has unsuccessfully sought out alternative – and less anticompetitive – purchasers.¹²

Although it was often difficult enough in the past for the merging parties to demonstrate that the prerequisites set out under (a) and (b) were met, even more problems can arise with regard to prerequisite (c). The reason is that the “causal link criterion” generally requires that the market shares of the failing firm would *fully* accrue to the acquiring firm absent the merger.

As long as the only two competitors in a given market merge, the *Bundeskartellamt* has so far regularly assumed that the criterion was fulfilled.¹³ However, if there are more than two market participants, this cannot be easily assumed because it is likely that some of the market shares of the failing company will also fall to the other market participants.¹⁴ In such cases, other evaluative criteria – like the effect the market exit of the failing firm has on the market structure – could be taken into account. This approach has in particular been favoured by the Monopolies Commission (*Monopolkommission*).¹⁵ The *Bundeskartellamt* has so far not had to explicitly decide this question in its enforcement practice.

As far as the so-called “failing division defence” is concerned, the *Bundeskartellamt* has stated in its Interpretation Principles that it would recognise this defence neither for “failing divisions” nor for “failing affiliates”.¹⁶ However, it has so far not had to explicitly decide this question in its enforcement practice.

2.2 *Balancing Clause (Abwägungsklausel)*

Under the balancing clause, a merger that would lead to the creation or strengthening of a dominant position can be cleared if the undertakings concerned demonstrate that it would lead to improvements on third markets that more than outbalanced (*überwiegen*) the disadvantages of market dominance. This

¹⁰ See, for example, BKartA DE-V 1226 (1234)– *RTL/n-tv* (2006).

¹¹ BKartA WuW/E DE-V 1226 (1234) – *RTL/n-tv* (2006).

¹² See, for example, BKartA, Tätigkeitsbericht 1997/1998, p. 87 (89) – *DuMont Schauberg/Kölnische Rundschau*; BKartA DE-V 1407 (1421) – *LBH Hamburg/Mariahilf* (2007).

¹³ See, for example, BKartA WuW/E DE-V 848 (852) – *Imation/EMTEC* (2003) and the Interpretation Principles (please note that the Interpretation Principles are currently under review).

¹⁴ See, for example, Federal Court of Justice (*Bundesgerichtshof*) WuW/E BGH 1655 (1660) – *Zementmahanlagen II* (1979) and Higher Regional Court of Dusseldorf (*OLG Düsseldorf*) VI-Kart 6/05(V) – *Rhön/Grabfeld* (2007), para. 141.

¹⁵ See *Monopolkommission*, Sondergutachten 42, Die Pressefusionskontrolle in der Siebten GWB-Novelle, para. 140. The Monopolies Commission is an independent, evaluative and advisory body assessing the development of competition law in Germany (see <http://www.monopolkommission.de/>).

¹⁶ Please note that the Interpretation Principles are currently under review.

clause can generally also be applied to failing firm scenarios.¹⁷ The relevant companies would then in particular have to demonstrate that the rescue merger would lead to improvements on third markets that more than outbalanced the disadvantages of market dominance. Given that the improvements must generally be demonstrated on *third* markets, the hurdles for merger clearance based on the balancing clause remain relatively high.¹⁸ Nevertheless, there have in the past been failing firm cases, in which merger clearance was granted based on the balancing clause.¹⁹ Recently, however, there have been no such cases.²⁰

2.3 Ministerial Authorisation (*Ministererlaubnis*)

Under the provisions for a ministerial authorisation, the Federal Minister of Economics and Technology can authorise a merger prohibited by the *Bundeskartellamt* if the restraints of competition resulting from it are outweighed (*aufwiegen*) by advantages to the economy as a whole or if the concentration is justified by an overriding public interest. Generally, a ministerial authorisation can also be applied for in failing firm cases. The merging parties would then have to demonstrate that the rescue merger would lead to advantages to the economy as a whole that outweighed the restraints of competition or that the merger would be justified by an overriding public interest.

In the few cases, in which the failing firm defence was brought, the provisions for a ministerial authorisation have been applied very restrictively.²¹ Nevertheless, as is the case with the balancing clause, there have been failing firm cases in which (partial) merger clearance was granted based on a ministerial authorisation.²² It needs to be emphasised, though, that the relevant companies could in all these cases demonstrate that the proposed merger would lead to additional advantages to the economy as a whole that outweighed the restraints of competition resulting from it or that the concentration was justified by an overriding public interest. Recently, there have been no failing firm cases in which a ministerial authorisation was applied for.

As far as the failing division defence is concerned, the Federal Minister of Economics and Technology has emphasised that it was primarily the duty of the parent company to support the failing division in any economically reasonable way.²³ However, specific criteria that could be used in determining whether the potential support was economically reasonable or not, have not yet been devised. Given the fact that the Interpretation Principles²⁴ do not recognise the failing division defence,²⁵ no such criteria have emerged during the enforcement practice of the *Bundeskartellamt*.

¹⁷ See, for example, OLG Düsseldorf VI-Kart 6/05(V) – *Rhön/Grabfeld*, para. 140/141 and *Emmerich*, Fusionskontrolle 2005/2006, in: *Die Aktiengesellschaft* 2006, page 861 (870).

¹⁸ Regarding this prerequisite, see for example, BKartA, WuW/E DE-V 1407 (1423) – *LBK Hamburg/Mariahilf* (2008) and OLG Düsseldorf VI-Kart 6/05 (V) – *Rhön/Grabfeld*, para. 141.

¹⁹ See for example BKartA, Tätigkeitsbericht 1976, page 79 – *Karstadt/Neckermann*.

²⁰ For a recent (non-failing firm) case that deals with the balancing clause see BKartA B7-200/07 – *KDG/Orion* (available at <http://www.bundeskartellamt.de/wDeutsch/download/pdf/Fusion/Fusion08/B7-200-07.pdf>).

²¹ See, for example, WuW/E BW 177 (180) – *IBH/WiBau* and WuW/E BW 159 (162) – *Thyssen-Hüller*.

²² WuW/E BW 155 (157) – *Babcock/Artos* (1976; ministerial authorisation granted subject to obligations); WuW/E BW 159 (162) – *Thyssen/Hüller* (1977; ministerial authorisation partially granted); WuW/E BW 177 – *IBH/WiBau* (1981; ministerial authorisation granted).

²³ WuW/E BW 177 (181) – *IBH/WiBau* (1981). See also WuW/E BW 165 (173) – *Veba/BP* (1979).

²⁴ Please note that the Interpretation Principles are currently under review.

²⁵ See above, section 2.1.

3. Conclusion

The failing firm defence (*Sanierungsfusion*) has in the past been an important enforcement tool for the *Bundeskartellamt*, especially in times of economic crisis. The *Bundeskartellamt* has thereby generally dealt with it as an issue of causality (*Kausalität*). In other words, it has recognised the failing firm defence particularly in those cases where the competitive effects of the proposed merger would equal the competitive situation absent the merger (*i.e.* in case of a market exit by the failing firm). However, there are stringent prerequisites for this criterion to be fulfilled. These prerequisites have emerged during the past enforcement practice of the *Bundeskartellamt* and were also laid down in the Interpretation Principles issued in the year 2005.²⁶

²⁶

Please note that the Interpretation Principles are currently under review.

IRELAND

Introduction

This is the written submission from the Irish Competition Authority (“the Authority”) to the October 2009 OECD Roundtable on the Failing Firm Defence (“FFD”). The submission considers the discussion questions and issues contained in the letter by the OECD Secretariat dated 16 July 2009.

1. Definition of the FFD - How is the failing firm defence defined in your jurisdiction? Please refer to your jurisdiction’s applicable court decisions, statutes, or competition agency guidelines. In particular, what criteria need to be met and what elements of proof are required in your jurisdiction to invoke the FFD successfully?

The FFD is set in the context of the substantial lessening of competition test (the “SLC test”), which is the substantive test applied to mergers by the Authority.¹ The application of the SLC test is set out in the Authority’s *Notice in Respect of Guidelines for Merger Analysis* (the “Merger Guidelines”)² rather than in the Competition Act 2002 (the “Act”).

The SLC test is interpreted in terms of consumer welfare. Consumer welfare depends on a range of variables including price, output, quality, variety and innovation. In most cases, the effect on consumer welfare is measured by whether the price in the market will rise. The conclusion that an SLC will result from a merger is thus based on whether the price to buyers is expected to rise (or output to fall). Where price is not the appropriate variable, welfare is measured by the changes in the relevant variables.

For an overview of the substantive test and its building blocks in analysing horizontal mergers, the reader can refer to the Authority’s submission to the June 2009 OECD WP3 Roundtable on the standard for merger review.³

Currently, Part 3 of the Act applies to mergers and acquisitions in all sectors, with special provisions applying to media mergers.⁴ However, in October 2008, the Credit Institutions (Financial Support) Act

¹ Under section 21 of the Competition Act 2002 (the “Act”), the Authority has to determine within one month after the notification of the transaction whether, in its opinion, a merger or acquisition will not be to substantially lessen competition in any market for goods or services in Ireland and, accordingly, whether a merger or acquisition may be put into effect or that it intends to carry out a full investigation. In sum, if the Authority cannot clear a merger during the preliminary investigation, it must carry out a full investigation under section 22. Under section 22 of the Act, on the completion of a full investigation the Authority shall determine whether the merger or acquisition may be put into effect (with or without conditions) or not.

² The Authority’s *Notice in Respect of Guidelines for Merger Analysis*, December 2002, is available at: <http://www.tca.ie/MergersAcquisitions/MergersAcquisitions.aspx>.

³ Working Party No. 3 on Co-operation and Enforcement, Roundtable on “The standard for merger review, with a particular emphasis on country experience with the change of merger review standard from the dominance test to the SLC/SIEC test”, Ireland, 9 June 2009.

⁴ The Act allows for the possibility that a media merger cleared by the Authority on competition grounds after a full investigation may still be prevented from being put into effect by the Minister on public interest grounds. These essentially relate to media diversity and plurality, the strength and competitiveness of

2008 (the “Credit Institutions Act”) was enacted which modifies certain provisions of the Act. The Credit Institutions Act allows the Minister of Finance to take jurisdiction over a merger or acquisition involving banks that he determines is required in order to ensure the stability of the Irish financial system.⁵

In light of the fact that the Act is expected to be amended as part of the government’s review of the Act⁶ and given its experience in applying the SLC test to over 400 merger notifications under the Act, the Authority intends to publish a new set of Merger Guidelines. Since it is unlikely that the Act will require a change of the substantive SLC test, the general thrust of any new guidelines can be expected to remain the same. This is likely to be true also for the section devoted to the FFD.

Paragraph 5.17 of the Merger Guidelines is devoted to the FFD. It states that:

“A merger may not substantially lessen competition in a market if part or all of the merging assets are certain to exit the market in the event of the merger not taking place. The incentives for a firm to exaggerate the extent of its weakness are recognised, and accordingly, in order to consider this “failing firm” defence, very strict criteria must be clearly demonstrated:

(a) The alleged failing firm must be unable to meet its financial obligations in the near future;

(b) No possibility exists that the firm will be successfully reorganised under the process of Examinership;

(c) The firm has made good-faith and verifiable efforts to elicit reasonable alternative offers of acquisition that would keep its assets, both tangible and intangible, in the relevant market and be less of a threat to competition than the proposed merger. It must be shown that such efforts have resulted in the firms being unable to sell for a price in excess of the liquidation value of its assets; and

(d) Without the merger taking place, the assets of the failing firm would definitely exit the relevant market.

Such conditions may rarely be met in practice.”

Normally, assets that are not economically viable would not be expected to remain in the market. The requirements of the failing firm defence are designed to identify those limited circumstances in which the firm’s assets would exit the market but for the proposed acquisition. In such cases, the acquisition of a failing firm’s assets is likely to cause its assets to become economically viable and thus remain in the market if it generates significant efficiencies. In these circumstances, the counterfactual - with which the

media businesses indigenous to the State and the dispersion of media ownership amongst individuals and other undertakings.

⁵ See response to Question 6. See also Ireland’s Submission to 2009 February OECD Roundtable on Competition and Financial Markets.

⁶ On 13 November 2007, the Minister announced a public consultation on the Act. On 14 October 2008, the Minister for Finance announced in the 2009 budget that the Competition Authority would be amalgamated with the National Consumer Agency. Therefore the review of the Act is now part of the wider process of introducing legislation that would incorporate both consumer and competition protection functions. At the time of writing this submission, the new Act is still being drafted but no changes to the legal test have been envisaged so far.

post-merger situation should be compared – would need to reflect the expected failure of one of the parties and any resulting loss of rivalry.

There is no definition of a “failing firm” in the Merger Guidelines, nor in statute or court decisions in Ireland. Generally speaking, a firm in liquidation could be considered to a failing firm.⁷ To date, the FFD has been invoked by merging parties only in one case out of over 400 merger notifications under the Act. However, the FFD was never tested in that case.⁸

In the course of 2008 and 2009, the Authority reviewed a number of mergers directly associated with the financial and economic crisis.⁹ In those cases, the Authority showed a flexible approach in the application of its merger review procedure to accommodate the specific circumstances of each individual case by expediting the review process. For example, the acquisition by HMV Ireland of Zavvi stores was cleared in 9 days only. The Authority granted HMV Ireland a request to shorten the period for third party comments (from 10 to 5 days) in light of the circumstances of the particular case. The Authority, among other things, considered that: (i) the company was in liquidation; (ii) the provisional liquidator had agreed to provisionally run the retail business of the Zavvi stores, pending clearance by the Authority; and, (iii) that the proposed transaction did not raise competition concerns.¹⁰

None of the deals associated with the economic and financial crisis raised substantive competition issues. The majority involved the acquisition of assets or businesses that were already in liquidation but did not raise any competition concerns. Despite the financial and economic context, typical issues of the FFD like the choice of less anticompetitive alternative buyers did not arise. Therefore, the Authority was able to clear each on the basis of a standard-form SLC test without reference to the FFD.

⁷ Under Irish law, the liquidation or winding-up of a company, in other words, its legal death can take one of two forms. It can be a winding-up by order of the court (also known as an official liquidation). Far more frequently, however, it will be a voluntary winding-up (which, in turn, may be either a members' voluntary winding-up, or a creditor's voluntary winding-up). In a creditors' voluntary liquidation, the liquidator is primarily concerned with the interests of the creditors while the main purpose of a members' voluntary liquidation is selling the company's assets and distributing the surplus to its shareholders. To be distinguished from the examinership and liquidation process is the receivership, which is not usually initiated by the company itself, but rather by its creditors. It normally arises when the company has defaulted on a contract to repay loans or debts outstanding. The receiver's primary role is to recover the money owing to the creditor and, in theory, the company can continue trading while in receivership. However, in order to recover the creditor's money the receiver may have to sell off assets to the point that the company can no longer continue to operate. In those circumstances, the company is likely to end up in liquidation.

⁸ In the merger case Smart Telecom / E-nvi, the acquired firm E-nvi was in provisional liquidation at the time of the notification of the transaction. Four days later, the company went into liquidation following a meeting of the creditors at which a liquidator was appointed. The parties, as part of the submission, also put forward a failing firm argument in accordance with the Authority's Merger Guidelines. Given the lack of competition concerns as a result of the proposed transaction the Authority did not consider in detail the merits of the arguments put forward for the failing firm argument.

⁹ In 2008: M/08/012 – JP Morgan/Bear Stearns; M/08/005 - Collins Stewart/ ISTC; and Lloyds TSB/HBOS. In 2009: M/09/002 - HMV Ireland Zavvi; M/09/006 – Mubadala/SR Technics; and M/09/014 - Noonan Services / Federal Security Group.

¹⁰ Interestingly, the acquisition of Zavvi stores by the HMV group was also assessed in UK by the OFT. In that case, the acquirer put forward a FFD claims.

- 2. Type and Quantum of Evidence - How can the elements you identify in response to the previous question be established? For example,**
 - 2.1 *What kind of evidence – and how much of it – is necessary to satisfy a court or an agency that a firm is actually ‘failing’?***
 - 2.2 *What counterfactual scenarios should be examined: should the only alternative to be examined be the one of exit from the market or should it encompass a loss of competitive constraint on the part of the target (for example, poor enough performance so as to prevent outside financing at affordable rates), other possible transactions, etc.***
 - 2.3 *What should be the depth of the analysis to gauge the potential impact on competition of each of the alternative scenarios? Under what circumstances should an enforcement agency or court be satisfied that an otherwise anticompetitive merger is the best known alternative?***
 - 2.4 *Failing Divisions. What should be done when the failing “firm” is a division of a larger, viable company? In other words, should a “failing division” defence be allowed? If so, why? What kind of evidence should be required to establish it?***

Questions 2.1 and 2.3 are not applicable since the FFD has never been tested as noted in paragraph 9 above.

In relation to question 2.2, the Authority considers that all the possible counterfactual scenarios should be considered *prima facie*. However, the Authority is mindful that it might not be feasible to analyse in depth all the counterfactual scenarios. Thus, the Authority’s limited resources will be focused on those counterfactual scenarios that appear to be the most likely based on information in the possession of the Authority.

In relation to “Failing Divisions” of question 2.4 above, the Authority does not exclude the possibility that the same criteria of the FFD would apply, though the Merger Guidelines is silent on this. However, in assessing a failing division claim, the Authority would carefully consider the ability of the parent company to manipulate its books in a manner that may create the appearance of a failing division when the division is not in fact failing.

- 3. Harmonisation and evolution - Are you aware of approaches to the FFD that are different from the one used in your jurisdiction? If so, is the approach in your jurisdiction better? Why? Would it be sensible to try to harmonise the approach to the FFD across jurisdictions? Has your own approach to the FFD evolved over the years and if yes, how and why?**

The Authority considers that the criteria for assessing FFD as set out in the Merger Guidelines are consistent with those in the *ICN Merger Guidelines Workbook* of the International Competition Network.

4. Market context

- 4.1 *Declining Industry. Should it matter to the analysis that the failing firm is part of a declining industry?*
- 4.2 *Nature of competitive interaction. Should the type of competition in the market(s) affected by the transaction matter in the assessment of the FFD? In particular, should court and agencies be more lenient when firms compete for the market through investment and innovation?*
- 4.3 *Small economy. What role, if any, does the size/extent of the local market play in the evaluation, as opposed to the size of any trans-border or global market? What role, if any, does the industry's importance to the local economy play when assessing an FFD defence?*
- 4.4 *Capital markets. Should the assessment of the FFD take into account possible limitations in the availability of external funds (debt and equity) resulting from the particular characteristics of the industry in which the merging parties operate or more general macroeconomic conditions?*

The Authority would carefully assess any FFD claims submitted by the merging parties. In particular, the Authority would assess the implications of the imminent exit of one of the merging parties within the context of the appropriate counterfactual. An appropriate definition of the counterfactual is important given that it will provide the benchmark to assess the competitive effects of the merger.

In relation to question 4a the Authority would consider the implications of a declining industry insomuch as it affects its forward looking analysis of the counterfactual scenario and the post-merger situation.

In relation to question 4b the Authority considers that the type of competition in the market(s) affected by the transaction does not affect the analytical framework of the FFD but may impact on the outcome of the assessment of FFD. The Authority considers that the FFD requirements apply to any type of competition, whether or not innovation and investment are the key drivers.

In relation to question 4c the Authority considers that the size of the Irish economy should not have any influence on competition policy, its objectives, analytical framework and practice¹¹ to the assessment of FFD.

In relation to question 4d the Authority considers factors such as the overall macroeconomic conditions (for example, whether economy is overall in a recession) and capital markets (for example, whether there is unavailability of credit and whether this is a temporary phenomenon) insomuch as it affects its forward looking analysis of the counterfactual scenario and the post-merger situation. For instance, to the extent that a recession is expected to persist, the Authority would consider the unfavourable projections for future industry conditions into its forward-looking analysis.

In conclusion, the Authority does not support the view that a lenient approach to the FFD claims should be considered when factors such as a weaker economic condition or a distressed industry are at play. The Authority would consider if these factors are relevant to assess the conditions of the post-merger situation versus the situation absent the merger (if the failing firm were to exit the market).

¹¹ See the Authority's submission to the Survey on Competition Law in Small Economies, Special Project for the 2009 ICN Annual Conference available at <http://www.icn-zurich.org/Downloads/Special%20Project/ICN%20SP%202009%20-%20Answers%20from%20Ireland.pdf>.

- 5. Should the FFD Analysis Be Changed During Economic Crises? - Because of the current global economic crisis, we may expect to hear that the FFD should be made easier to invoke. It may be argued, for example, that maintaining the traditionally high hurdles for the FFD will get in the way of much-needed rationalisation of the over-capacity that now exists in many industries. Or some might argue that mergers should be encouraged in order to strengthen weakened industries. Alternatively, some might point out that because the availability of capital is now much lower than usual, authorities cannot afford to be so selective in approving buyers. Otherwise, it may take too long to find a buyer who presents few or no competitive concerns and who can actually raise the necessary financing to acquire the (failing) target firm. Do these or any other arguments justify a more lenient approach?**

The starting point is that even in good times some firms make financial mistakes, operate in shrinking markets (due to technological advances or changing tastes), suffer losses, and file for bankruptcy. However, many firms, despite temporary difficulties are able to survive and continue competing. This competitive process can be seen as an evolutionary process whereby firms that are most effective at serving consumers or reorganising themselves recover and survive from financial distress, while those who are inefficient are likely to exit the market.

This evolutionary process can be especially intense and valuable during tough economic times like present. Unlike a boom, when inefficient firms may survive and even grow, an economic downturn will tend to drive out the less efficient firms. This may give rise to opportunities for rationalisation or reallocation of capital and human resources to more value-added or growing sectors or industries.

According to an article on *The Irish Times*,¹² in the first half of 2009, examinership applications were up by over 25% on the same period last year.¹³ Normally, a successful examinership application is either a function of new investment, or sale of a certain number of core assets or the attraction of fresh borrowing. The article claims that given the inability or reluctance of the banks to lend in the current environment, the most successful examinerships are now due to investment from third parties.

Recent figures indicate that for every three companies which were put into examinership, only one will come out the other side and two will go into liquidation. This marks a dramatic change in previous success rates, according to the article. Between 2002 and 2006 for example, approximately 95% of the companies going into examinership survived as viable entities. However, success rates have unsurprisingly dropped significantly over the past two years and the outlook for companies which have gone into examinership has deteriorated significantly. In 2008, 70% of the examinership applications would have been successful but this has now decreased to 30%. A key factor behind this decrease is, according to the

¹² F. Reddan, "Examinership process called into question", *Irish Times*, Monday, 14 September 2009.

¹³ Examinership is a court enforced moratorium on creditor action which allows a period of time during which a company can be restructured. It is similar in many ways to the Chapter 11 procedure in the United States. The process involves the appointment of an individual (invariably an accountant) to act as examiner. The examiner is charged with formulating proposals for a compromise or scheme of arrangement between the company and its members and/or creditors. The examiner has no executive role and the company's directors and management remain in control of the company and of its day-to-day operations throughout the protection period. The moratorium can last for up to a maximum of 100 days by which time the examiner must have formulated and circulated his proposals, convened and held meetings with all classes of members and creditors affected by his proposals and reported back to the High Court. The proposals typically involve the introduction of new funds and the writing down of historic debt. The court then holds a further public hearing at which creditors who voted against the proposals can be heard. If the court confirms the Proposals they become binding on the company, its members and creditors from a date set by the court.

article, a combination of inappropriate companies seeking to survive via examinership and the difficulty they face in finding money to re-invest in the business.

The increase in failure in successful examinership applications appears to point to the fact the courts are becoming more and more reluctant to give protection to troubled companies, given that so many were “on life support with no prospect of survival.”¹⁴ Therefore, this seems to suggest that Irish courts are not taking a lenient approach to examinership applications.

The Authority considers that a weak economy may mean that there are likely to be more merger cases involving financially troubled firms and as a result, more mergers are likely to meet the FFD requirements. However, the Authority believes that those mergers that do not meet the FFD requirements and that substantially lessen competition should be blocked in troubled economic times just as they would in more “normal” times. The alternative would be a reduction in competition and harm to consumers and the economy. The Authority believes that, properly understood and applied, the FFD criteria and requirements are appropriate even in the current difficult economic times.

Against this background, the Authority considers that a lenient approach to FFD could be damaging to the economy in terms of reduction in competition, harm to consumers and slower recovery of the economy. This does not mean that the Authority would not consider the specific circumstances and facts of each case. For instance, if in a particular case, the Authority cannot afford to be selective in approving alternative buyers to the acquiring firm of the anti-competitive merger, the Authority may consider whether remedies are available to alleviate competition concerns.

6. Mergers between Financial Institutions - Do any special issues arise when the FFD is invoked in a merger between financial institutions (during a financial crisis)? If so, what are they and how should they be handled? What should be the relative weight attributed to competition and prudential objectives in the assessment of mergers between financial institutions?

The Credit Institutions (Financial Support) Act 2008 provides for a guarantee scheme to safeguard all deposits and liabilities in the banks that have signed up to the guarantee scheme. In addition, the Credit Institutions Act enables the Minister for Finance (the “Minister”) to take jurisdiction over a merger or acquisition that he determines is required to ensure the stability of the Irish financial system. Therefore, under the Credit Institutions Act, certain mergers and acquisitions involving banks are not notifiable to the Authority and the Minister is not obliged to seek the Authority’s advice on competition in respect of mergers notified to him.¹⁵

Under the Credit Institutions Act, the Authority is required to provide any advice, information and assistance that the Minister may require for the purposes of making a decision. The Authority considers that the word “assistance” might include the Minister requiring the Authority to investigate a merger or acquisition which meets the criteria set out in section 7(1) of the Credit Institutions Act (*i.e.* the stability of the Irish financial system). If asked, the Authority advice will be based on the standard competition analysis for mergers and acquisitions (the SLC test), and it will apply FFD arguments if required.

Under the Credit Institutions Act, it is in the Minister’s function to balance out the competition and financial stability objectives in forming his opinion.

¹⁴ In the Irish times article, this quotation appears to be attributed to one of the judges of the commercial court handling the examinership applications.

¹⁵ See Ireland’s Submission to 2009 February OECD Roundtable on Competition and Financial Markets.

7. Interplay with other policy instruments - How should a more lenient approach to FFD be articulated with other aspects of competition policy such as the review of agreements or the assessment of State Aids (where applicable)?

As stated above, the Authority does not favour a more lenient approach to the FFD. The Authority would, however consider all the relevant circumstances and facts of each individual case, including the impact of the current economic and financial crisis. These factors would be taken into account in assessing the post-merger situation and the counterfactual scenario.

A more lenient approach in this area of merger review may generate or reinforce calls for exemptions in other areas of competition law. The Authority believes that a new wave of economic protectionism would make the recovery from the crisis more difficult given the interdependence of most economies.

JAPAN

1. The Issue of the Failing Firm Defence under the Antimonopoly Act

Under the Antimonopoly Act (AMA) in Japan, the condition that “the effect of a business combination may be substantially to restrain competition” should be satisfied to prohibit a business combination.

Although there is no provision in the AMA that gives the interpretation of “the effect may be substantially to restrain competition,” the Japan Fair Trade Commission (JFTC) sets out its framework of determining the effect of what kind of business combination may be substantially to restrain competition by formulating and publishing “the Guidelines to Application of the Antimonopoly Act Concerning Review of Business Combination” (formulated in 2004 and most recently revised in 2007; hereinafter referred to as “the M&A Guidelines”).

More specifically, the M&A Guidelines categorise the types of business combinations into (a) horizontal and (b) vertical and conglomerate business combinations, and then provide the cases when the effect of a business combination may be substantially to restrain competition by unilateral conduct or co-ordinated conduct for each type of business combination. In addition, the M&A Guidelines show determining factors such as the position of the company group (“the company group” refers to all companies that would form, maintain and strengthen the joint relationships by the business combination) and the competitive situation, import, entry, competitive pressure from related markets, competitive pressure from users, etc. and describe each of the determining factors. The M&A Guidelines further indicate that these determining factors should be given comprehensive consideration to decide whether the effect of a business combination may be substantially to restrain competition.

The M&A Guidelines consider the poor business results, etc. of the company group as one of the determining factors for either type of business combination. This means that the so-called failing firm defence is regarded as one of the determining factors to consider whether the effect of a business combination may be substantially to restrain competition, like other factors such as import, entry, etc.

2. How the Failing Firm Defence is described in the M&A Guidelines

In the M&A Guidelines, the poor business results, etc. of the company group are explained as follows: (NOTE: The following description is about the substantial restraint of competition by unilateral conduct in the case of horizontal business combinations, but the same applies to other types.)

"Financial Conditions of the Company Group"

A. Poor Results, etc.

To evaluate the business ability of the company group, the financial conditions, such as whether the results of part of the company group or the business section in question are poor or not, are also taken into consideration.

Meanwhile, the possibility that the effect of the business combination may be substantially to restrain competition in a particular field of trade is usually thought to be small if a party to the combination has excess debt or is unable to obtain finance for working capital and it is likely to go bankrupt and exit the market in the near future, and it is difficult to find any business operator that can rescue the party with a combination that would have less impact on competition than the business operator that is the other party to the combination.

B. When the Possibility that the Business Combination May Be Substantially to Restrain Competition Is Usually Thought to Be Small

Whether or not a business combination has the potential to substantially restrain competition in a particular field of trade is determined by taking into comprehensive consideration all relevant determining factors in each of the specific cases. In the following cases, however, the possibility that the effect of a horizontal business combination may be substantially to restrain competition in a particular field of trade by unilateral conducts is usually thought to be small.

(a) A party to the combination has excess debt or is unable to obtain finance for working capital and it is obvious that the party would be highly likely to go bankrupt and exit the market in the near future without the business combination.

Moreover, it is difficult to find any business operator that can rescue the party with a combination that would have less impact on competition than the business operator that is the other party to the combination.

(b) The performance of a business department of a party to the combination is extremely poor and it is obvious that the party would be highly likely to exit the market in the near future without the business combination. Moreover, it is difficult to find any business operator that can rescue the business department with a combination that would have less impact on competition than the business operator that is the other party to the combination.

Under the M&A Guidelines before the revision in 2007, it was regarded that the market share of the company group after the business combination needs to be 50% or less for the poor business results, etc. to be acknowledged for consideration in the review of business combinations (hereinafter referred to as "the M&A review"). On the other hand, after their revision, by eliminating the upper limit of the market share, the M&A Guidelines articulated that there is a possibility that the poor business results, etc. will be accredited for consideration in the M&A review even if the market share of the company group is more than 50%.

The M&A Guidelines also provide examples to show the strong likelihood that the company will go bankrupt and exit the market in the near future, such as when a party to the combination has excess debt or is unable to obtain finance for working capital.

In addition, as is clear from the excerpt from the M&A Guidelines shown above, (not only the poor business results, etc. of a company as a whole, but) poor business results, etc. of only a business department of a party to the combination can be taken into consideration in the M&A review.

3. How the Poor Business Results, etc. of the Company Group are Acknowledged

It is necessary to determine on a case-by-case basis whether the poor business results, etc. of the company group should be considered or not. The M&A Guidelines do not provide any explanation about what kind of facts should be considered and what kind of evidence should be the basis for such facts when the poor business results, etc. of a company group are to be acknowledged. In this regard, “Policies dealing with prior consultation regarding business combination plans” (formulated in 2002 and most recently revised in 2007, hereinafter referred to as “the Prior Consultation Guidelines”) formulated and published by the JFTC would be helpful. The JFTC receives prior consultations from the parties to business combinations regarding whether the planned business combinations may raise issues of concerns or not under the AMA. (Such kind of a prior consultation shall be hereinafter referred to as “a prior consultation.”) In reality, most of the substantial reviews of business combinations are conducted through the prior consultation process. The Prior Consultation Guidelines provide the process and the procedures of the prior consultations.

The Prior Consultation Guidelines present as a convenient reference to the parties to the business combinations the examples of materials voluntarily submitted by the parties for showing the basis for factors examined in the M&A review. Regarding the financial condition of the company group, the following materials are given as examples:

- Materials showing the financial status of a company posting poor business results;
- Materials showing the status of negotiations with other companies capable of bailing out the company posting poor business results.

This suggests that the JFTC would use these materials as evidence in certifying the poor business results, etc. of the company group.

Needless to say, the materials that the JFTC examines in the M&A review are not limited to those mentioned above. Other materials would include those showing the causes and processes that led to the poor business results and the reasons that it is difficult for the company to recover by itself.

4. Cases Referring to Poor Business Results, etc. of the Company Group

Although there are cases in which the JFTC considered the poor business results, etc. of a company as a whole or a specific business department as a determining factor in the M&A reviews, the number of such cases is not large. In this contribution paper, the following cases are chosen from the cases¹ which the JFTC published the results of its review in the past.

4.1 *Merger of Iyo Bank Ltd. and Toho Sogo Bank Ltd.*

In this case, Iyo Bank and Toho Sogo Bank, which are both regional banks with head offices in Ehime Prefecture, planned to merge on 1 April 1991. It was expected that the post-merger bank would have high market shares in deposits and loans in the whole Ehime Prefecture as well as certain parts of the prefecture. However, in addition to the fact that the increments of the market shares were not large as a whole, the purpose of the merger was to avoid the bankruptcy of the Toho Sogo Bank and it would be very difficult to find any other appropriate merger partner than Iyo Bank. Taking these points into consideration, the JFTC held that the merger would not be substantially to restrain competition in any particular field of trade.

¹ The JFTC compiles and publishes the results of the main mergers and acquisitions cases every fiscal year.

4.2 *Hokuyo Bank's acquisition of the business of Hokkaido Takushoku Bank*

In 1998, Hokkaido Takushoku Bank, which was one of the nation's largest city banks, gave up rebuilding itself because it became almost unable to raise funds from the short-term financial market, and planned to transfer its whole business in the Hokkaido area where it mainly operates, to Hokuyo Bank.

The combined market shares after the business combination in deposits and loans were expected to become large in the whole Hokkaido area as well as in certain parts of Hokkaido. However, the JFTC concluded that the acquisition would not be substantially to restrain competition in either particular field of trade because, in addition to the existence of major competitors, Hokkaido Takushoku Bank had given up rebuilding itself and decided to transfer its business due to difficulties in raising funds.

KOREA

1. Overview of Failing Firm Defence Regulation

1.1 Definition and Regulation System

Pursuant to Clause (1) Article 7 of the Monopoly Regulation and Fair Trade Act (hereinafter the “MRFTA”), Korea prohibits anti-competitive mergers, but explicitly recognises the failing firm defence under Clause 2 of the same provision. That is, an acquisition of a non-viable firm is approved as an exception. This provision was introduced into the MRFTA in 1999 after an economic crisis in late 1997 in a bid to facilitate corporate restructuring and ensure efficiency and transparency of its M&A review.

Under the MRFTA, a “non-viable firm” refers to a company whose total capital as indicated in a balance sheet is less than its paid-in capital for a reasonable period of time. Specific criteria are stated in the KFTC Notification on the M&A Review Guidelines VIII. 2.

Meanwhile, for a company to be considered as a non-viable firm, just showing its bad financial condition is not enough, but it has to meet other requirements including the prospect of an imminent liquidation of its production facilities but for the concerned business combination. In other words, the MRFTA and its Enforcement Decree recognise an acquisition of a non-viable firm as an exception only when a company can hardly expect its production facilities to be utilised in the market without the acquisition, and other less-competition-restricting Merger & Acquisitions are unlikely.

Therefore, the three requirements for the failing firm defence to stand are (1) when the concerned M&A involves a non-viable firm, (2) when it is hard to expect production facilities, etc. to be used in the concerned market but for the M&A and (3) chances of M&As with less anti-competitive effects are low. The KFTC might approve such M&As after reviewing whether they meet the requirements, and the burden of proof falls upon the concerned enterprises.

Clause 2 Article 7 of the MRFTA

The provisions of Clause (1) shall not apply if the Fair Trade Commission deems that a combination of enterprises meets the requirements described below. In this case, the parties concerned shall prove that they meet such requirements.

1. Such combination is made with a nonviable company meeting the requirements prescribed by the Presidential Decree, *e.g.* a company whose total capital as indicated in a balance sheet is less than its paid-in capital for a reasonable period of time.

Article 12-4 of the Enforcement Decree of the MRFTA

Conditions set forth under the Presidential Decree” as per Item 2, Clause (2), Article 7 (Restrictions on the Combination of Enterprises) refer to any of the following cases:

1. The continued use of the company's production facilities, etc., in the relevant market is difficult without a combination of enterprises.
2. Carrying out a combination of enterprises that is less anti-competitive than the combination of enterprises in question is difficult.

1.2 *Whether to Grant an Exception to Non-viable Business Units*

Whereas the MRFTA has no explicit statutes, it is interpreted to grant an exception to non-viable business units just like non-viable firms. Consider a firm that is overall financially sound, but some part of its business units are deemed non-viable with continuous loss. If it faces an exit from the concerned market without the M&A and cannot expect other M&As with less anti-competitive effects, such business units should be acknowledged as an exception from prohibited M&As in line with the purpose of this regulation.

There are some cases that the KFTC approved the acquisition of non-viable business units as exceptions: DC Chemical's takeover of Kohap's Phthalic Anhydride(PA)¹ operation in 2002; NutraSweet's takeover of Daesang's aspartame business in 2003. Moreover, the KFTC amended the M&A Review Guidelines in 2007 to allow the criteria to determine non-viable firms to be applied to determining non-viable business units.

1.3 *Criteria for Determination*

To determine whether a firm is non-viable, the KFTC has to consider the following conditions pursuant to the M&A Review Guidelines VIII. 2.

- Whether the company's total shareholder's equity in its balance sheet is less than the paid-in capital for a considerable period of time;
- Whether the company's operating income is less than the interest expense for a considerable time, and the company records ordinary loss during that period of time;
- Whether the company filed for bankruptcy or applied for restoration as prescribed in the Act on Debt Restoration and Bankruptcy;
- Whether the company is under the management of its creditor financial institution because the company concerned entered into a contract to delegate management to the financial institution for the disposal of bad bonds.

Meanwhile, non-viable business units as well as non-viable firms are exempted from prohibited M&A cases, with the criteria the same as the aforementioned 4 cases.

To determine a non-viable status, the abovementioned factors should be examined, but they are not prerequisite. For instance, even if a company falls under the third criteria, it does not automatically make a non-viable firm. The fact that the company applied for reorganisation procedure is a mere proof for the current unsound financial condition of the firm, not an indicator of its actual viability or its potential to normalise its business and become a meaningful player in the concerned market.

In the Samick Music's acquisition of Young Chang (2004) case, right after Samick stopped giving financial aid to Young Chang following the KFTC's order, Young Chang applied for liquidation procedure with its worsening financial condition. Still, the court ruled that Young Chang could not be regarded as "a firm in insolvency or expected to face it in the near future." If a company with deteriorated financial condition has potential to become a meaningful player again through reorganisation procedure, it would be desirable not to recognise the failing firm defence given the intent of the law, as the court interpreted.

¹ PA (Phthalic Anhydride) is a white scale-shape solid at room temperature and when heated, turns into colourless crystal liquid. This is used as an ingredient for the phthalate plasticizer, pigments, polyester resin, paints, etc.

Special economic conditions such as the level of a decline of the industry or competition in the relevant market are considered when the KFTC determines the failing firm defence. In relation to DC Chemical's takeover of Kohap's PA business, the KFTC saw that the PA business unit was in over supply globally, and thus decided that it would be nearly impossible to liquidate the PA facilities but for the concerned acquisition.

On the contrary, in the Samick-Young Chang case, Samick argued that Young Chang would face exit from the relevant market for a gradual decrease in demand of the domestic piano industry. However, the KFTC saw that the demand decrease was temporary and by the nature of durable goods, the demand would increase along with economic recovery, thereby concluding that the production facilities in question would not be out of use in the market.

Yet there have been no argument over whether to accept the exception considering the following factors: the competition level of the market, the need for protecting the market, the macroeconomic condition of capital utilisation, etc. This is probably because such factors would be considered in all kinds of M&A, not just in determining the failing firm defence

1.4 *Burden of Proof and Degree of Proof*

Clause (2) Article 7 of the MRFTA clearly stipulates that the concerned enterprises should prove that the merger meets the requirements to be allowed. Therefore, the concerned enterprise should make efforts to present convincing proof to the KFTC (or the judge in case of litigation).

In the Samick-Young Chang case, the Supreme Court set out general conditions for the criteria for non-viable firms and clearly stated that burden of proof is on the merging parties.

2. Major Cases

2.1 *Cases where the Failing Firm Defence was Recognised*

Since 2000, the KFTC exceptionally recognised the LG Chem's acquisition of PVC business from Hyundai Petrochemical (Sep. 2000), Samyang's setting up a joint venture concerning polyester unit of SK Chemical (Oct. 2000), DC Chemical's acquisition of PA and DOP businesses from Kohap (Jan. 2001), NewtraSweet's acquisition of aspartame business from Daesang (Mar. 2003). The commission approved those M&As citing the failing firm defence.

2.1.1 *LG Chem's Acquisition of PVC Business from Hyundai Petrochemical Co. (Sep. 2000)*

LG Chem acquired PVC business from Hyundai Petrochemical and notified it to the KFTC. After the merger, LG Chem's market share increased to 47.8%, taking the top of the market and creating a bi-polar market structure with Hanwha Chemical (47.7%). This was thought to be anti-competitive, but the failing firm defence was recognised, making the merger approved as an exception.

Specifically, the following factors were taken into considerations.

First, Hyundai Petrochemical was a failing firm, with its operating profit outweighed by interest payment for 3 consecutive years from 1998. Its PVC business also constituted a failing unit. Without selling the business unit, this firm was very likely to face liquidation due to shortage of funds.

Second, without the merger, it was thought that Hyundai's production facility would be unlikely to be used in the market because it was difficult for Hyundai to find a third party to buy the business unit due to its weak cost structure and insufficient economies of scale.

Third, there was little possibility of M&As with less anti-competitive effects. Hyundai tried to sell its ailing PVC business to several local and foreign companies, but all failed. Even the company I which Hyundai had been negotiating on foreign investment attraction excluded PVC businesses from the investment. Those incidents supported the fact that there was little possibility of less-competition-restricting M&As in relation to Hyundai's PVC business acquisition.

2.1.2 *DC Chemical's Takeover of Kohap's PA and DOP² Business Units (Jan. 2003)*

DC Chemical agreed to take over the PA and DOP business units from Kohap, and notified the deal to the KFTC. After its deliberation on the case, the KFTC concluded that the deal would restrain competition in the PA market, but recognised the failing firm defence.

The Commission considered the following factors.

First, Kohap was designated as a company subject to workouts in July 1998, and starting from 2000, its capital was completely impaired and its operating income and net-income was deficient.

Second, but for the deal, Kohap's production facilities, etc. seemed likely to go out of use in the concerned market. Since PA was globally in over supply at the moment, it was virtually impossible to dispose of Kohap's PA and DOP facilities without an M&A with DC Chemical.

Third, it seemed that there were no chances of M&As with less anti-competitive effects. The number one player in the market was the only enterprise, aside DC Chemical, capable of taking over the concerned facilities, but it would do greater harm on market competition.

2.2 *Cases where the Failing Firm Defence was Dismissed*

The followings are the recent cases where the KFTC disapproved M&As and didn't accept failing firm defence: Samick's acquisition of shares in Young Chang (Sep. 2004) and Muhak's acquisition of shares in Daesun Distilling (Dec. 2002).

2.2.1 *Samick's Acquisition of Shares in Young Chang (Sep. 2004)*

Samick Music and its affiliate participated in the capital increase of Young Chang, acquiring a 48.58% of stake and notified it to the KFTC on March 26 2004. The KFTC issued a corrective order to Samick to sell its shares, citing a risk of creating a monopolist in the upright piano market (September 1 2004)

KFTC's Resolution on the Case

At that time, Young Chang was in the midst of liquidity crisis for it paid out retirement benefits due to a massive layoff in 2003. However, the KFTC thought that Young Chang has high potential to turn around, with third parties aspiring to acquire it. Also utility of its facilities was quite high, thus there was low possibility of being liquidated.

Upon Samick's suspension of financial aid, Young Chang went bankrupt on September 2004. Yet the commission deemed that a bankrupt firm doesn't necessarily exit from the market because even in case of declaring bankruptcy, many companies make a turnaround through court receivership and settlement procedure.

² Plasticizers refer to ester additives that increase the plasticity or fluidity of the material (usually polymer materials) to which they are added.

High Court's Resolution on the Case

Samick brought the case to the High Court against KFTC's corrective measures, and the Court's ruling regarding the company's failing firm defence was as follows.

"At the time of the deal, Young Chang's financial condition was very poor, but this was a temporary liquidity crisis stemmed retirement benefits payout in the wake of its restructuring. So it is difficult to tell that Young Chang is in insolvency or to face it in the near future."

"Given that Young Chang was enjoying high brand recognition and recorded considerable sales performance, it is hard to expect it to exit from the relevant market."

Moreover, companies other than Samick offered to take over Young Chang or to participate in its capital increase with consideration, which led the Court to reason that there could be other M&As with less anti-competitive effects. Therefore this deal could hardly meet one of the requirements to be approved, the Court viewed. As a result, the Court discarded Samick's failing firm defence in this case.

Supreme Court's Resolution on this Case

The Supreme Court upheld the decision of the KFTC and the judgment of the High Court which had dismissed the failing firm defence.

2.2.2 Muhak's Acquisition of Shares in Daesun Distilling (Dec. 2002)

In the market of soju, a distilled beverage native to Korea, Muhak acquired a stake of 33.77% of Daesun Distilling and notified it to the KFTC on June 29, 2002. The KFTC ordered Muhak to sell the stakes, citing that the post-merger firm's share in the distilled soju market of the Busan and South Gyeongsang Province markets took up 91.5% and 97.2% respectively which made it a monopolist in the concerned market undermining competition.

KFTC's Resolution on this Case

The KFTC dismissed the failing firm defence for the following reasons.

For years, Daesun had its capital impaired, but during the period in question, its operating profits were surpassing its interest payment, and in 2001 the year before the merger, it recorded ordinary profit of 85.9 billion won. Also, its operating profits ranked 2nd in the industry in 2001 and its sales operating margin 1st for 3 latest years in a row, indicating its financial condition getting better.

In addition, it accounted for 84.4% of the Busan soju market, securing a stable domestic demand, and it was undergoing settlement proceedings. Also considering its continuous surpluses, it's hard to think that Daesun would face an immediate exit from the market.

High Court's Resolution on this Case

Muhak filed a suit with the High Court, but the court dismissed the case quoting KFTC's resolution. As Muhak gave up on appeal, this was final judgment.

3. Conclusion

Facing the global economic crisis, there are voices calling for easing the criteria for the failing firm defence in Korea. Yet, the KFTC keeps the incumbent provisions intact after reviewing the past deliberation cases and global standards. That's because Korea has concluded that undergoing the economic crisis set off in 1997, the current system already has proved its effectiveness and sufficiency.

In the Samick-Young Chang case, the KFTC did not recognise the concerned enterprise's failing firm defence, citing that Young Chang's stakeholders could undergo economic difficulties in the short term, but in the long run, the piano industry will regain competitiveness, both domestically and internationally. In fact, Young Chang went bankrupt after the KFTC's decision, but over the course of liquidation procedure, it made a turnaround in about 2 years, acquired by a firm for a price about 5 times higher than the one presented by Samick.

The rationale for the failing firm defence is that acquiring a non-viable firm won't restrain competition as much as acquiring a well-functioning firm, and serves public interests by assuring the failing firm's assets to be reused in the market. Against this backdrop, for a company that is temporarily suffering shortage of liquidity, but can normalise its management, it requires proper sanctions since it still can affect the competitive landscape of the relevant market. Moreover, if there is much room for less anti-competitive M&As considering corporate value or a third party's attempt to acquire, not to recognise the failing firm defence would live up to the purpose of a M&A review regime.

NEW ZEALAND

The OECD's invitation for written submissions noted that the 2009 Roundtable has been organised from the perspective that, while the failing firm defence "has remained a rarely used component" of merger policy, the current global economic and financial crisis could lead to more claims that a merger target was a failing firm.

The experience of the Commerce Commission (the Commission) over an extended period has been that, although failing firm claims have not been numerous, they have not been rare events. With the possibility of an increase in failing firm claims in mind, the Commission recently prepared new failing firm guidelines.

To date, there has not been any particular increase in failing firm claims in New Zealand in relation to merger proposals. This is against a background of a reduced number of applications for the clearance of mergers and acquisitions. In 2008-09 only eleven clearances were determined, compared with twenty six in 2007-08.

1. New Zealand Competition Law and the Analysis of Failing Firm Claims

Section 47 of the Commerce Act 1986 (the Act) prohibits the acquisition of "assets of a business or shares if the acquisition would have, or would be likely to have, the effect of substantially lessening competition in a market."

New Zealand operates a voluntary merger regime. This allows a firm that is proposing to undertake a merger or acquisition to choose whether to apply to the Commission for 'clearance' under section 66 of the Act, or authorisation under section 67, or to proceed without a clearance or authorisation. The Commission will grant a clearance if it concludes that the proposal would not result in a breach of section 47. If the Commission is not satisfied that there is not likely to be a substantial lessening of competition, it will decline to clear the proposal. The Commission will grant an authorisation where it is satisfied that a proposed merger is likely to result "in such a benefit to the public that it should be permitted". Most merger and authorisation applications to the Commission are for clearances; applications for authorisation are uncommon.

The Commission monitors un-notified mergers and acquisitions, and, where it appears that section 47 might have been breached, it will undertake an investigation. This could include the question of whether the target firm was failing. Where an investigation leads the Commission to conclude that a breach has occurred, it may seek remedies in the High Court.

There is no legal test or definition of a 'failing firm' in New Zealand, and the term is not used in the Act. However, where appropriate, the concept forms part of the analysis of the likely effect of a proposed merger or acquisition, in the formulation of counterfactual scenarios.

2. 1993 Discussion Paper

In October 1993 the New Zealand Commerce Commission and the Australian Trade Practices Commission (now the Australian Competition and Consumer Commission) released a joint discussion paper entitled "Acquisitions and the failing company argument."

The paper identified two central factors. The first was whether the supposedly ‘failing company’ was likely to experience commercial failure. The analysis would continue only if this was the case. The second was whether, if the company did fail, its resources would exit the market and so cease to represent an actual or potential source of supply (or other constraint) on the market. If this was the likely outcome “the acquisitions are unlikely to raise dominance or competition concerns...”

The paper observed that:

“The investigations of company failure and of resource exit are matters for judgement, based on commercial fact and experience, rather than matters of formula. Nonetheless, there are factors that might be checked in the investigation. These factors are neither necessary nor exhaustive but they may be helpful in establishing directions for inquiry.”

Several additional factors were suggested as having possible application. They included whether the target firm had taken measures to redeem itself, whether it was insolvent, whether there were pre-existing links between the target and the acquirer, whether the target had sustained continuous losses making it unlikely it could trade out of its difficulties, whether the target or the acquirer had made the first approach and whether there were any reasonable alternatives to outright sale.

The principles outlined in the discussion paper continue to be broadly applicable. The position that a decision on whether a firm should be considered to be failing is a matter for the Commission’s judgment, rather than being determined by the application of a formula, appears sound. The main refinements to the approach outlined in the 1993 paper to take account of more recent developments are the need to clarify the nature and quality of the evidence the Commission requires to allow it to reach a view.

3. Commission Decisions Involving Failing Firm Issues

While failing firm claims in New Zealand have not been numerous, the Commission has been required to consider the issue on a number of occasions. The analysis that was applied in two early cases (1984 and 1991) and in three recent cases (2008-09) is outlined below.

3.1 J. Wattie Canneries/Jim Bull, (Decision 85, June 1984)

The failing firm argument was first considered 25 years ago in the Commission’s decision involving substantial aggregation in the production and distribution of frozen potato products. While the competition law then in force (the Commerce Act 1975) differed from the present law, the discussion of the failing firm argument bears similarities to how the issue is currently assessed. Points made in the decision included the following in paragraph 10:

- “...if the target company were “failing’ to the extent that it was soon likely to cease business then a takeover proposal relating to that company may be found not to significantly reduce competition – a consideration which can be taken into account...”
- “...it must be probable that...the company’s departure from the industry or the significantly reduced competition it is able to offer is imminent. This would exclude the case, for example, where the company continues to provide significant competition, albeit on a less vigorous basis, by being able to reorganise its affairs by selling off unprofitable assets, obtaining extra equity capital, or otherwise restructuring.”

3.2 *NZ Co-operative Dairy and Waikato Valley (Decision 264, June 1991)*

This was an early decision under the current Commerce Act 1986. The application involved the proposed merger of two dairy companies. This decision outlined how the failing firm argument had been assessed. Issues highlighted in the Commission's decision were:

- There is no failing firm exemption in the Commerce Act, but the potential failure of the target company could form part of the competition analysis;
- The purpose of the test is not to protect an individual company, but to protect the competitive process;
- The test is whether supply would continue in the absence of approval of a proposed merger;
- The financial difficulties of the target company are not the determining issue;
- The failing firm test would not be met if restructuring had allowed the target firm to continue to provide competition, even though to a lesser extent than previously.

3.3 *Southern Cross Health Trust/Aorangi Hospital (Decision 650, September 2008)*

This decision was on a proposal that the operator of a privately funded hospital in Palmerston North acquired the only other privately funded hospital in that city.

The Commission's decision noted that, while the applicants had not explicitly proposed a failing firm (or failing division) argument, the application had been presented within such a framework. The applicant had submitted that one of the hospitals would close and exit because, among other factors, there were unsustainable economic losses, the population base could not support two private hospitals and all options pursued to improve the business had been exhausted.

The Commission did not agree with the applicant's conclusions. The Commission considered that, while one likely counterfactual scenario was that the Southern Cross hospital would close within the relevant timeframe for competition analysis, the evidence indicated a real and not merely remote possibility that it would remain as a competitor for at least two years and would therefore continue to compete. The Commission's view was there was insufficient evidence to dismiss the latter as a possible scenario, and the application was declined.

3.4 *Shell New Zealand Ltd and Mobil oil New Zealand Ltd (Decision 655, October 2008)*

This application was for Shell to acquire the 'Aerostop Network' assets of Mobil. The network supplied aviation fuel to light aircraft and helicopters through unattended bowser refuelling facilities at several airfields and airports.

The Commission accepted that Mobil was determined to exit the relevant markets. Two likely counterfactuals were formulated. One was that Mobil would exit these markets and close the Aerostop Network. The second was that Mobil would exit the markets, but would sell to Shell the facilities in locations where there was no aggregation of market share, sell the other outlets that it could to third parties and close the outlets that could not be sold.

The Commission concluded that, while in the factual scenario the merged entity would face no constraint from existing competitors, it would face significant constraint from potential competitors in the form of de novo entry. On this assessment, the Commission cleared the proposal.

3.5 *Fletcher Building Ltd and Stevenson Group Ltd (Decision 663, February 2009)*

The proposal was for Fletcher to acquire the masonry assets of Stevenson in Auckland and in Whangarei. The assets were used for the manufacture and wholesale supply of concrete masonry products.

The factual scenario was that the proposal would remove the existing competition from Stevenson faced by Fletcher.

The counterfactual scenario was that, following sustained and substantial losses in its masonry business, despite efforts to reverse them, Stevenson would exit the business by sale or closure. (A decision to that effect had been made formally by Stevenson's board of directors).

The Commission considered that there was a real and substantial prospect that the closure of Stevenson's masonry business was imminent, absent sale to another party.

Stevenson claimed that there was no third party offer that would yield a price greater than the outcome of closure. The Commission investigated the likelihood of (a) a third party purchase of the business as a going concern, and (b) the third party purchase of Stevenson's assets, and their use to compete with Fletcher, if the business closed. The investigation did not identify any serious alternative offers. While some interest was shown by a number of parties, there was little indication that any of this interest would lead to credible alternative offers. The Commission took account of the downturn in the construction industry and the potential impact of the current recession.

The Commission concluded that the proposed acquisition would not have, or be likely to have, the effect of substantially lessening competition in the relevant markets. The proposal was cleared.

4. New Guidelines

The 1993 discussion paper noted above has been out of print for many years, and, until recently, the Commission's published guidance on how it would approach failing firm claims was limited to a relatively short section in the Merger and Acquisitions Guidelines issued in January 2004. However, further guidance to the business and legal communities has been available in the competition analysis in the Commission's determinations on clearance applications where failing firm claims had been made.

The possibility that the current economic situation might lead to an increased number of failing firm claims recently led the Commission to review its approach to failing firms. In July 2009 the Commission released draft guidelines for public comment. These took account of New Zealand law and the analytical approach the Commission had taken in the clearance decisions which the issue had been raised. The guidelines issued by competition authorities in a number of other jurisdictions were examined as part of the review.

The Commission's invitation for public comment noted that the draft guidelines did not indicate any relaxation in the normal competition analysis when assessing failing firm situations. Rather, the guidelines recognised the value to businesses in having clear guidance on the supporting evidence the Commission would require to allow failing firm claims to be assessed. A final version of the guidelines, incorporating some of the suggestions made by stakeholders during public consultation, is to be released shortly.

The guidelines point out that the Commission may take several factors into account in assessing whether there is evidence that failure appears to be actual, imminent or probable. The Commission may consider if there was a trend of negative cash flows over a sustained period, whether there was any prospect of restructuring or refinancing the business and whether there had been any serious but unsuccessful attempts by the failing party to rescue the business. Assessing whether there was an alternative third party purchaser would include examining if there was any prospect of a third party acquiring the business as a going concern, whether reasonable efforts had been made by the failing firm to find a third party purchaser, and the likely fate of the firm's assets on closure.

The guidelines note the Commission's awareness that the failure of a firm may make an urgent decision on a clearance application necessary, and they confirm that the Commission will endeavour to make its decisions in a timely manner. The need for applicants to provide relevant, complete and robust information when a failing firm argument is made, to assist the Commission to make its assessments quickly, was emphasised.

5. Suggested Issues

The Commission has the following comments on the suggested issues and questions that accompanied the invitation letter. The comments follow the headings in the OECD list.

5.1 *Definition of the Failing Firm Defence*

As outlined above, failing firms are not defined in legislation, and the concept is not regarded as a 'defence' under New Zealand law. The question of whether failure is probable is a matter of fact in identifying the relevant counterfactual(s).

5.2 *Type and Quantum of Evidence*

- While the Commission's Guidelines contain a non-exhaustive list of types of evidence that could assist the Commission to reach a view on the likelihood of failure by the target firm, there is no checklist of what evidence must be provided, and no weighting scheme has been applied when the evidence is assessed. The guidelines outline the types of evidence that might usefully be supplied to the Commission to support failing firm claims. The types mentioned include management accounts, budgets and forecasts, analyses of margins and profitability, board minutes and papers, internal strategic papers and independent appraisals of the business. It was noted that the Commission might sometimes obtain such information directly from the target company, rather than exclusively through the prospective acquirer. The Court also would assess the evidence as a matter of fact.
- The Commission considers all likely counterfactuals. Where there is more than one real and substantial counterfactual, each is assessed against the factual. If competition is substantially lessened when comparing any of the counterfactuals against the factual, then the acquisition has the likely effect of substantially lessening competition in a market.
- In the failing firm scenario, the assessment therefore is based on whether a likely counterfactual is that the target firm will exit the market in the near future, and that it will not be acquired as a going firm by a third party competitor; or that its assets will not be acquired by third parties and used to provide supply in the relevant markets. The depth of competition analysis is likely to be substantial. If the likely counterfactual is that the target firm would continue to participate in the market, even though providing a reduced constraint for the prospective acquirer, this would not satisfy the Commission that a firm is failing.

- It is possible for the Commission to give clearance to the acquisition of a failing division. However, as the Commission's Guidelines indicate: "Such cases require particular care because of the ability of the parent firm to allocate costs, revenues and intra-company transactions among itself, its subsidiaries and its divisions."

5.3 *Harmonisation and Evolution*

- The Commission considers that, while there are some differences in the approach to the failing firm concept between jurisdictions, its approach is broadly in line with that of many other jurisdictions. A distinctive feature of the approach taken in New Zealand is the assessment of multiple counterfactuals following a High Court judgement in 2007¹, not just the most likely counterfactual. While there could be advantages in narrowing any differences that might exist between jurisdictions in the way failing firm claims are assessed, differences in legal systems and differences in court precedents will limit the extent to which harmonisation could be achieved.
- One aspect in which New Zealand differs from some other jurisdictions is the approach the Commission takes to financial failure. A number of jurisdictions require actual or likely insolvency, whereas, as described above, the Commission's approach does not require this.
- The basic principles underlying the Commission's approach to the assessment of failing firms have not changed to any great extent since the 1984 *Wattie* decision outlined above. The main changes have been the requirement to consider multiple counterfactuals, and to describe more fully the types of evidence that would assist the Commission.

5.4 *Market Context*

- *Declining industry.* In terms of the clearance process, the fact that an industry is declining would not necessarily be a factor in the analysis. The question would remain whether failure of the target firm was probable within the timeframe for competition analysis. In principle, the situation of a declining industry could be considered in the authorisation process; the test in section 67 of the Act is whether the acquisition "will result, or will be likely to result, in such a benefit to the public that it should be permitted".
- *Nature of competitive interaction.* It does not seem desirable to relax the tests applied to determine whether a target firm is failing. If firms are competing "for the market through investment and innovation" the issue does not seem likely to arise.
- *Small economy.* It does not seem necessary to take a different approach to whether a firm is failing on the basis of the size of the economy. While higher market concentrations are likely in small economies, the fundamental question of how the proposed acquisition of an allegedly failing firm is likely to affect competition remains. In New Zealand's case, the importance of an industry to the local economy does not affect the competition analysis in the case of clearance applications. However, this dimension could be examined if an application was made for authorisation of the proposed acquisition.
- *Capital markets.* The impact of the availability of debt or equity funding, whether industry-specific or influenced by more general macroeconomic conditions would be a matter of fact in relation to whether the allegedly failing firm could survive.

¹ *Woolworths v Commerce Commission* High Court, Wellington (CIV-2007-485-1255)(CIV-2007-485-1379)(CIV-2007-485-1731)

- *Should the FFD analysis be changed during economic crises?* In the Commission's view, the approach applied to assessing failing firm claims should not be relaxed in a crisis if the context is that of applications for clearance. The impact of the availability of debt or equity capital on the feasibility of a third party acquisition of the failing firm would be a matter of fact to be assessed in deciding the counterfactual(s). If a prospective acquirer considers that other issues should be taken into account, an application could be made for authorisation.
- *Mergers between financial institutions.* Banks have a critical role in the functioning of an economy. However, the Commission's role is that of promoting and preserving competition in markets. Prudential objectives should continue to be the responsibility of the Central Bank and/or the Government.
- *Interplay with other policy instruments.* The Commission does not have a role in the assessment of State Aids. The Commission is responsible for enforcing the legislation assigned to it. Other aspects of more broadly defined competition policy are matters for Government decision.

6. Conclusions

The Commerce Act 1986 does not recognise the concept of a failing firm and there is no legal test or doctrine on the concept. However, for at least the past 25 years the Commission has, where appropriate, taken account of the relevance to future competition of the possibility that the target firm in a proposed merger could be failing. The first articulation of the Commission's approach was in a 1984 decision made under the previous competition statute.

The failing firm concept is part of the Commission's analytical framework for assessing the counterfactual outcome of merger proposals. (While the term 'counterfactual' was not used by the Commission until relatively recent years, the concept it embodied had been long recognised, as noted above). There have been several cases where the Commission concluded that a target firm was failing and gave clearance on these grounds. There have been other cases where the Commission did not accept that the counterfactual was failure, and where clearance consequently was denied.

The Commission's 1993 joint discussion paper with the Australian Trade Practices Commission outlined an approach to failing firm claims that is still broadly applicable. The most substantial change has been the introduction of the requirement to consider multiple counterfactuals.

The Commission's recently prepared guidelines affirm that there has been no change in principle in how failing firm claims are assessed in the analysis of the likely competitive effects of merger and acquisition proposals. The guidelines emphasise that whether a firm should be regarded as failing is a question of fact, and is not the outcome of the application of a formula, and they outline the types of information that would assist the Commission to conclude whether the target firm should be regarded as failing.

The recent guidelines were issued against the background that the current economic and financial crisis might lead to an increased number of applications for the clearance of merger and acquisition proposals, and that it would be helpful to the business and legal communities to have the Commission's approach updated and explained in more detail. In the event, there has not so far been any increase in clearance application involving failing firm claims. Indeed, the total number of clearance applications recently has been below the average of recent years.

The Commission recognises that there will be cases where urgent decisions are needed on applications to clear the acquisition of allegedly failing firms. The Commission is ready to act as quickly as is reasonably possible, but, nevertheless must see sufficient evidence to satisfy itself that the claim that a target firm is failing is valid. Applicants can help to minimise the time required if they provide the Commission promptly with relevant evidence.

POLAND

The *failing firm defence* concept (hereinafter also referred to as “FFD”) has not been directly regulated in the Polish antimonopoly law. In consequence neither Polish antimonopoly authority nor courts has presented their opinions on the subject. It does not mean, however, that when conducting merger investigations the problem of companies at risk with bankruptcy has not been discussed. Despite the fact that Polish law lacks regulation directly referring to the *failing firm defence* concept, it is possible to find in the Polish law some provisions which indirectly refer to the concept in question. Two provisions should paid particular attention:

- Article 14.4 of the Antimonopoly Act, which excludes the obligation to notify the concentration of entrepreneurs if the concentration takes place in the course of bankruptcy proceedings.
- Article 20.2 of the Antimonopoly Act introducing as an additional concentration assessment test, a public interest test, which gives the possibility of accounting for the *failing firm defence* concept when using the test to assess concentration.

1. **Excluding Obligation to Notify Concentration of Entrepreneurs if Concentration takes place in the course of Bankruptcy Proceedings**

In the Polish antimonopoly law entrepreneurs are obliged to notify their intent of concentration when turnover criteria are met (Article 13.1 of the Antimonopoly Act) and when a transaction is considered to be a form of concentration, specified in the Act (Article 13.2 of the Antimonopoly Act).² However, Article 14 of the Antimonopoly Act specifies situations in which entrepreneurs are not obliged to notify their intent of concentration. Pursuant to Article 14.4 of the Antimonopoly Act, there is no obligation to notify the intent of concentration if this concentration takes place in the course of bankruptcy proceedings, providing that the entrepreneur which intends to take over the control is not a competitor or does not belong to a capital group composed of competitors of an entrepreneur which has been acquired. The basis for this provision is the observation that concentrations taking place in conditions specified in this norm do not have any negative impact on the market and thus, do not have to be subject to assessment performed by an antimonopoly authority. Thus, the aim of this regulation is to reduce charges and limit transaction costs borne by entrepreneurs, as well as a better allocation of powers and funds of an antimonopoly authority.

The analysis of Article 14.4 leads to the conclusion that the article will be applied providing that two premises are met simultaneously:

- Concentration takes place in the course of bankruptcy proceedings;
- An entrepreneur taking over the control is neither a competitor nor is a member of a capital group composed of competitors of an entrepreneur which has been acquired.

When analysing the first premise, it is important to note that it refers to a situation in which bankruptcy proceedings are in progress or when a sale transaction of an entrepreneur is a direct result of

² Polish Antimonopoly Act does not include a definition of concentration; it only provides the information on what types of transactions are considered to be concentrations.

such proceedings. Further resale of an acquired bankrupt enterprise will be subject to notification. Additionally, it refers to a situation in which bankruptcy proceedings are conducted in Poland, in a Polish court and based on Polish legal regulations. Thus, the regulation in question does not apply to situations in which bankruptcy proceedings take place abroad. The second important premise is that an entrepreneur taking over the control is neither a competitor nor is a member of a capital group composed of competitors of an entrepreneur which has been acquired. According to the definition provided in the Polish Antimonopoly Act, a competitor is an entrepreneur who simultaneously introduces or may introduce, purchase or may purchase goods on a relevant market (Article 4.11 of the Antimonopoly Act). In practical terms it means that the provision in question is used by banks and investment funds.

2. Failing Firm Defence as an Important Circumstance taken into Account when Applying Public Interest Test

A basic merger test in Polish law is SIEC test. However, a public interest test is an additional merger test, which can be applied in certain situations. Pursuant to Article 20.2, Polish antimonopoly authority gives its consent for concentration, which will result in a significant impediment to competition, particularly by creating or by strengthening dominant position, providing that there exist overriding public interest and particularly if:

- Concentration will contribute to economic development or to technical progress; or
- Concentration may have positive impact on the national economy.

Analysing above premises it may be said that especially the second provision may be used for the purposes of applying FFD. Bankruptcy of inefficient companies may result in significant negative social effects, *i.e.* unemployment. This argument was raised several times during the debate on rescuing Polish shipyards. Threat of unemployment may be exemplified by two decisions of Polish antimonopoly authority which concerned the establishment of two energy groups, *i.e.* Polska Grupa Energetyczna³ and Grupa Tauron.⁴ When justifying approval for these anticompetitive mergers between energy producers Polish antimonopoly authority referred to the analysis of Polish needs in the area of energy, namely obsolete and too small capacity as far as energy in Poland is concerned. What is important, the OCCP indicated also that concentrations in question would contribute to the Polish energy security and would result in saving of workplaces.

It is also important to take account of procedural consequences of such a construction of the provisions in question. If SIEC test constitutes a basic merger test and a public interest test is an exception, it determines the distribution of burden of proof. In case of a SIEC test, it is an antimonopoly authority which shall prove that a notified concentration leads to significant impediment to competition. Whereas if we resign from applying this basic merger test, it is the party to the proceedings which shall prove that an intended transaction will contribute to economic development or to technical progress, or that it can have a positive impact on the national economy. It is an entrepreneur who, as a professional, has complete knowledge about the market on which he or she conducts business activities, as well as about consequences that a notified concentration can have. Consequently, it is an entrepreneur who shall prove that his or her personal benefits which result from a given transaction translate into general social benefits accessible to all market participants. The role of an antimonopoly authority in the proceedings is to verify the above mentioned assertions in the hearing of evidence in order to balance values protected by law and to make a final decision.

³ Decision of the OCCP President of December 22, 2006, No. DOK 163/06, not published.

⁴ Decision of the OCCP President of March 8, 2007, No. DOK 29/07, not published.

Another aspect of the discussed regulation, related to the proceedings, is an exceptionally high standard of burden of proof which rests on a given party. Evidence proceedings, based on Article 20.2, are rather complicated. It results from the fact that every concentration may have both positive and negative impact on the market. Generally, positive and negative effects appear simultaneously, and as a result, after producing evidence, Polish antimonopoly authority has to balance all anti-competition and pro-competition effects of concentration. It is important to note that if Article 20.2 is applied, the nature of pro-competition effects of concentration should be exceptional, since benefits resulting from a transaction will have to concern as many entities as possible, if not all consumers. The same applies when party tries to rely on FFD considerations.

- Harmonisation and evolution

As stated above there is no explicit regulation of FFD in Polish law. Neither there has been any discussion on this subject. It may be result of rather insignificant number of cases when parties are invoking FFD considerations. Existing legal framework responds to those considerations and seems to work fine. Therefore we see no need for harmonisation of national approaches to the FFD, for jurisdictions where the FFD concept is absent. However, it may be a case for those national jurisdictions which regulated FFD.

- Market context

When analysing market context one should bear in mind particularities of Polish economic transformation. During the last decade of XX century Poland was confronted with several declining industries. Polish antimonopoly authority had to deal with this issue in numerous of cases. However, it has never been accepted that declining industries should be treated in a special, more lenient way. The only exceptions were situations when overriding public interest came into play.

- Should the FFD Analysis Be Changed During Economic Crises?

Despite the economic crisis, Polish antimonopoly authority has not noticed in the examined cases the multiplication of arguments referring to the crisis, including arguments raising the issue of the FFD. Because of the lack of direct regulation of the FFD in the Polish law, it is difficult to say whether the attitude towards the FFD should be liberalised. However, it seems that a possible increase in the number of cases where the FFD would be analysed does not have to mean that the FFD would be justified in every case. It is also difficult to accept the situation in which we depart from fundamental rules governing the process of choosing potential purchasers because of the crisis. We should try to investigate every case in order to see whether the lack of potential purchasers is objectively justified or whether there are other factors which may come into play. One should remember that the crisis is a part of the market economy and the fact that it has started means that one day it will probably finish, whereas, giving its consent to concentration or accepting a purchaser who raises serious doubts will be permanent and will prevail even after the crisis finishes.

- Mergers between Financial Institutions

The issue of the FFD has not been raised in any concentrations between financial institutions supervised by Polish antimonopoly authority. It is also worth mentioning that in the period of the economic crisis, Polish government has not undertaken any actions aiming at saving inefficient financial institutions. From the point of view of Polish antimonopoly authority, we do not consider it necessary to undertake such actions or to change merger assessment rules for the needs of financial institutions.

- Interplay with other policy instruments

According to the Polish antimonopoly authority, one should very carefully approach the possibility of employing the FFD in the assessment of agreements concluded between different entrepreneurs. The crisis may create incentive and sometimes an excuse to undertake various anti-competition initiatives, for instance in the form of crisis cartels.

However, it is difficult to find any justification for the practice of applying the FFD concept to analyses concerning state aid. The state aid law elaborated, in a comprehensive way, the methodology of the assessment of companies which are in a difficult financial situation or companies which are in bankruptcy. Balance test for the assessment of new state aid projects, introduced by the Commission, constitutes a new comprehensive instrument for the economic assessment of state aid. This test also creates the possibility of assessing the financial situation of potential beneficiaries of state aid projects and of creating adequate state aid funds.

SPAIN

1. Introduction

The Spanish pharmaceutical sector is a highly regulated market where both prices and margins are fixed by Law in certain cases, in particular, in reimbursable prescription-only pharmaceuticals dispensed in Spain.

The Spanish pharmaceutical market has been traditionally characterised by the great influence of brand medicines with scarce competition between brand and generic medicines. However, in the last years, and mainly due to an increase in sanitary expenditure, new legislative initiatives have been adopted to promote the entry of generic medicines and thus increasing competition between brand and generic medicines.

The purpose of this paper is to put forward *the key elements of the Spanish pharmaceutical sector* both from the regulatory framework and from the competition enforcement angles, focusing on *some interesting antitrust cases* which the Spanish Competition Authority has dealt with in the last years.

2. Regulatory Framework of the Spanish Pharmaceutical Sector

2.1 Authorities

The Spanish Health system is regulated under Act 29/2006 of Guarantees and the Rational Use of Medicines and Health Products.

In relation with the sanitary authorities, the main players in the pharmaceutical system, according to current legislation, are the following:

- The Directorate General of Pharmacy and Health Products of the Ministry of Health, which controls the pricing and reimbursement process;
- The Interministerial Commission on Pharmaceutical Prices which imposes the price of reimbursable prescription-only pharmaceuticals dispensed in Spain and decides on final pricing;
- The Spanish Medicine Agency (Ministry of Health), which is responsible for the evaluation, authorisation, inspection, surveillance and control of pharmaceuticals;
- The general practitioners, who play a fundamental role in the demand for prescription pharmaceuticals, being responsible for the prescription itself of these medicines;
- The pharmacists that, according to Act 29/2006, are obliged to dispense generic medicines, if any, for a certain prescription; and, within the generic medicines, those with the lowest price.

2.2 Health Legislation

In 1986, the General Health Act established a National Health System (NHS) in Spain. It is a highly decentralised system, with universal coverage and financed through general taxation. There are 17

Autonomous Communities which have full powers regarding public health and healthcare services planning. The health system financing remains centralised and it is distributed between the Autonomous Communities according to a capitalisation scheme. Under the NHS, healthcare is provided free of charge except for pharmaceuticals.

Pharmaceuticals are classified in Spain into the following groups:

- Prescription-only pharmaceuticals, which are all reimbursed;
- Non-prescription reimbursable pharmaceuticals, which can be prescribed by a medical doctor (and, thus, reimbursed by the NHS) or not prescribed (and not reimbursed);
- Over the counter (OTC) pharmaceuticals, which are not reimbursed;
- Other non-prescription, non-reimbursable pharmaceuticals, which are not OTC.

In 2006, a new law on “Guarantees and the Rational Use of Medicines and Health Products” was adopted.⁵ This new act introduced a new reference pricing system. The pricing of reimbursable prescription-only pharmaceuticals dispensed in Spain is carried out by the Interministerial Commission on Pharmaceutical Prices within the Ministry of Health.

Furthermore, in 2007, a Royal Decree⁶ was adopted in order to regulate the procedure of authorisation, register and dispense conditions of medicines for human use.

3. Competition in the Spanish Pharmaceutical Sector

3.1 *Competition among Branded Pharmaceuticals*

Competition among branded pharmaceuticals depends on the therapeutic group to which they belong, and, more specifically, depending on the ATC3 or ATC4. In Spain, there are markets for certain therapeutic groups which are highly competitive, but also others where competition does not exist due to the fact that just a very little number of medicines are commercialised for certain diseases.

According to Act 29/2006, prices of branded pharmaceuticals are fixed by the Ministry of Health taking into account the prices of the three EU Member States where the medicine is commercialised at a lower price. In case the medicine is not commercialised in any EU Member State, the Ministry of Health, when fixing the medicine’s price, carries out an investigation of the trade-off effectiveness-cost in which different factors are taken into account, such as the R&D cost, the investment made by the company and the therapeutic action of the medicine.

3.2 *Competition between Branded Pharmaceuticals and its Corresponding Generics*

Competition between branded pharmaceuticals and its corresponding generics depends once again on the therapeutic group to which they belong and, therefore, on the ATC3 or ATC4. Prices play in these

⁵ Act 29/2006 of Guarantees and the Rational Use of Medicines and Health Products.

⁶ Royal Decree 1345/2007.

cases a key role. Yet, again, there are markets with a high degree of competition between brand and generic medicines but there are still many markets where no generics are commercialised.⁷

Under Act 29/2006, and aiming at the promotion of competition between brand and generic medicines, the practitioner is recommended to prescribe according to active ingredients and not according to a particular brand. At the same time, in the case of reimbursable pharmaceuticals, pharmacists are obliged to dispense the medicine with the lowest price in case brand and generic medicines exist for the same treatment and in case the lowest price medicine are both the generic and the branded medicine.

As far as patents are concerned, Royal Decree 1345/2007 establishes two exclusivity periods: an exclusivity period of 11 years for brand medicines data and an exclusivity period of 20 years for the patent itself.

Moreover, the first generic medicine that is commercialised usually has a discount between 10-35% of the brand medicine regarding the same treatment. Nevertheless, subsequently commercialised generics do not have a regulated price or discount, being fixed by the generic medicines companies, and, therefore, there exists the possibility of fixing lower prices than the reference prices established each year by the Government.

According to a recent report issued by the European Commission on the pharmaceutical sector inquiry, Spain is one of the EU Member States with greater delays in the generic medicines entry. On average, the delay stands up to 13 months from the original medicine patent expiration date.

However, this does not necessarily mean the existence of competition concerns between brand and generic medicines in Spain. In fact, typical initial problems for generic entry have not been detected in this sense, given that pharmaceutical companies have reacted by applying 3 different commercial policies:

- They have tried to develop their own generic medicine;
- They have decreased the price of their brand medicine; or
- They have stopped promoting their brand medicine.

Therefore, as far as the Spanish Competition Commission is concerned, so far the delay in Spain regarding generic medicines entry in the market has been caused by existing problems regarding authorisation, register and marketing procedures of generic medicines by sanitary authorities.

3.3 *Competition among Generic Pharmaceuticals*

Competition among generic pharmaceuticals obviously depends again on the therapeutic group to which they belong and more specifically they are analysed depending on the ATC3 or ATC4. In Spain, there are markets highly competitive in this sense but also markets for certain therapeutic where only one generic is active, especially in the case of markets characterised by a low demand.

4. Competition Enforcement in the Spanish Pharmaceutical Sector

In recent years, The Spanish Competition Authority has dealt with two important cases in the pharmaceutical sector.

⁷ For example, in the paracetamol market there is only one brand pharmaceutical and several generics whilst in the levetiracetam market (an antiepilepsy pharmaceutical) there are no generics yet.

The first one (the URIACH Case) is related to predatory prices of a branded pharmaceutical company as a result of the entrance of a generics one.

The second case (PHARMACY ASSOCIATIONS), and probably the most important one given the sanction imposed for the declared infringement, is related to a recommendation made by several associations of pharmacists to cause a boycott to a generic company which had announced the commercialisation of its products at lower prices than the regulated reference ones.

4.1 *The URIACH Case*

This case was originated by a complaint issued by GES GENERICO (a Spanish company devoted to the production and marketing of generics) in 2005 against GRUPO URIACH for an alleged abuse of a dominant position consisting of selling under cost its medicine *Venofer* (a medicine for hospital use to treat the lack of iron), aiming at the elimination of its competitors.

In Spain, medicines for hospital use are only dispensed at the pharmaceutical service area in each hospital. Therefore, it can only be sold to hospitals, generally through tenders.

URIACH was marketing its medicine *Venofer* at a maximum authorised price (PVL) of 59.02€/pack of 5 ampoules (11.80€/ampoule) until the generic *Feriv* was launched, marketed by GES GENÉRICOS on the 1st July of 2005, at a price of 29€/pack (5.80€/ampoule). Since then, URIACH started marketing its medicine to the Sanitary Services and to private hospitals at a price of 13.50€/pack (2.70€/ampoule).

As a result of the investigation the former *Servicio de Defensa de la Competencia* (now Investigations Division of the CNC) issued a report to the Council concluding the existence of an abuse of dominant position in the market for trivalent iron, through predatory pricing by URIACH of its medicine *Venofer*. However, the Council decided to file the case as they considered that URIACH had just reacted to the entry of a new competitor and, hence, they started a price war among them.

4.2 *The Pharmacy Associations Case*

The special interest of this case lays on the fact that the entry by a generics company was hampered by several pharmacy associations and not by its direct competitors, the brand medicine producers.

In fact, this case reflects the present situation in the Spanish market where the main competition concerns are not between brand and generic pharmaceuticals but between distributors and pharmaceutical producers of generic pharmaceuticals on the one hand and between the pharmacies and pharmaceutical producers on the other.

Focusing on this particular case, it was originated in 2007 by a complaint from *Laboratorios DAVUR* (a Spanish company which produces and commercialises generic pharmaceuticals) against four Pharmacy Associations alleging restrictive practices. These practices consist of a collective boycott against DAVUR products through a collective recommendation of these associations to their associates (pharmacies).

In March 2007, *Laboratorios DAVUR* decided to decrease the price of twelve of its generic pharmaceuticals below the reference prices set by the Health Ministry. The following were, among others, the main marketed pharmaceuticals of the company: Omeprazole, Simvastatin, Paroxetine and Fluoxetine.

After this decision, several Pharmacy Associations made recommendations to almost all the pharmacies in Spain (22,360 e-mails were sent) in order to stop the commercialisation of DAVUR medicines on the basis that, from their point of view, pharmacists were not obliged to dispense the cheapest medicine but the medicine that is included in the Ministry Order imposing reference prices of generic

medicines. The e-mails and letters sent also recognised the fear that DAVUR lower prices could significantly affect the annual price revision made by the Health Ministry, leading to lower reference prices of generic medicines on the following year and, therefore, a decrease in their future revenues.

As a result, many Spanish pharmacists decided not to deal with *Laboratorios DAVUR* avoiding the entry of its products in their pharmacies.

During the investigation proceedings, *Laboratorios DAVUR* came to an agreement with the main claimed associations and withdrew its complaint. Nevertheless, the Investigations Division decided to continue with the investigation *ex-officio*. Finally, on the 24th March 2009, the Spanish Competition Commission Council solved to declare the existence of infringement of article 1 of the Spanish Competition Act, qualified as a collective recommendation to homogenise the pharmacies behaviour against *Laboratorios DAVUR* in the market for generic medicines subject to medical prescription.

The Spanish Competition Commission Council imposed a total fine of EUR 1 million to these associations.

5. Final Remarks

Due to its nature, the pharmaceutical market is a highly regulated market in Spain where even several margins, discounts and prices are fixed by the Public Administration. As far as generics are concerned, from a competition point of view, barriers of entry to generics companies still persist originated by the existing legal procedures to obtain the binding authorisations and registrations.

In this respect, so far, competition problems concerns have arisen rather more from concerns between distributors and pharmaceutical producers of generic pharmaceuticals or between pharmacies and pharmaceutical producers, than between brand and generic pharmaceuticals.

Nevertheless, the Spanish Competition Authority has been especially active to ensure a successful entry of generics in the Spanish pharmaceutical sector, tackling both legal barriers of entry through its reports on legislative initiatives as well as other competition concerns that may be detected such as the DAVUR boycott which was sanctioned early this year.

SWITZERLAND

1. Failing Firm Defence Provisions by the Swiss Competition Law

Under the Swiss Competition Law, *i.e.* the Federal Law on Cartels and Other Restrictions of Competition (Act on Cartels, ACart) and the Swiss Merger Control Regulation (together the Swiss Competition Law), the Swiss Competition Authority (Comco) may intervene against mergers if they create or strengthen a dominant position liable to eliminate effective competition. Unlike some other jurisdictions, the Swiss Competition Law does not stipulate any specific failing firm defence arguments.

According to Art. 10 para. 2 let. a ACart, the Comco may prohibit a merger only if it is likely that the merger creates or strengthens a dominant position liable to eliminate effective competition. Thus, for a prohibition, the merger has to be considered as being the cause of the dominant position in question. This mandatory causal connection for prohibiting a merger has two important effects. Firstly, the creation or strengthening of a dominant position through internal company growth is not covered by Art. 10 ACart. Secondly, in the event of a rescue merger, the causal connection gives the Comco the possibility to clear the merger even if a dominant position is created or strengthened through the merger. This is because the merger is not the cause for the creation or strengthening of the dominant position since the market shares and resources of the company in need of rehabilitation would have anyway devolved to the absorbing company. Thus the merger is not the cause of the deterioration of the market structure (“failing firm defence”).

Similar to the approach taken by the European Commission and other competition authorities, the Comco requires the following conditions to be present in order for the failing firm defence to be applicable:

- Without the acquisition, the firm to be acquired would exit the market;
- The acquirer would obtain the shares of the firm to be acquired if the latter would exit the market; and
- There are no alternative offers for the acquisition of the failing firm that are less restrictive to competition.

2. Significant Cases

For the first time, the failing company defence was successfully used in the Comco’s decision regarding the merger of two publishers in French-speaking Switzerland, leading to the creation of the newspaper *Le Temps* in 1997.¹ Since then, several cases have referred to the failing company defence argument. A few of these cases are presented below.

2.1 *Le Temps*

In its *Le Temps*-decision, the Comco considered that due to the circumstances on the relevant markets it was likely that a failing of the merger would lead to the market exit of one of the two involved newspaper editors, namely the publisher of the “*Journal de Genève et Gazette de Lausanne*” (hereafter

¹ RPW 1998/1, p. 55 et seq.

JdG), in the short or long term. Reasons given were the saturation of the press market, the stagnation of readership, the increase of printing costs, and the decline of the investment in the advertising market. Furthermore, it was thought to be likely that the market shares of the publisher of JdG, the “Société Anonyme du Journal de Genève et de la Gazette de Lausanne”(hereafter SAJG), in case it would fail, would be gained mainly, if not solely, by the Edipresse group, the second company involved in the merger and the main publisher of “Le Nouveau Quotidien”, due to its strong market position. Experts acknowledged that in French-speaking Switzerland, there was only space for one single *supra*-regional daily newspaper. Thus, through the merger, the Edipresse group would be able establish a quasi-monopoly and competition would therefore be significantly impeded. Even though, the Comco concluded that the creation of a new company with shared control by the Edipress Group and the SAJG was the solution having the least restrictive effects to competition since SAJG would still remain at the market as an independent editor group.

2.2 *Emmi / SDF and AZM / Emmi*

In 2003, the Comco had to decide about the merger between Emmi and Swiss Dairy Food (hereafter SDF).² It came to the conclusion that the merger might create a dominant position but due to failing firm defence arguments the merger was not causal for the deterioration in the market structure. Comco’s inquiries stated that (a) without financial support SDF would have to file for bankruptcy in medium term, (b) due to adequate know-how, financial power, logistics and the necessary overall assortment Emmi would obtain SDF’s shares and (c) there were no alternative offers for the overall assortment of SDF.

On 6 March 2006, the Comco cleared the acquisition of the AZM *Aargauer Zentralmolkerei* by Emmi AG.³ Although the Comco found that the acquisition would put Emmi in a dominant position on the Swiss markets for milk, cream and butter, it cleared the acquisition on the basis of failing firm defence arguments. It considered it to be likely that, in the absence of the acquisition, AZM would exit the market and Emmi would gain AZM’s share. Following its *AZM/Emmi*-decision, the Comco issued a recommendation to the Swiss Federal Council. The latter proposed to accelerate the opening of the Swiss markets for the products concerned since these were regulated under the Swiss law and were therefore closed to foreign competitors. The Comco concluded that effective competition in the relevant markets could only be restored by means of opening up of the Swiss market.

2.3 *Tamedia / Edipresse*

In 2009, the Comco had to decide once again about a merger in the market of newspapers in the French speaking part of Switzerland. In September 2009, the Comco approved the acquisition of the Swiss activities of the Edipresse group by the Tamedia AG.⁴ The assessment showed that there were no market additions in most of the relevant markets. An exception was the market for commuter newspapers in the French speaking part of Switzerland. Here, the merger would lead to the consolidation of the two remaining commuter papers in that region, the “20minutes” and “Le Matin Bleu”. The Comco concluded that the advertisement market of the French speaking part of Switzerland gave space but for one single commuter newspaper. The independent expert, who was assigned by the Comco, confirmed this assessment. Since the introduction of commuter newspapers to the market, Tamedia with 20minutes and Edipresse with Le Matin Bleu suffered losses of several dozen million Swiss francs. Due to these losses Le Matin Bleu would have been ruled out from the market within a short time even without the merger. In addition, the analysis showed that no publisher in the present situation was ready to acquire Le Matin Bleu.

² RPW 2003/3, p. 529 et seq.

³ RPW 2006/2, p. 261 et seq.

⁴ Comco press release: <http://www.news-service.admin.ch/NSBSubscriber/message/attachments/16857.pdf>.

Strictly speaking, the merger just described was not decided on the basis of a failing company defence, but rather on that of a failing division defence. Le Matin Bleu is not an independent enterprise, but only the commuter newspapers division of the Edipresse Group respectively of 20minuten AG. Thus, this case raised the question whether a merger could be permitted despite the creation or strengthening of a dominating market position, by which effective competition can be eliminated, if only a part of the enterprise and not the enterprise as a whole is concerned. It was the first case, for which the Swiss competition authorities had to decide whether the justification of a rescue merger finds application also on individual divisions of enterprises or not, and how the arguments should be applied.

In principle it is not impossible to permit a merger with arguments of the failing division defence. However, according to the Comco's opinion, particularly high demands have to be met for the proof that the merger is not causal for the deterioration of the market structure (missing causality). Otherwise, each sale of an allegedly unprofitable division could be justified under merger control aspects, if the seller explains that the business activities had to be stopped in case of the interdiction of the planned merger. The high requirements of the failing division defence are particularly valid in view of to the susceptibility to manipulation of the profit and cost accountings.

In its decision, the Comco stated that the conditions of the failing division defence are in general congruent to the failing company defence, but as previously mentioned, particularly high requirements have to be placed. Therefore, the failing division defence is applicable if the following three criteria are cumulatively fulfilled:

- Without external support the absorbing business division would disappear from the market within a short time;
- The other enterprises involved in the planned merger would absorb most or all market shares of the disappearing business division;
- There is no alternative solution that is less harmful for the competition than the merger.

TURKEY¹

1. The Control of Concentrations

An important subject concerning the function of competition policy during the crisis is “control of concentrations”. Adoption of a more flexible approach in the evaluation of concentrations during the crisis and even by-passing the supervision of competition authorities on “public interest” grounds constitutes an important debate topic in current crisis.

As it is the case in other areas of competition policy, it would be a big mistake to circumvent competition law enforcement in the evaluation of concentrations during the financial crisis on “public interest” grounds. Mergers and acquisitions made in an environment with no competition supervision would increase the concentration within the market, and the burden thereof will be paid by the consumers. At this point, one can claim that anti-competitive effects of those mergers and acquisitions authorised during the crisis may be prevented through *ex post* remedies after the crisis has passed. However, we believe that this is far from a real solution. This is because allowing anti-competitive consolidations within the economy may cause irreparable damages. On the other side, when the operational costs of *ex post* supervision on competition authorities are taken into consideration together with the limited resources of those authorities, it may not be possible to conduct an effective *ex post* supervision concerning the anti-competitive market structures in the whole economy.

Basically, the current case-law in competition law regarding the control of concentrations allows a “flexible” approach concerning the acquisition of undertakings which are in financial distress. As it is known, “failing firm defence” has generally been taken into consideration by competition authorities where one or more of the parties to the transaction are carrying a serious risk of going out of business. Therefore, it is possible to authorise the acquisition of undertakings in trouble without making crisis-specific amendments in the application of the current rules.

During the current crisis, Turkish Competition Authority has not yet received a merger notification incorporating the failing firm defence. However, this defence was taken into account in some of the past decisions of the Turkish Competition Authority. The first of these decisions is the *Erciyas*² decision. In the decision concerning the acquisition of some of the assets of Toros Biracılık ve Malt Sanayi A.Ş. (Toros) by Erciyas Biracılık ve Malt San. A.Ş. (Erciyas), it can be seen that the failing firm defence was accepted, though not explicitly. It was determined that the dominant position in the market would be strengthened after the notified transaction. Nonetheless, it was stated that it would be impossible for Toros to continue its operations and that disallowing the transaction would lead to a waste of resources for both the economy of the country and for the parties. Also, within the same decision, it was found that no other undertaking wished to acquire the assets owned by Toros and that Erciyas intended to invest and increase its production capacity by acquiring the relevant assets. The transaction under consideration was authorised for the aforementioned reasons, in spite of the possibility for a strengthening of the dominant position and a significant restriction in competition.

¹ This contribution is an excerpt from the contribution of Turkey submitted to the Competition Committee for the Roundtable on Real Economy: The Challenges for Competition Policy in Periods of Retrenchment (DAF/COMP/WD(S009)9/ADD2) held on 16 – 18 February 2009.

² Competition Board Decision dated 12.2.1998 and numbered 379-43, (Official Gazette, dated 19.11.1998, and numbered 23528).

Another decision whereby the Competition Board accepted the “failing firm defence” was *Uzel*³ decision. Failing firm defence was considered in the decision concerning the acquisition by Uzel Holding A.Ş. (Inc.) (Uzel), of Efe Otomotiv Sanayi ve Ticaret A.Ş. (Efe Automotive Industry and Trade Inc.) (Efe). In this market where the parties to the acquisition produced components used in automotive sector, Uzel’s market share would reach 62% after the acquisition and there would remain two main undertakings. It was likely that there would be significant restriction of competition in the market in the post-transaction process. However, without the acquisition, Efe would most likely be excluded from the market. The decision expressly stated a view in support of “defending the failing firm”. Even though concentration would increase significantly in the relevant market post-acquisition, it was stated that Uzel’s market share could have increased even where the transaction was not authorised. Furthermore, the decision also mentioned that the production capacity of the failing undertaking would leave the market and that there were no alternative mergers and acquisitions which were less restrictive of competition. It was also stated that machinery and manpower could remain idle. Therefore, the likelihood of negative social effects in the absence of the transaction was also pointed out.

In the recently taken *Vatan Newspaper*⁴ decision which involves failing firm defence, it was decided that the acquisition of Vatan Newspaper by Doğan Group would result in the group’s market share reaching 40 % in terms of net sales and 64% in terms of advertisement revenue, and that the synergy and portfolio effect brought about by the inclusion of Vatan Newspaper in the group was capable of increasing the market share even further both in terms of the number of net sales and advertisement revenue, that therefore the transaction would result in the strengthening of the dominant position of Doğan Group; however the transaction was conditionally authorised on the grounds that the indebtedness of Vatan Newspaper to Doğan Group was not a collusive act entered into for making use of failing firm defence, that the bankruptcy of Vatan Newspaper was inevitable, that there was not a better alternative buyer for the competitive structure in the market, that in the absence of the merger the brand of Vatan Newspaper would inevitably be excluded from the market and the resulting gap would most likely and substantially be filled by Doğan Group, and that the effects which restrict competition and which would arise in the market if the transaction is authorised would still arise if the transaction was not authorised.

Given the abovementioned decisions of the Competition Board, it can be said that generally four conditions are to be met for the failing firm defence to be accepted in Turkish competition law. The first condition is that the failing firm would leave the market in the near future. The second is the nonexistence of alternative mergers and acquisitions which would restrict the competition less. The third condition is the impossibility of the failing undertaking to stay in the market through methods such as its reconstruction or narrowing down its activities. The last condition is that, even in the absence of the merger and acquisition, the market share of the failing undertaking would pass to the acquiring undertaking.

While evaluating mergers and acquisitions in a crisis period, in addition to the evaluations concerning the substance of the transaction, finalisation of the merger and acquisition examination in a short time is of great importance as well. This is because, ensuring that the measures taken in a crises period produce maximum benefit depends, before all else, on the timely initiation of the measure. At this point, it might be beneficial if the competition authorities finalise the evaluations of the mergers and acquisitions notified to them as soon as possible, without waiting for the statutory timeframes, and thus ensure legal clarity for undertakings as soon as possible. But of course, an important duty rests with the undertakings in this process too, in terms of notifying the merger and acquisition accurately and co-operating constructively with the competition authority in the evaluation process, so that the final decision can be taken within a short time.

³ Competition Board decision dated 20.07.2000 and numbered 00-27/294-164 (Official Gazette dated 05.03.2002 and numbered 24686).

⁴ Decision dated 10.3.2008 and numbered 08-23/237-75.

Provided that it is limited to the crises period, another solution which can be adopted so that the expected benefit of the planned merger and acquisition takes effect promptly is the finalisation of the merger and acquisition without waiting for the competition authority's final decision. Especially where there are no serious concerns as to the merger and acquisition and where irreparable damages are not likely, adoption of such a method by competition authorities might prove beneficial for the expedition of the process. But there is no doubt that the application of this option in practice is primarily dependent on such a power being granted to competition authorities by the relevant legal arrangements. For instance, under Turkish competition law, the Competition Authority does not hold such a power.⁵

⁵ Under the Act No. 4054 Article 16, carrying out a merger and acquisition without the authorization of the Competition Authority is subject to administrative fines.

UNITED KINGDOM

1. Introduction

UK merger control law does not require that a qualifying merger be notified to the relevant competition authorities. Companies can proceed at their own risk and are not penalised in any way for failing to notify mergers, although the ‘voluntary’ UK regime allows for own-initiative investigation by the OFT at any point up to four months after the transaction has completed. This position is in contrast to many merger control regimes where parties are not permitted to complete the transaction unless and until merger control clearance has been obtained.

As a result, a number of the issues facing the application of the failing firm defence (FFD) in jurisdictions that do have compulsory notification systems may therefore not apply, or do not apply to the same extent, to the UK system.

Nevertheless, in substantive terms, the OFT and the CC (the UK Authorities) apply the FFD as part of their counterfactual assessment of reviewed mergers in a similar way to the framework applied in the US and by the European Commission (EC). The UK Authorities believe that this framework is suited to dealing with all market conditions and economic circumstances and do not see any justification for its requirements being softened, even in the current economic downturn. Mergers can result in long-lived structural change to markets via the removal of an independent competitor. By contrast, changes to market and economic conditions are often temporary, allowing otherwise anticompetitive mergers in; for example, times of economic difficulty may lead to consumer harm in more prosperous times in the future, and may even hinder economic recovery.

The FFD, as applied in the UK, EC and other jurisdictions, has shown itself capable of being applied in a variety of markets and economic conditions, including the current economic downturn. As such, the UK Authorities do not believe, on the evidence we have seen, that the FFD needs to be modified or the evidentiary standards associated with proving it relaxed.

2. Outline of the UK Merger Regime

The assessment of mergers in the UK is conducted as a two-phase process, giving distinct but interrelated roles to the OFT, the CC and sometimes the Secretary of State.⁶ Both anticipated mergers and completed mergers are covered by the legislation, and the UK Authorities may investigate mergers either prior to completion or post completion.

As noted above, UK merger control law does not require that a qualifying merger be notified to the OFT. However, companies can seek legal certainty by informing the OFT (the Phase 1 authority) about a prospective merger in advance so as to obtain clearance (and the OFT encourages companies to contact it early in the merger process). Companies which choose to complete their transaction without obtaining merger clearance assume the merger control risk that their transaction could ultimately be ‘unwound’ if

⁶ The Secretary of State at the Department for Business, Innovation and Skills (BIS) has a role in certain merger decisions where there is a public interest or special public interest. Where the Secretary of State has issued an intervention notice, the OFT (and Ofcom, in the case of media mergers) must advise the Secretary of State on any mergers which might fall within the scope of the public interest or the special public interest provisions of the Act. The Secretary of State may refer public interest and special public interest cases to the CC (see paragraph 0, below, on the role of the Secretary of State in relation to stability of the UK financial system).

competition concerns are established. For example, in 2008 three investigations of completed mergers not notified to the OFT resulted in structural remedies.⁷

The OFT has a duty to refer to the CC for further investigation any relevant merger situation where it believes that ‘it is or may be the case that’ the merger has resulted or may be expected to result in a substantial lessening of competition (SLC). This statutory formulation is sometimes expressed in shorthand as meaning that a Phase 2 investigation may be triggered by the OFT having a ‘realistic prospect’ that an SLC will result from the merger.

After a more extensive investigation, the CC must consider whether a merger ‘has resulted, or may be expected to result’ in an SLC, and it will apply a balance of probabilities standard to its analysis; in other words, it addresses the question: is it more likely than not that an SLC will result?

The OFT’s ‘realistic prospect’ threshold is intentionally a lower and more cautious threshold than that applied by the CC after more extensive investigation. Where merging parties argue that prevailing conditions of competition are not the appropriate benchmark to assess merger effects (as in a FFD), the OFT has explicitly adopted a cautious approach in recognition that counterfactuals are easily the subject of self-serving speculation – relatively easily alleged but difficult, given the information asymmetries, to verify independently.

The OFT’s reference test means that where merging parties argue that the target business would have exited the market absent the merger in any event (such that a FFD may be applicable) the OFT therefore requires ‘sufficient, compelling evidence’ that the various elements of the FFD are established. The differential standard applied at Phase 1 by the OFT and Phase 2 by the CC means that it is possible for the OFT to reject a failing firm counterfactual for lack of compelling evidence, but for the CC to accept one, having conducted further analysis.⁸

3. UK Failing Firm Guidelines

The OFT and CC’s approach to the application of the FFD are consistent with each other and based on the same conceptual analysis. In essence, there are two pre-conditions for the FFD to apply in the UK:

- The firm would inevitably have exited the market absent the merger (with no serious prospect of reorganisation); and
- There must be no substantially less anticompetitive alternative to the merger.

The OFT restated its position on the FFD (as found in its existing guidelines and decisional practice) in December 2008. Although this restatement did not change the rules applied, it was designed to ensure that, in the face of the economic downturn, businesses could see clearly the framework applied by the OFT in this area.⁹ The restatement (presented in full at Annex A) states that, for the FFD to be accepted, the OFT must receive ‘sufficient, compelling evidence’ that exit was inevitable and that there was ‘no realistic and substantially less competitive alternative’. If the OFT considers there to be no realistic prospect that the firm would have survived, or that there was no substantially less anticompetitive outcome to the merger, it will allow the FFD.

⁷ In one instance, the acquirer provided the OFT with structural undertakings in lieu of a reference to the CC. In the remaining two cases, the CC imposed structural remedies.

⁸ See the example of the OFT’s and CC’s assessments of the acquisition of Millway by Long Clawson, discussed at paragraph 22, below.

⁹ *Re-statement of OFT’s position regarding acquisitions of ‘failing firms’, Dec 2008.* OFT 1047.

The CC's current guidance¹⁰ (presented in full in Annex B) requires all of the following conditions to be satisfied:

- The business must be unable to meet its financial obligations in the near future;
- The business must be unable to restructure itself successfully; and
- There should be a no less anti-competitive alternative to the merger.

The CC's examination of the evidence and facts will be more in-depth than the OFT's given it has more time to come to a decision. It will also require compelling evidence to satisfy itself on the application of the conditions.

The UK Authorities have recently produced new draft joint merger guidelines. These were published as a consultation document in April 2009,¹¹ and will cover the approach of the OFT and CC (albeit, taking account of the different evidential thresholds each body has) as to whether a merger gives rise to an SLC (although the actual analysis in this area is unlikely to change materially from existing practice). The relevant section of the draft guidelines is set out in Annex C. The three considerations under these draft guidelines are:

- The inevitability of exit of the firm in question;
- Whether there would be a substantially less anti-competitive alternative buyer for the firm; and
- Whether failure of the firm would be a substantially less anti-competitive outcome than the merger.

4. Substance of Analysis

There are a range of sources from which the UK Authorities will generally seek to obtain evidence to assess whether a firm is failing. These will usually include the alleged failing firm itself, its customers and competitors. There are a number of types of evidence that the UK Authorities will look for in each case as well, including the profitability of the company and its ability to meet its financial obligations going forward. However, each set of circumstances will be different and the UK Authorities do not have a definitive list of the sources or types of evidence that will satisfy them that a failing firm counterfactual is appropriate. Rather, they will look to all the relevant circumstances of a case and perform a bespoke investigation tailored to the facts of the case at hand.

4.1 *Inevitability of Exit of the Firm in Question*

With respect to this first limb, the UK Authorities will need to be satisfied that there is no serious prospect of the target business trading out of its current position in its current form or in a reconfigured structure, taking into account the reality that even businesses in financial difficulties often survive and recover.

In order to determine whether a firm would inevitably have exited the market absent the acquisition, the UK Authorities will look to see whether the firm is in such a perilous position that it is unable to meet its financial obligations in the near future. We look at such evidence as: past and current company accounts and in particular its most immediate liabilities; whether the company is in a formal process for companies

¹⁰ *Merger References: Competition Commission Guidelines*, June 2003.

¹¹ OFT/CC: *Merger Assessment Guidelines: consultation document*, April 2009.

in financial difficulties, such as administration, receivership or liquidation; how management has tackled the issue of impending failure,¹² such as board meeting minutes, management accounts commentary and strategic plans for the business. The firm may have hired advisers to perform strategic reviews, and where these can be shown to have been prepared independently and objectively these are likely to be particularly good evidence.

Example: Holland and Barrett/Julian Graves¹³

Holland and Barrett (a subsidiary of NBTY Europe Limited) and Julian Graves were two of the UK's largest specialist health food retailers. The merger was referred to the CC by the OFT on 24 March 2009. The CC ultimately found that the FFD was not made out because it was not persuaded there was no substantially less anticompetitive alternative to the merger.

Julian Graves had been acquired by the Icelandic investment company Baugur in a highly leveraged transaction with debt finance provided by an Icelandic investment bank, Landsbanki. Julian Graves was leveraged further to provide funds for the subsequent acquisition of Whittard of Chelsea; it began to make losses and was put up for sale in May 2008.

At the OFT stage, the merger parties argued that Julian Graves' financial performance was declining, most of its suppliers had indicated they would cease supplying it and KPMG had refused to sign an audit opinion stating Julian Graves was a going concern. Nevertheless, the OFT was not convinced on the evidence before it that Julian Graves would inevitably have exited the market, nor that it could have been restructured. It was also not persuaded that there were no other potential (and less anticompetitive) buyers for the business.

The CC examined the management accounts and margins of Julian Graves, and its financial 'headroom'. It also reviewed evidence of operational problems provided to it by the acquirer.

The CC found Julian Graves was struggling to maintain its debt payments to Landsbanki and management was resorting to desperate measures to generate cash, including significant price discounting and opening stores in new locations simply in order to receive landlord incentive payments. Many suppliers had put stop orders on Julian Graves as a customer, causing Julian Graves' stock levels to fall and its range of available products to contract, and landlords were beginning to take legal action to pursue rent payments. At the time of the acquisition the business was still trading but had negative net assets. Julian Graves' auditors did not feel that they could sign off their audit opinion on the accounts to March 2008, which would require a belief that the business was a going concern, until they had received a letter of parental support from NBTY (the acquiring company under investigation) following the acquisition. The CC therefore concluded that Julian Graves would have been unable to meet its financial obligations in the near future.

Nevertheless, the CC ultimately declined to find the FFD was met in this case, because other buyers had expressed 'clear and credible interest' in acquiring Julian Graves and, but for the merger, one of these would have been likely to acquire it.

Once satisfied that the company would not be likely to survive in its present form, the UK Authorities will then look to whether the firm could be successfully reorganised. The two most common ways in which a company can be re-structured are via a financial restructure (changing the way the firm is financed) and an operational restructure (changing the firm's strategy, which may include closing down unprofitable business units).

¹² In fact, the absence of any indication of management concern over the firm's financial position is good prima facie evidence that the firm was not failing.

¹³ OFT Report *Completed acquisition by NBTY Europe Limited of Julian Graves Limited*, 24 March 2009; CC Final Report *Holland and Barrett / Julian Graves*, 20 August 2009.

When determining whether financial restructuring is a possibility, the UK Authorities will look to the sources of finance potentially available to the firm and the relative cost of each. The asset book of the firm can be a useful source of information, as there may be assets against which finance could be raised. The possibility of the firm raising finance through further investment from shareholders or investors will also be considered, and internal strategy documents and interviews with management will be examined.

Internal strategy documents will also be useful in helping to assess whether the firm's strategy could be amended so as to make it a viable business. For example, in its assessment of Stagecoach/Preston Bus,¹⁴ a merger involving the provision of local bus services, the OFT declined to find the target was failing because the evidence before it suggested there was a realistic prospect that it could have restructured its business by reducing the frequency and number of its routes. The OFT referred the case on 28 May 2009, and the CC's Phase 2 inquiry is ongoing at the time of writing.

Interviews with management, customers and competitors may also provide useful insights as to how a firm may have been able to re-organise itself. At the OFT stage in particular, the OFT will need to be satisfied that all bona fide attempts were made by the target exploring the possibility of restructuring, and that none of these carried a realistic prospect of succeeding.

Example: Long Clawson/Millway¹⁵

Long Clawson and Millway (a division of Dairy Crest) were both manufacturers of cheese, including the 'Stilton' variety. Long Clawson's acquisition of Millway was referred to the CC by the OFT on 8 October 2008. Long Clawson did not advance a FFD to the OFT, but did so to the CC. The CC ultimately found that the FFD was made out in this case.

The target – Millway – had operational performance issues that were long-standing, and the CC sought evidence of previous restructurings in order to determine its effectiveness. It spoke with Dairy Crest, customers and other third parties and found that Dairy Crest had made a number of investments to improve the production facility and address Millway's problems. Some of Millway's customers had also worked with it over a long period to address quality problems. The CC noted that neither Dairy Crest's capital investment into Millway's production site, nor Millway's collaboration with its customers, successfully resolved Millway's production and quality issues.

The CC concluded that, had it been possible to restructure Millway so as to make the business profitable, Dairy Crest would have done so. The fact that Dairy Crest had been unable to make the business profitable after many years of management attention and financial investment suggested that it was not feasible and the loss of significant customers made a successful restructuring even more unlikely.

Although this paper is focused on the FFD, it should be remembered that the FFD is merely one particular type of counterfactual to a merger. Occasionally, companies may meet the requisite standard for 'inevitable exit' for reasons not primarily driven by the financial position of the company. For example, in the OFT's assessment of First/Black Prince,¹⁶ the merger parties successfully argued that the target's exit was inevitable because its owner wished to retire for health reasons. The company's situation was shown to be such that, although reorganisation was theoretically possible, there was no incentive for the owner to go down this route, and it would have been more profitable for the owner to close the business and sell off the assets. The OFT was therefore satisfied that, with or without the merger, the target would have exited the market.

¹⁴ OFT Decision: *Completed acquisition by Stagecoach Group plc of Preston Bus*, 28 May 2009.

¹⁵ OFT Report: *Completed acquisition by Long Clawson Dairy Limited of Millway Limited*, 8 October 2008 and CC Final Report: *Long Clawson Dairy Limited / The Millway business of Dairy Crest Group plc*, 14 January 2009.

¹⁶ OFT Decision: *Anticipated acquisition by First West Yorkshire Limited of Black Prince Buses Limited*, 27 May 2005.

4.2 *Whether there would be a Substantially Less Anti-Competitive Alternative Buyer for the Firm*

4.2.1 *No Realistic and Substantially Less Anti-Competitive Alternative*

The UK Authorities must also be satisfied that there are no substantially less anticompetitive alternatives to the merger. This may take the form of other potential purchasers whose acquisition of the target business would produce a substantially better outcome for competition. Even if such a purchaser may not be prepared to pay the seller as high a purchase price or otherwise benefit the target business, the UK Authorities will take into account any realistic prospect of alternative offers above liquidation value. Alternatively, in some cases it may also be better for competition that the target business fails and the remaining players compete for its market share and assets rather than being transferred wholesale to a single purchaser. Each of these two possibilities is discussed below.

4.2.2 *No Substantially Less Anticompetitive Merger*

In considering this part of the FFD test, the UK Authorities are likely to consider whether the company has made a bona fide attempt to engage all potential purchasers.¹⁷ In this regard, we will ask for lists of potential purchasers contacted and a copy of any information memorandum, and we will contact potential acquirers for their views. As liquidation of the assets is the next alternative to a sale of the business, any bid above liquidation value is likely to be considered realistic. When speaking with other potential purchasers, the UK Authorities will take into account the hypothetical nature of the questions¹⁸ (particularly regarding acquiring assets out of liquidation), how the purchase would have been financed and, of course, any competition implications.

What is considered a ‘bona fide’ attempt to sell a business will depend on the nature of the case. In transactions involving listed, high profile companies, for example, it may not be necessary to undertake an extensive and high profile advertising campaign. For example, in HMV/Zavvi,¹⁹ the OFT was satisfied that there was sufficient awareness of the sale processes (plural because multiple stores were involved and each had their own sale process) through targeted marketing of the stores to potentially interested parties and because the demise of Zavvi had been widely publicised in the UK press. Conversely, in Long Clawson/Millway, the OFT was not satisfied that all bona fide attempts had been made because only three potential purchasers had been contacted.²⁰

Where mergers are of a more localised and/or less publicised nature, different types of evidence may be required. For example, evidence of Expressions of Interest (EOIs) being sought, advertisements run in local newspapers and so on.

¹⁷ This is likely to be particularly important at Phase 1 given the OFT’s ‘realistic prospect’ threshold for a reference to the CC.

¹⁸ These are hypothetical in the sense that potential acquirers are being asked to comment on what their bidding behaviour would have been had the current merger not gone ahead. For example, would they have bid for the business? Would they have been likely to purchase some of the assets of the target in the event of liquidation?

¹⁹ OFT Report: *Anticipated acquisition by HMV of 15 Zavvi Stores*, 28 April 2009.

²⁰ During the more detailed CC investigation, however, it transpired that there were no other purchasers that would have bought the business, even if they had been asked to bid. For example, the CC identified one purchaser that had expressed an initial interest in acquiring Millway, but concluded that, had it done proper due diligence on the business, it would not have been likely to make a full bid. Thus, the CC determined that there was no substantially less anticompetitive merger in that case.

4.3 *Whether Failure of the Firm would be a Substantially Less Anticompetitive Outcome than the Merger*

With regards to this third limb of the test, even where the UK Authorities are satisfied that there is no prospect of the business being reorganised or it being acquired in a substantially less anticompetitive transaction, it may be preferable for competition to let the firm fail and for its assets and customers to be re-distributed among the remaining market participants. For example, where evidence indicates that the target and acquirer are likely to be close competitors (via diversion ratio analysis, for example), the UK Authorities will need solid evidence that letting the business fail is not a better outcome for competition. This situation arose in Arcelor/Corus,²¹ where the OFT did not consider that letting the business fail would have been a substantially less anticompetitive alternative to the merger. Post-merger, nine out of Corus' top ten customers switched to Arcelor. The OFT considered that, had the target failed, these customers may have been more evenly spread across the remaining competitors in the market, a substantially less anticompetitive outcome.

In Tesco/Kwik Save,²² the OFT did not believe that the exit of a number of failing grocery stores was a substantially better competitive outcome than the acquisition of the stores by Tesco. Tesco proposed to operate a grocery store from each of the premises, which preserved that store as a local option for consumers. There was no evidence that rivalry between the remaining stores would have produced better outcomes for consumers, and the OFT thus considered the acquisition was not substantially more anticompetitive than letting the stores fail.

Example: Long Clawson / Millway

The CC found that, in the counterfactual, Millway would have been closed in an orderly manner by Dairy Crest to ensure that none of its customers suffered any undue disruption and its remaining customers would have switched to other producers (including the acquirer, Long Clawson). It estimated that, if customers had switched in proportion to the pre-merger market shares of Long Clawson and the one other remaining large Stilton producer, the difference between the increase in Long Clawson's market share and the increase in market share as a result of the merger was small. It also noted that switching was relatively easy and customers were not tied by contract to their existing supplier.

Therefore, the CC concluded that, though there may be a loss of competition following the merger, in particular for those customers which are reluctant to switch or face higher switching costs, this loss of competition was not substantial compared with the situation in the absence of the merger.

5. **Failing Divisions**

The UK Authorities consider that the FFD analysis should apply also to failing divisions, provided companies can prove a division would have exited the market to the requisite evidentiary standard. Divisions of companies can take the form of individual assets (for example, a factory or store), product lines (for example, a brand or product line) or even a whole business within a larger group and the OFT

²¹ OFT Report *Completed acquisition by Arcelor SA of Corus UK Limited's UK hot-rolled steel sheet piling business*, 9 September 2004.

²² OFT Report *Anticipated acquisition by Tesco Stores Limited of five former Kwik Save stores (Handforth, Coventry, Liverpool, Barrow-in-Furness and Nelson)*, 11 December 2007.

and CC have both recently accepted failing division arguments in Homebase/Focus²³ (OFT) and Long Clawson/Millway (CC), discussed below.

Nevertheless, the UK Authorities will require compelling evidence that a division was more likely to be closed than restructured, due to the opportunities for businesses to transfer costs and revenues between divisions of a group. We will therefore assess decisions to close down divisions very carefully, particularly with regard to the question of whether the division would inevitably exit the market absent the merger.

In terms of failing stores/assets, Homebase/Focus was a merger involving hardware stores. The OFT received evidence that property agents had been appointed to sell, or hand back to their respective landlords, failing stores by a certain date. If this was not achievable then they would be closed. The OFT therefore found that these stores would inevitably have exited the market. The OFT also found that the exit of these stores would have removed capacity from the market and led to reduced choice for consumers, which the OFT decided was not a substantially less anticompetitive outcome.

Long Clawson/Millway was a case where the CC accepted that Dairy Crest's stilton cheese manufacturing arm, Millway (the target), was a failing division.²⁴ Millway had been experiencing severe production problems at its plant and had lost several large supermarket customers. Further, aside from one year, it had sustained pre-tax losses every year since 1988. A closer inspection of its accounts revealed that Dairy Crest had written off the full carrying value of Millway's plant on its own balance sheet and Dairy Crest had given it support to allow it to continue trading as a going concern. Finally, analysis revealed that no central costs had been apportioned to Millway and that internal transactions had been carried out on an arm's length basis.

In terms of the likelihood of re-structuring the business, the monitoring trustee appointed by the CC²⁵ in that case reported that either costs would have to be reduced by 45%, or prices increased by 29% (without losing any sales volumes) in order for Millway to break even. Further, the long history of loss-making by Millway, combined with previous unsuccessful attempts by Dairy Crest to restructure the division, led the CC to conclude that there was no chance that Millway could be successfully re-structured. The CC was thus able to conclude with confidence that Millway was a failing division.

6. Appropriate Counterfactual

Whether the FFD should be invoked forms part of the counterfactual analysis of a merger. As noted earlier, a firm's exit must be inevitable for the FFD to be applied by the UK Authorities. Nevertheless, even where the UK Authorities decline to find that exit would have been inevitable, they will consider the competitive constraint the target was likely to have imposed in the future and whether this was likely to be significantly diminished. For example, where a firm is 'flailing', but not 'failing', the fact that it will exercise a diminished competitive constraint going forward will be taken into account. Similarly, the prospect of alternative transactions and restructuring, also considered as part of the FFD, may also be taken into account.

²³ OFT Report: *Completed acquisition by Home Retail Group plc of 27 leasehold properties from Focus (DIY) Ltd*, 12 May 2008.

²⁴ See paragraphs 22 and 29, above, for more details about the facts of this case.

²⁵ In completed mergers, the OFT and CC will often seek interim undertakings to prevent the acquirer from integrating the target into its business. At Phase 2, the CC may also seek to appoint a monitoring trustee, whose responsibility is to monitor and report on the compliance with these interim measures.

In light of the above, the UK Authorities do not consider there to be a justification for including scenarios other than a firm exiting the market into the definition of a failing firm, because these are more easily and cleanly considered at other parts of the competitive assessment.

7. Depth of Analysis

The OFT and CC perform as in-depth an investigation as they can in the time available. The OFT stage is significantly shorter than the CC stage (20-40 working days compared with, typically, up to 16 weeks for the CC to publish provisional findings) and so the depth of analysis that it can undertake (that is, the amount of evidence it can gather and assess) is often less than a longer, in-depth inquiry will allow. Occasionally, this can mean that a merger is not cleared on FFD at Phase 1, but that the CC eventually clears it on FFD at Phase 2.

For example, in Long Clawson/Millway, the OFT's investigations did not result in sufficient, compelling evidence being adduced such that it could confidently rule out the realistic prospect that the target, Millway, could have been re-organised and continued to operate in the market.²⁶ The OFT was also not satisfied there was no realistic prospect of an alternative substantially less anticompetitive buyer being found for the business given the limited number of potential acquirers it surveyed. As the OFT noted, when a company sells to its closest competitor, the OFT will require 'particularly strong evidence that there is no less anticompetitive purchaser available to whom the assets might have been sold.' In light of this, the OFT could not rule out the realistic possibility that Millway would have either remained in the market, or a substantially less anticompetitive merger would have taken place absent the merger.

At Phase 2, the CC took a more in-depth look at Millway's accounts, as well as surveying a number of other potential purchasers of the Dairy Crest business, and satisfied itself that Dairy Crest would inevitably have exited the market and Millway would have organised an orderly closure of Dairy Crest absent the transaction.

8. Policy Considerations, including Failing Firm Counterfactual Analysis in Times of Broader Economic Downturn

8.1 *Harmonisation and Evolution*

8.1.1 *Harmonisation*

The UK Authorities believe that their approach is consistent with that applied by the EC, US and other authorities, with 'inevitable exit from the market' and 'no substantially less anticompetitive alternative' being the key requirements. We think that this consistency is both appropriate and desirable, and reflects the fact that each of these regimes is seeking to answer the same fundamental question, namely: is the merger the cause of the lessening of competition?

A significant number of mergers each year are notifiable (or at least reviewable) in multiple jurisdictions. A consistent approach minimises transaction costs, increases certainty for merging parties and lowers the chances of inconsistent outcomes of merger reviews occurring between member states (which in turn reduces forum shopping). Given the assessment of a FFD is about determining whether there is a causal link between the merger and the exit of an independent competitor (which involves the application of well-established economic principles), the UK considers harmonisation to be both desirable and achievable.

²⁶

It should be noted that Long Clawson did not advance a FFD at the OFT stage.

8.1.2 *Evolution*

Since the introduction of the Enterprise Act 2002 (the Act), and the publication of the OFT's and CC's respective guidelines, the UK Authorities' approach to the application of the FFD has remained fundamentally consistent. Although the wording of the respective authorities' current guidelines differ, the approach taken (in terms of assessing causation) is essentially the same, albeit that the two UK Authorities apply that structural framework in the context of different evidential thresholds. The OFT and CC are presently in the process of jointly codifying their practice and advice on how the FFD is applied in the UK.²⁷

9. **Market Context**

The UK Authorities consider their approach to the FFD is flexible enough to be applied in any industry, regardless of the economic or market context. Since the introduction of the Act, the FFD has been considered by the UK Authorities in a variety of contexts such as supermarkets, local buses, sports retailing, passenger ferries and metal production. The size of these markets has varied from many millions of pounds (*e.g.* metal production) down to markets below £10 million (*e.g.* local buses). The size and extent of markets and their importance to the local economy has therefore not had a material impact on the application of the FFD.

The UK's FFD framework has also proven flexible enough to deal with changes in deal with changing economic conditions, including the current financial crisis. We recognise that markets and circumstances can and do change, and take into account all factors relevant to the particular circumstances of a case. In this way, we aim to assess the FFD in a 'real world' context. For example, access to capital has recently become an increasingly important consideration for firms in the past couple of years as credit and debt finance have become harder to secure.

To the extent that access to capital is relevant and any constraints can be demonstrated to the requisite level, the UK Authorities will take this into account, regardless of whether it is caused by characteristics peculiar to the industry concerned, or by more macro conditions. In *HMV/Zavvi*, the target, Zavvi, had been trading at a loss for a substantial period of time and had a substantial excess of liabilities over realisable assets at the time of entering administration. In order to survive, it would have needed an investment of many tens of millions of pounds. The OFT received evidence from the administrator that a sale of Zavvi as a going concern was not possible for a number of reasons, including the difficulty in raising debt finance in the prevailing economic climate and the prohibitive level of investment required to turn Zavvi around. The low levels of liquidity in funding markets at the time were also a factor taken into account in reaching the decision that Zavvi was a failing firm.

Where a merger takes place in an industry that is declining, there may be evidence relevant to the assessment that is not present in stable industries. For example, where new products will soon either replace or substantially displace existing technology, this will be a relevant factor taken into account in a FFD. However, where an industry's decline is temporary (because, for example, of decreased consumer demand in a recession) caution should be exercised. In certain circumstances it may be possible for assets (even whole divisions) to be mothballed until demand picks up again. The inevitability of exit should therefore be scrutinised closely in such circumstances.

Transactions involving competition for the market and in nascent markets also raise particular issues because these markets are necessarily new and growing and often involve innovative new technologies about which little is known. In these circumstances, it is not uncommon for new technologies to 'leap frog' existing ones before the existing technology has been fully exploited. Nevertheless, the UK Authorities

²⁷ The OFT's draft joint merger guidelines are reproduced at Annex C.

cannot see any reason why the FFD is not equally well adept at dealing with such situations, although we note the FFD (as with many other aspects of such cases) could be harder to prove to the requisite level in nascent markets, given the difficulty in obtaining reliable evidence.

The UK Authorities have not yet had the opportunity to assess a failing firm claim in the context of failing industries or nascent markets, but consider the test and their approach is appropriate and sufficiently flexible to deal with such circumstances.

10. Failing Firm in Times of Economic Crises

As noted earlier, there is no compulsion on merger parties to pre-notify mergers to the UK Authorities and there are therefore no legal barriers to merger parties completing deals and notifying the OFT afterwards (or choosing not to notify and taking the risk that the OFT will choose to investigate the transaction on its own initiative). In light of this, the UK Authorities do not see any justification for relaxing in times of economic crises the substantive or evidentiary standards of the FFD in the UK. We recognise, however, that in jurisdictions where pre-merger notification is mandatory, delaying the completion of a transaction while antitrust approval is being secured can have undesirable consequences for businesses in some circumstances. Nevertheless, the UK Authorities would still be concerned about any relaxing of the substantive FFD analytical standard purely because economic conditions have deteriorated.

Allowing mergers which are intended to rationalise over-capacity in industries, for example, carries with it the danger that, while there may be no immediately observable effect on competition, there may be long term harm. Particularly in industries with high barriers to entry, allowing mergers to concentrate capacity in markets may allow remaining companies to withhold capacity when economies improve and demand increases. Relaxing the FFD to strengthen weakened industries in an economic crisis may have similar results.

Issues are also likely to arise surrounding how such a relaxation of the test is implemented and, more crucially, how and when it is tightened again when economies recover.

Of course, we recognise that there are legitimate reasons why it may be desirable to allow otherwise anticompetitive mergers, such as where they generate efficiencies that will be passed on to consumers, or where public benefits arising from a merger outweigh the competitive detriment. However, we believe that these objectives are better met through their own 'gateways' and are not properly analysed via the FFD. For example, rationalising industry capacity may, in particular circumstances, lead to efficiencies that could justify a merger clearance, provided it can be demonstrated that these efficiencies will be passed through.

11. Mergers between Financial Institutions

The financial services sector is characterised by complex products, information asymmetries and networks which pose challenges for regulators and policymakers. However, these features are not unique and we have not seen any evidence that warrants a different approach to the FFD being taken in mergers between financial institutions, although considerations peculiar to these markets will obviously be taken into account.

The most obvious example of the FFD being considered in relation to financial markets in the UK is the OFT's consideration of the merger between two of the UK's largest retail banks, Lloyds TSB and Halifax – Bank of Scotland (Lloyds/HBOS).²⁸ In that case, the OFT recognised that HBOS was in significant financial difficulties, but did not consider it realistic to assume the UK Government would have let it fail.

²⁸

OFT Report to the Secretary of State on Lloyds/HBOS merger, 24 October 2008.

Nevertheless, in this case the Secretary of State declined to refer the merger to the CC for a more detailed investigation on public interest grounds, namely the stability of the financial system, even though the OFT considered the merger raised competition concerns. In this case, the public benefits were deemed to outweigh these competition concerns.

ANNEX A: RESTATEMENT OF OFT'S POSITION REGARDING ACQUISITIONS OF 'FAILING FIRMS'

1. Introduction and Summary

This restatement publicises the OFT's position regarding its approach to cases where merging parties seek to persuade the OFT that a merger raising competition concerns should be cleared on 'failing firm' grounds, or reasons similar to it.

The following codifies the OFT's position as set out in its existing guidance and decisional practice. It does not constitute new guidance that departs from or relaxes the OFT's basic approach, because the applicable principles are capable of being applied whatever the economic and market conditions.

The OFT considers that consistent and transparent application of the criteria it uses to approach such cases is the best means of ensuring that businesses can continue to assess regulatory risk whatever the economic and market conditions. This statement is designed to assist that process and to confirm that the OFT will provide informal advice (IA) in appropriate cases on the application of the 'failing firm' criteria.

2. OFT's Approach to Analysing 'Failing Firm' Claims

'Failing firm' claims are, in essence, ones that the target business¹ will exit the market without the merger; any harm to competition should therefore not be attributed to the merger. As the substantial lessening of competition, or 'SLC', test requires that the merger be the cause of competitive harm, the OFT has always believed that meritorious 'failing firm' cases should be allowed to proceed relatively swiftly through clearance by the OFT.

Statistically speaking, meritorious cases have been relatively few to date.² However, the fact that the OFT has in practice applied the defence four times under the Enterprise Act 2002 (the Act) suggests the standard applied by the OFT is attainable in practice if the necessary facts and evidence are produced.

For example, the OFT will consider application of the 'failing firm' defence to situations where the target business was not yet in liquidation or administration, subject always to satisfaction of the general criteria by which the OFT assesses this standard.

¹ 'Failing firm' arguments may alternatively apply to the acquiring business. Whether referring to the target or the acquiring business, 'failing firm' arguments may apply to an entire business or to divisions or stand-alone business units (for example, individual retail stores). The term 'target business' is used as shorthand in this restatement.

² The OFT has applied the 'failing firm' defence four times under the Act: (i) *Anticipated acquisition by First West Yorkshire Limited of Black Prince Buses Limited* 26 May 2005 (failing firm defence met in respect of a bus business as a whole); (ii) *Anticipated acquisition by Tesco Stores Limited of five former Kwik Save stores (Handforth, Coventry, Liverpool, Barrow-in-Furness and Nelson)* 11 December 2007 (failing firm defence met in respect of individual local grocery stores); (iii) *Completed acquisition by the CdMG group of companies of Ferryways NV and Searoad Stevedores NV* 24 January 2008 (failing firm defence met in respect of target business); and (iv) *Completed acquisition by Home Retail Group plc of 27 leasehold properties from Focus (DIY) Ltd* 15 April 2008 (failing firm defence met in respect of an individual DIY store).

3. Criteria to Assess Absence of Causal Link between the Merger and any Competitive Harm

The OFT's position on how it approaches the counterfactual – including 'failing firm' claims – is set out in detail in the OFT's existing guidance and decisional practice in this area.³

Where merging parties argue that prevailing conditions of competition are not the appropriate benchmark to assess merger effects because the target business would have exited the market absent the merger in any event, the OFT has explicitly adopted a stringent approach in such cases out of recognition that counterfactuals are easily the subject of self-serving speculation – relatively easily alleged but difficult, given the information asymmetries, to verify independently.

The OFT's duty under the Act (as clarified in *IBA Health v OFT*⁴) to refer a merger to the Competition Commission (CC) for further investigation where the merger creates the realistic prospect of a substantial lessening of competition requires the OFT to take a cautious approach to claims by merging parties that the loss of competition would have occurred anyway independent of the merger. This explains the OFT's requirement for compelling evidence where merging parties present arguments on a counterfactual other than the prevailing conditions of competition (including 'failing firm' claims).

The OFT has made it clear that it will only clear a transaction based on 'failing firm' claims where it has sufficient compelling evidence that all of the following conditions are met.

- Inevitable exit of the target business absent the merger
 - The target business would inevitably have exited the market in the near future. This will often be because the business in question is in a parlous financial situation, even if not yet in liquidation, but may be for some other reason such as a change in the seller's corporate strategy.
 - Having demonstrably explored such options, there is no serious prospect of the target business being reorganised; this takes account of the reality that even businesses in receivership often survive and recover.
- No realistic and substantially less anti-competitive alternative
 - There are no other realistic purchasers whose acquisition of the target business would produce a substantially better outcome for competition. Even if such a purchaser may not pay the seller as high a purchase price or otherwise benefit the target business, the OFT will take into account any realistic prospect of alternative offers above liquidation value.
 - Alternatively, in some cases it may also be better for competition that the target business fails and the remaining players compete for its market share and assets rather than being transferred wholesale to a single purchaser.

The above criteria demonstrate clearly that what is important for the OFT in its merger assessment is not merely that the target business would have exited the market, but also that the merger in question does not result in a SLC compared to other realistic scenarios following exit of the target business.

³ See in particular OFT *Mergers - Substantive assessment guidance* OFT 516 May 2003 paragraphs 4.36 – 4.39 and *Tesco/Kwik-Save and Home Retail Group/Focus*. The issue of the counterfactual will also be covered in the *Joint OFT / CC Substantive Merger Guidelines* which are expected to be published during 2009.

⁴ *IBA Health Ltd v OFT* [2004] EWCA Civ 142.

Moreover, as is its usual practice, the OFT will not treat completed acquisitions more favourably than anticipated transactions for these purposes. The OFT will not let a ‘done deal’ colour its judgment on whether to investigate a transaction not notified to it, and on the substantive questions of whether exit was inevitable and what options other than the merger in question were available. As the OFT and CC decisions in the *Thermo/GVI* case⁵ (involving ‘failing firm’ claims) show, completed mergers may be referred and unwound by the CC in appropriate circumstances. As noted in the CC’s remedies guidance,⁶ costs to the parties of such action are not normally taken into account in determining whether divestment remedies are proportionate.

4. Application of the ‘Failing Firm’ Criteria in Prevailing Economic and Market Conditions

The OFT will take account of prevailing economic and market conditions when assessing evidence put forward by merging parties. A contextual evaluation of evidence will be important in relation to, for example:

- The inevitability of the target business exiting the market because of, for example, cash flow difficulties or an inability to raise capital; and
- The realistic availability of alternative purchasers for the target business as a result, for example, of difficulties in raising investment finance.

However, as a legal and policy matter, the OFT will not, regardless of prevailing economic and market conditions, relax the ‘sufficient compelling evidence’ standard required to demonstrate that a merger between close competitors is not itself the cause of any SLC.

- Although merging parties may find their businesses under financial pressure as a result of changing conditions, their customers may well be in a similar position. Weakening evidentiary standards to allow anti-competitive mergers is likely to bolster operators with market power at one level of the supply chain, only to increase pressure downstream as a result of anti-competitive price increases, or other anti-competitive conduct, resulting from the merger. The creation of, or increase in, market power in UK markets, where this is far from inevitable, will also fail to serve productivity of the UK economy well in the longer term.
- There is no good reason why owners of struggling businesses should be permitted to sell to another close competitor in the market simply because it is prepared to pay the highest price for the target business. Businesses wishing to exit the market must be aware of the implications of choosing to try to sell to a close competitor. To advance a ‘failing firm’ argument, they will need to adduce evidence to demonstrate the absence of any realistic and substantially less anti-competitive alternative purchaser. In terms of execution risk for a deal, the quickest and least risky sale is to a purchaser that raises no competition issues, if such a purchaser exists, even if the price that purchaser offers is lower than that which was offered by a close competitor.
- In situations where the target business is failing and there is genuinely only one purchaser for the business in question, merging parties must be aware that they will need to provide compelling

⁵ OFT Decision: *Completed acquisition by Thermo Electron Manufacturing Limited of GV Instruments Limited* 15 December 2006 and CC Report: *A report on the completed acquisition of GV Instruments Limited by Thermo Electron Manufacturing Limited* (2007).

⁶ CC - 8 *Merger Remedies: Competition Commission Guidelines* (November 2008).

evidence of this to the OFT if they are to avoid a reference to the CC. Mere assertion that this is the case will not suffice.

5. Provision of Informal Advice on ‘Failing Firm’ Situations

The OFT fully appreciates the significance of changing economic and market conditions for firms operating in the UK. In such circumstances, the OFT considers it important to provide assistance and guidance to businesses in terms of their regulatory risk assessments where appropriate. The OFT has this year provided IA on a number of occasions, including in relation to struggling businesses.

The OFT therefore emphasises its willingness to provide IA on the specific issue of whether the target business can be regarded as a ‘failing firm’, provided always that the normal conditions for IA are met – including that the case is a credible candidate case for reference.⁷

However, the OFT notes that the normal limitations that apply to the provision of IA – principally that it is non-binding on the OFT and that its accuracy is wholly dependent on the information provided by the merging parties – are particularly relevant in the context of IA concerning ‘failing firm’ situations.

Specifically, the OFT will rarely be in a position to confirm that there is no realistic and substantially less anti-competitive purchaser for the target business outside the context of a market test involving third parties. It will therefore be more realistic for the OFT to give guidance on whether the sales process anticipated (or conducted) by the seller of the business suffices to provide the necessary evidentiary comfort to the OFT on this point.⁸ Providing IA to the seller alone, or in conjunction with a proposed acquirer, is therefore likely to be more beneficial, all else equal, than an application from an acquirer alone, who is unlikely to have the best-available evidence on the financial situation of the target, and the degree to which less anti-competitive options than the merger have been exhausted by the seller.

⁷ The OFT’s position on when it will provide IA is set out in detail in the OFT’s existing guidance in this area. See in particular OFT *Interim arrangements for informal advice and pre-notification contacts* April 2006 and OFT *Mergers - jurisdictional and procedural guidance - Draft guidance consultation document* March 2008.

⁸ For example in OFT Decision *Completed acquisition by Home Retail Group plc of 27 leasehold properties from Focus (DIY) Ltd* 15 April 2008, the OFT was able to place weight on the fact that the process under which the relevant stores had been offered for sale had been open and involved retailers of many different kinds, including each of the other three national DIY sheds (paragraph 91).

ANNEX B: TEXT OF CURRENT CC MERGER GUIDELINES ON FAILING FIRMS**1. Failing Firms**

3.61 In some cases, whether or not one of the firms merging would fail may be an issue. Where the CC considers that one of the firms would fail then the situation in the market without the merger may be similar to that which would result from the merger, and thus the merger itself may not lead to any significant changes in the extent of competition in the market.

3.62 For a firm to be considered a failing firm, the CC will need to be satisfied that:

- The firm is unable to meet its financial obligations in the near future; and that
- The firm is unable to restructure itself successfully.

3.63 Whether and to what extent the CC will take the failing firm issue into account will depend on various circumstances. First it will need to consider whether any other persons might have acquired the firm, its businesses or any of its assets or wish to do so. A further consideration is how the sales of the failing firm, should it exit the market, will be redistributed among the firms remaining in the market. If without the merger they are likely to be dispersed across a number of other firms, then the merger, by transferring most or all sales of the failing firm to the acquirer may well have a significant impact on competition in the market. In other cases the great majority of sales may be expected to switch to the acquiring firm anyway, in which case the merger may have little effect on competition. In some instances, similar sorts of considerations to those outlined above may apply to situations where it is argued that a division or subsidiary of one of the parties to the reference does not have a viable future.

ANNEX C: UK AUTHORITIES' NEW JOINT DRAFT MERGER GUIDANCE ON FAILING FIRMS

1. The 'Failing Firm' Defence

4.27 One example of a likely and imminent change in the structure of competition arises where one of the merger parties is about to exit from the market on the basis that it is thought to be failing. The Authorities will consider the implications of the inevitable exit of one of the merger firms or of its assets in the context of the counterfactual. Where parties argue that prevailing, pre-merger conditions of competition are not the appropriate counterfactual because one of the merger firms would have exited from the market (because it had 'failed') without the merger, the Authorities will consider: (a) the inevitability of exit of the firm in question; (b) whether there would be a substantially less anti-competitive alternative buyer for the firm; and (c) whether failure of the firm would be a substantially less anti-competitive outcome than the merger. These considerations are discussed below.

2. Inevitability of Exit

4.28 The pre-merger competition conditions may not prevail even if the merger is prohibited if one of the merger firms would have exited from the market in the near future. Typically this issue arises when the firm in question is failing, but it may on rare occasions be for another reason, such as a change in the seller's corporate strategy. In these circumstances, the counterfactual might need to be adjusted to reflect the likely failure or exit and any resulting loss of rivalry.

4.29 The Authorities will look at the facts of the case to assess whether one of the firms would inevitably exit from the market. For instance, it may in some circumstances be inevitable that a firm in a perilous situation or in liquidation would exit, but the Authorities will not always accept that a firm on the verge of administration will inevitably exit from the market. (Given the OFT's 'is or may be the case' standard—see paragraph 2.4 and its footnote—it will require compelling evidence.) Decisions by profitable parent companies to close down loss-making subsidiaries or divisions are unlikely to satisfy the criteria that exit was inevitable, though they may do so in exceptional instances. There must also be no serious prospect of reorganising the business.

3. No Substantially Less Anti-Competitive Alternative Buyer

4.30 Even if exit is inevitable, the Authorities will also consider what could realistically have happened (for the OFT) or would have happened (for the CC) to the assets of the firm that would have inevitably exited. The counterfactual will be based on the Authorities' findings. There may, realistically, be other buyers, whose acquisition of the firm or assets would produce a substantially better outcome for competition than the merger under consideration. These buyers may be interested in obtaining the assets as a means of entering the market. Alternatively, there could be one or more firms already in the market interested in buying the assets.

4.31 The OFT, as a Phase 1 body, will not adopt a counterfactual based on an alternative buyer. Instead, if it cannot dismiss as unrealistic the prospect of a substantially more competitive alternative buyer, it will assess the merger against prevailing or pre-merger conditions. For the CC, at Phase 2, if the counterfactual is treated as being one in which the assets would have been sold to an alternative buyer, it will then compare the competition effects of the merger under consideration against the merger contemplated in the counterfactual.

4.32 When considering the prospects for an alternative buyer, the Authorities will look at available evidence supporting any claims that the merger under consideration was the only possible merger (*i.e.* that there was genuinely only one purchaser for the firm or assets). The Authorities will take into account the prospects of alternative offers above liquidation value. The possible unwillingness of alternative purchasers to pay the seller as high a purchase price or otherwise benefit the target business would not rule out a counterfactual in which there is a merger with an alternative purchaser.

4. Failure of the Firm is not Substantially Less Anti-Competitive

4.33 Even where the Authorities are satisfied that there is no suitable alternative buyer, they will consider whether exit of one of the merger firms (or its assets) and the competition for that firm's market share by the remaining players in the market would be a substantially less anti-competitive outcome than the merger.

UNITED STATES

In the United States, the acquisition of a firm that qualifies as “failing” is not subject to liability under Section 7 of the Clayton Act.¹ The United States Department of Justice and Federal Trade Commission (hereinafter, collectively referred to as the “Agencies”) articulate the rationale for this defence and the framework they use to analyse whether a company qualifies for this defence in our *Horizontal Merger Guidelines* (“*Merger Guidelines*”), which were issued in 1992 and revised in 1997. This defence is also well established in our case law.²

The failing firm defence is narrow in scope and is rarely invoked in court or before the Agencies. When invoked, the defence is rarely successful. It has been upheld in only a few court decisions since 1930.³ Moreover, in light of the strict legal standard, there have been few mergers in which this defence has been proffered and in which the Agencies have accepted it after investigation.

Part I of this submission provides a general overview of the framework the Agencies and U.S. courts employ when analysing the failing firm defence. Part II discusses in detail each of the four requirements for satisfying the defence, as set forth in the *Merger Guidelines*. Part III of the paper addresses a related defence called the failing division defence, and Part IV covers a related consideration involving claims that the merging firm is “flailing” or is a weakened competitor. Finally, Part V of this submission discusses why the demanding standards required to qualify for the failing firm defence should not be relaxed in periods of economic distress.

1. Overview of the Analytical Framework for the Failing Firm Defence

The failing firm defence was first introduced into U.S. jurisprudence by the Supreme Court in 1930.⁴ Pursuant to the case law that has developed since then, our courts will find that the defence applies if two conditions are met. First, the acquired firm must be in a failing condition, which means that it faces “the grave probability of business failure,”⁵ such as when it is in, or is about to enter, bankruptcy or receivership.⁶

¹ 15 U.S.C. § 18.

² See generally ABA Section of Antitrust Law, *Antitrust Law Developments* (6th ed. 2007) 363-68.

³ See, e.g. *Int’l Shoe v. FTC*, 280 U.S. 291 (1930); *Sutter Health; Reilly v. Hearst Corp.*, 107 F. Supp. 2d 1192 (N.D. Cal. 2000); *Culbro Corp. ; FTC v. Great Lakes Chem. Corp.*, 528 F. Supp. 84 (N.D. Ill. 1981); *United States v. M.P. M., Inc.*, 397 F. Supp. 78 (D. Colo. 1975); *Granader v. Public Bank*, 281 F. Supp. 120 (E.D. Mich. 1967); *United States v. Md. & Va. Milk Producers Ass’n, Inc.*, 167 F. Supp. 799 (D.D.C. 1958).

⁴ See *Int’l Shoe v. FTC*, 280 U.S. 291 (1930).

⁵ *Citizen Publ’g Co. v. United States*, 394 U.S. 131, 137 (1969), quoting *Int’l Shoe*, 280 U.S. at 302. In *International Shoe*, in which the Supreme Court first articulated the failing firm defence, the Court seemingly grounded the defence in the avoidance of social costs of liquidation, specifically harm to shareholders of the failing firm and the communities in which its operations were located. This emphasis on social costs was not repeated in the Court’s subsequent *Citizen Publishing* decision. The emphasis on social costs has been repudiated by many as mistaken, in that social costs of liquidation do not necessarily exceed social costs of alternative dispositions. See, e.g. 3 Phillip E. Areeda & Herbert Hovenkamp, *Antitrust Law*, ¶952c at 278 (2009) (“Note that potential conflict is not simply between stockholders on the

Second, the acquired company must have had no other reasonable alternatives to the proposed merger that are less detrimental to competition.⁷

Regarding the financial condition of the firm, it is important to “distinguish between a firm ‘merely’ facing financial distress and a firm whose fundamental ability to compete effectively in the future is in doubt.”⁸ For example, when a firm has valuable assets that should allow it to compete efficiently but has difficulty meeting its financial obligations, or has too much debt, or needs new management and a new business strategy, it may well be able to emerge from its financial trouble as an effective competitor.⁹ “The fact that a firm has been losing money does not mean that it is a ‘failing firm’ in an antitrust sense.”¹⁰ For example, “accounting losses do not necessarily correspond to true economic losses from ongoing operations, especially for firms that have taken on substantial debt.”¹¹

While the precise conditions in the *Merger Guidelines* are articulated slightly differently than in the case law, the analysis of whether a firm is failing is essentially the same. In particular, pursuant to the *Merger Guidelines*, “a merger is not likely to create or enhance market power or to facilitate its exercise, if imminent failure, as defined below, of one of the merging firms would cause the assets of that firm to exit the relevant market.”¹² Importantly, the Agencies’ analysis is forward looking. The four requirements of the failing firm defence are as follows:

- The allegedly failing firm would be unable to meet its financial obligations in the near future;
- It would not be able to reorganise successfully under Chapter 11 of the Bankruptcy Act;¹³

one hand and employees and affected communities on the other. Jobs lost in one community will at least partially be matched by jobs gained in another. Thus, even if the stockholder interest were to be downgraded, the choice would be between one community and another, or (where there is some job loss because of consolidated operations) between a larger number of jobs in one place and greater efficiency elsewhere. There is no reason for antitrust enforcement agencies or courts to become enmeshed in issues of that kind, particularly where there is no warrant for considering any of these factors in the text of §7, except insofar as they pertain to the effect on economic competition.”). In addition, *International Shoe*’s consideration of social costs appears to many as out of step with contemporary antitrust analysis, which recognizes competition as the paramount value served by antitrust laws. *Id.* ¶952c2 at 278 (2009). See also *Anticipating the 21st Century, Competition Policy in the New High-Tech, Global Marketplace, Volume I, A Report by the Federal Trade Commission Staff* (May 1996), at p. 115 (“Others noted that jobs are as likely lost through a merger as through no merger...”), available at http://www.ftc.gov/opp/global/report/gc_v1.pdf.

⁶ See *United States v. Greater Buffalo Press, Inc.*, 402 U.S. 549, 555 (1971); *Citizen Publ’g Co.*, 394 U.S. at 137-38; *Int’l Shoe*, 280 U.S. at 302.

⁷ See *Citizen Publ’g Co.*, 394 U.S. at 137.

⁸ Remarks of Carl Shapiro, Deputy Assistant Attorney General for Economics, Antitrust Division, U.S. Department of Justice, Prepared for Delivery to ABA Antitrust Symposium, *Competition as Public Policy, Competition Policy in Distressed Industries*, May 13, 2009 (“Shapiro Remarks”), p. 15.

⁹ *Id.*

¹⁰ *Id.* at 21.

¹¹ *Id.*

¹² *Merger Guidelines* § 5.0.

¹³ 11 U.S.C. §§ 1101-1174 (1988).

- It has made unsuccessful good-faith efforts to elicit reasonable alternative offers of acquisition of the assets of the failing firm¹⁴ that would both keep its tangible and intangible assets in the relevant market and pose a less severe danger to competition than does the proposed merger; and
- Absent the acquisition, the assets of the failing firm would exit the relevant market.¹⁵

If a firm meets these conditions, it satisfies the failing firm defence and the reviewing Agency will not challenge the proposed transaction. However, these conditions are quite demanding and the defence is construed narrowly. The merging parties must convince the reviewing Agency that the entity to be acquired qualifies as a failing firm. When defending against an alleged Section 7 violation in federal court, this is an affirmative defence that must be alleged in the defendant's answer to the complaint,¹⁶ and the defendant bears the burden of proof.¹⁷

2. Analysis of *Merger Guidelines* Requirements

The four requirements set forth in the *Merger Guidelines* are discussed separately and in greater detail below.

2.1 *Inability to Meet Financial Obligations*

There is no fixed list of conditions that, if present, demonstrate that a firm cannot meet its financial obligations in the near future. This must be carefully analysed and a judgment must be made about the financial health of a company on a case-by-case basis. One of the main factors the Agencies consider when determining whether a firm can meet its financial obligations is whether it has sufficient cash flow. The Agencies also examine whether total liabilities exceed total assets over a period of time¹⁸ and whether a company's costs are greater than its revenues. A decline in sales or even negative current profits, by itself, is insufficient to demonstrate that the firm would be unable to meet its financial obligations.¹⁹ The Agencies also look at the likely ability of the firm to obtain new revenues or new customers and whether the losses are short term and unlikely to be repeated.²⁰ In addition, the Agencies may consider whether the company's productivity is declining, whether its supply of key inputs is being exhausted, or whether it is simply being poorly run by current management.²¹ Further, the Agencies may examine whether a company's financial problems are part of an irreversible downward trend or whether they are more attributable to the general, and temporary, depressed state of the economy. It is also important to consider

¹⁴ Under the *Merger Guidelines*, "[a]ny offer to purchase the assets of the failing firm for a price above the liquidation value of those assets – the highest valued use outside the relevant market or equivalent offer to purchase the stock of the failing firm – will be regarded as a reasonable alternative offer." § 5.1, n. 39.

¹⁵ *Merger Guidelines* § 5.1.

¹⁶ See *Joseph Ciccone & Sons, Inc. v. Eastern Inds., Inc.*, 537 F. Supp. 623, 628 (E.D. Pa. 1982); see also *United States v. M.P. M., Inc.*, 397 F. Supp. 78, 95 (D. Colo. 1975).

¹⁷ See *United States v. Gen. Dynamics Corp.*, 415 U.S. 450, 507 (1974).

¹⁸ See also *California v. Sutter Health Sys.*, 130 F. Supp. 2d 1109, 1134-35 (N.D. Cal. 2001).

¹⁹ See Remarks of Kevin J. Arquit, Director, Bureau of Competition, Federal Trade Commission, Before the American Bar Association, *The Failing Firm Defense and Related Issues*, Apr. 12, 1991 ("Arquit Remarks"), p. 9.

²⁰ See Ken Heyer and Sheldon Kimmel, *Merger Review of Firms in Financial Distress*, Economic Analysis Group Discussion Paper, Mar. 2009 ("*Merger Review*"), pp. 4, 6 (forthcoming in *Competition Policy International*).

²¹ *Id.*

whether the company's pre-merger, ordinary course of business documents reveal an imminent financial failure, or if the claims of failure appear to be invented to help defend the merger.²²

2.2 *Inability to Reorganise in Bankruptcy*

Second, under the *Merger Guidelines*, to qualify for the failing firm defence, the firm must be unable to reorganise in bankruptcy.²³ To determine whether a company can reorganise in bankruptcy, the Agencies consider whether the elimination of the company's debt through the bankruptcy proceeding could correct the company's financial problems. If, for example, the company is unable to meet its current and expected operating expenses from its expected revenues, or capital has been exhausted, reorganisation may not be possible. The Agencies may consider the company's projections for improving its condition and whether the company has a viable plan going forward. In addition, the Agencies may talk to the company's creditors to determine whether they can or will work out a plan to restructure the company's debts. It is insufficient to demonstrate that outstanding bank loans may be called in. Creditors may be willing to restructure loans, or loan additional funds, to keep a company in business if its future business prospects are encouraging.²⁴ Therefore, the Agencies investigate whether the firm has had discussions with its creditors and what the creditors plan to do in the absence of the merger.

2.3 *No Reasonable Alternative Less Detrimental to Competition*

Next, to demonstrate that there were no other reasonable alternatives less detrimental to competition, the *Merger Guidelines* and courts have required a firm to have made a good faith effort to seek "reasonable alternative" offers from other potential purchasers.²⁵ Any offer to purchase the assets of the failing firm for a price above the liquidation value of those assets—the highest valued use outside the relevant market or equivalent offer to purchase the stock of the failing firm—will be regarded as a reasonable alternative.²⁶ If the assets "would likely be purchased by a firm that presents no (or fewer) competitive problems and would continue being employed as an independent competitive force in the market, then the mere fact of

²² For example, in one of DOJ's cases, a firm was found to be failing when the firm suffered heavy losses year after year in the range of \$4 to 5 million per year and the firm never earned a profit. In another case, DOJ found a company likely to be failing because its equipment essentially would cease to operate within a few years, it did not have sufficient funds to purchase new equipment, and it was not likely to find a source to fund that equipment.

²³ By way of background, under Chapter 11 of the U.S. Bankruptcy Code, 11 U.S.C. § § 1101-1116, any company may initiate a bankruptcy reorganization proceeding. Once it files its reorganization petition, the company continues to operate, typically under the control of current management, and is given a wide variety of statutory powers to cancel or renegotiate contracts, use collateral to borrow additional funds, rescale its operations, and modify its debt and equity structure. Creditors may not initiate legal action against the company outside the bankruptcy process. Ultimately, the company will propose a plan of reorganization to keep its business alive and pay creditors over time. The court must approve the plan, and certain debts incurred prior to the filing of the bankruptcy petition will be discharged. The turnaround period may involve years of operation in Chapter 11 reorganization, until an economically viable business can be assured. If no feasible reorganization plan can be formulated, then, under a Chapter 7 liquidation proceeding, the assets of the company may be liquidated by a trustee, and the proceeds distributed pursuant to the priorities set forth in Chapter 7 of the Bankruptcy Code. 11 U.S.C. § § 701-716.

²⁴ *Merger Review*, p. 6.

²⁵ See *Merger Guidelines* § 5.1; see also *Sutter Health*, 130 F. Supp. 2d at 1136 (citing *United States v. Diebold, Inc.*, 369 U.S. 654, 655 (1962)).

²⁶ See *Merger Guidelines* § 5.1 n.39.

current financial distress does not imply that the proposed merger is necessarily benign.”²⁷ This is why the Agencies require the assets to be shopped before determining that a company is entitled to the defence.²⁸

Determining whether a company sufficiently pursued alternative purchasers can be difficult. The solicitation of alternative offers ought to be such as to avoid discouraging any offers above the assets’ liquidation value. For example, an offering solicitation ought not to suggest or imply that bids below a certain level will not be entertained, as this might discourage some bids above liquidation value.

The merging firms, of course, would prefer that their proposed transaction be permitted to go through. The required scope of the shop will depend on the nature and size of the relevant industry.²⁹ The Agencies require the following: that a number and variety of companies be contacted, including investment groups or companies from related industries; that sufficient information be provided to companies expressing interest; and that legitimate expressions of interest be pursued seriously.³⁰ Where an investment bank is retained to conduct the search, the investment banker must be given proper incentives to do an adequate job, and not, for example, be compensated with a share of the merger’s transaction price if no alternative buyer is located.³¹

The burden is on the merging parties to demonstrate that there are no reasonable alternative purchasers less detrimental to competition. It is not the Agencies’ obligation to find another willing purchaser. However, the fact that the Agency, through its investigation, cannot itself find another interested purchaser may be persuasive evidence that the merging firm’s unsuccessful shop was adequate. General expressions of interest from alternative purchasers, without the extension of an actual offer, generally do not constitute reasonable alternative offers.³² The Agencies also may agree to a supervised shop of the assets conducted by a broker over a period of time. If such a shop does not produce an alternative purchaser, and the other elements of the defence are met, the merger may be allowed to proceed.

2.4 *Exiting Assets*

Finally, the *Merger Guidelines* require that, absent the acquisition, the assets of the firm would exit the market. Simply because no alternative purchaser can be found does not imply that the allegedly failing firm would itself liquidate rather than continue to operate the assets in the market of competitive concern. It can be difficult to determine whether the assets would exit the market, in no small part because the evidence often rests largely in the hands of the allegedly failing firm.³³ The company should be able to provide the Agency with objective evidence sufficient to show that it is not more profitable for it to continue to operate the assets in the market than to have them employed elsewhere – such as through liquidation.

²⁷ *Merger Review*, p. 5.

²⁸ *Id.*

²⁹ For example, in one case the Department found that it was sufficient to contact only a few purchasers when the relevant market was small and unattractive to potential purchasers, the allegedly failing firm was not well established, and the firm had never earned a profit.

³⁰ Arquit Remarks, p. 16.

³¹ Arquit Remarks, p. 16.

³² See *Sutter Health*, 130 F. Supp. 2d at 1137; *United States v. Culbro Corp.*, 504 F. Supp. 661, 669 (S.D.N.Y. 1981).

³³ See Arquit Remarks, p. 29.

3. The Failing Division Defence

The *Merger Guidelines* also enunciate a defence for failing divisions of otherwise healthy companies. The requirements of the failing division defence, as articulated in the *Merger Guidelines*, are as follows:

*First, upon applying appropriate cost allocation rules, the division must have a negative cash flow on an operating basis. Second, absent the acquisition, it must be that the assets of the division would exit the relevant market in the near future if not sold. Due to the ability of the parent firm to allocate costs, revenues, and intercompany transactions among itself and its subsidiaries and divisions, the Agency will require evidence, not based solely on management plans that could be prepared solely for the purpose of demonstrating negative cash flow or the prospect of exit from the relevant market. Third, the owner of the failing division also must have complied with the competitively-preferable purchaser requirement of Section 5.1.*³⁴

U.S. courts have recognised the failing division defence,³⁵ noting that limiting the failing defence to an entire firm might unduly limit a company's ability to sell assets associated with a failing business and inadvertently harm rather than protect the competitive process.³⁶

The same basic principles that apply to analysing the failing firm defence apply to the failing division defence as well. However, several additional difficulties arise when analysing a failing division. First, a parent company has discretion to allocate costs among its divisions, which could allow it to cause one of its divisions to appear to be failing when it is not.³⁷ Accordingly, clear evidence demonstrating the division will be liquidated absent the merger is necessary.³⁸ And, as with the failing firm defence, the Agencies insist upon supporting evidence that is not based solely on documents that may have been prepared in order to demonstrate to the Agencies negative cash flow and the prospect of exit. Second, it is difficult to determine the amount of money the parent company can be expected to put into the subsidiary in the future.³⁹ The Agencies will therefore consider whether an independent lender or third-party investor with no incentive to merge anticompetitively with the prospective acquirer would put money into the division with the expectation that it eventually would operate profitably.

4. The “Flailing” Firm or Weakened Competitor

Even if a firm cannot satisfy the rigorous requirements of the failing firm defence, its financial position may still be relevant to determining whether the merger is anticompetitive.⁴⁰ This situation arises when a firm that is “flailing” may not be as competitive in the future as it was in the past. A firm's weakened financial condition may, but will not invariably, indicate that it is unlikely to compete effectively in the future. Where the firm is unlikely to be an effective competitor but for the merger, then it may well be the case that the merger will not substantially lessen future competition.

³⁴ *Merger Guidelines* § 5.2.

³⁵ See, e.g. *FTC v. Great Lakes Chem. Corp.*, 528 F. Supp. 84, 96 (N.D. Ill. 1981); *United States v. Reed Roller Bit Co.*, 274 F. Supp. 573, 584 n.1 (W.D. Okla. 1967).

³⁶ See *United States v. Lever Bros. Co.*, 216 F. Supp. 887, 899 (S.D.N.Y. 1963).

³⁷ Arquit Remarks, p. 23.

³⁸ *Id.*

³⁹ See *id.*

⁴⁰ See Shapiro Remarks, p. 22.

This argument is of course considered since merger analysis is properly forward looking. However, “[f]inancial weakness, while perhaps relevant in some cases, is probably the weakest ground of all for justifying a merger, and certainly cannot be the primary justification for permitting one.”⁴¹ Moreover, as one antitrust official noted, “[a]nyone who seeks to limit competition and pleads financial distress as a justification must make a convincing case that *consumers* will not be harmed by the proposed limitation on competition.”⁴²

U.S. courts have provided guidance for analysing this issue. The Supreme Court first acknowledged in 1974 that a weakened, though not failing, status might affect the competitive impact of a transaction.⁴³ The Court made clear in that case that the merging firm – a coal production company – did not qualify as failing, but that the firm’s lack of coal reserves rendered it a less effective competitor in the future for long-term contracts.⁴⁴ In addition, one court recently noted that, “[a] weak financial condition, or limited reserves, may mean that a company will be a far less significant competitor than current market share, or production statistics, appear to indicate.”⁴⁵ Courts typically consider the financial weakness of a firm “as one relevant factor among many” to be considered when determining whether the merger will substantially lessen competition.⁴⁶

The company’s financial difficulties are “only relevant if the defendant demonstrates that this weakness undermines the predictive value of the government’s market share statistics.”⁴⁷ In other words, the financial weakness must affect its prospects as a future competitor. For example, in the FTC’s 1997 investigation of Boeing Co.’s acquisition of McDonnell Douglas, the FTC determined that McDonnell Douglas’ significance as an independent supplier of commercial aircraft had deteriorated to the point that it was no longer a competitive constraint on the pricing of Boeing and Airbus for large commercial aircraft, even though McDonnell Douglas was not a failing firm. McDonnell Douglas’ decline in competitive significance stemmed from the fact that it had not made the continuing investments in new aircraft technology necessary to compete successfully against Boeing and Airbus, and many purchasers of aircraft indicated that McDonnell Douglas’ prospects for future aircraft sales were close to zero. Staff’s investigation failed to turn up any evidence that this situation was likely to be reversed, and the FTC closed the investigation without taking any action.⁴⁸

⁴¹ *FTC v. Arch Coal, Inc.*, 329 F. Supp. 2d 109, 154 (D.D.C. 2004), quoting *Kaiser Alum. & Chem. Corp. v. FTC*, 652 F.2d 1324, 1339, 1341 (7th Cir. 1981) (internal quotations omitted).

⁴² Shapiro Remarks, p. 19 (emphasis in original).

⁴³ *United States v. Gen. Dynamics Corp.*, 415 U.S. 450, 509 (1974).

⁴⁴ See *Gen. Dynamics*, at 508.

⁴⁵ *Arch Coal*, 329 F. Supp. 2d at 153.

⁴⁶ *Id.* at 157.

⁴⁷ *Id.* at 154. Insofar as a firm’s weakened financial condition generally is associated with poor sales, its weakened condition likely already is accounted for in the firm’s market share. See Phillip E. Areeda & Donald F. Turner, *Antitrust Law* ¶ 935c at 141 (1980).

⁴⁸ See Statement of Chairman Robert Pitofsky and Commissioner Janet D. Steiger, Roscoe B. Starek III and Christine A. Varney in the Matter of the Boeing Company/McDonnell Douglas Corporation, File No. 971-0051, July 1, 1997. Commissioner Mary L. Azcuenaga issued a separate statement, disagreeing, in part, with the majority’s conclusions. See Statement of Mary L. Azcuenaga, File No. 971-0051, July 1, 1997.

5. Failing Firm Defence in a Distressed Economy

There recently has been much discussion as to whether it would be appropriate to relax the requirements of the failing firm defence in a distressed economic situation.⁴⁹ “While there is no theoretical or empirical basis for departing from the basic principles of competition policy during general economic downturns, financial distress at the industry or company level is certainly *relevant* to antitrust analysis... [A]ntitrust enforcement should take account of real-world economic conditions.”⁵⁰ But, because antitrust analysis looks at competition at the industry and company level, the issues considered are in no way unique to a recession.⁵¹ As the head of the Department of Justice’s Antitrust Division recently stated:

*We are likely to see firms consider consolidation to alleviate perceived financial weakness in a distressed economy. A down economy does not change the fundamental analysis, however, which looks to the effects of the merger on competition. We will need to stick to the basics with a clear application of our guidelines to each transaction. For instance, although we may see “failing firm” defences asserted more often, the analysis should be the same as it was before—will the acquisition benefit consumers? Is the acquisition the only way to keep the firm’s assets in the market? When to credit a failing firm defence is just one of the issues we will face in the coming months.*⁵²

Similarly, “[i]f a merger involving a failing firm or division really will benefit consumers by generating cognisable efficiencies, that merger will meet the stringent standards of the failing firm test in the Guidelines.”⁵³ Properly applied, the requirements of the failing firm defence are appropriate even in a distressed economy,⁵⁴ and transactions that do not qualify for the defence “should be blocked in troubled economic times for the same reasons they should be blocked in more ‘normal’ times.”⁵⁵

6. Conclusion

The requirements of the failing firm defence, while strict, are based on sound economic principles. These requirements are designed to permit the merger of a failing firm or division if the outcome would benefit competition. The principles underlying this defence apply equally to healthy and distressed economies. In fact, history has taught that robust antitrust enforcement aids economy recovery⁵⁶ and is essential to a growing and healthy free market economy.⁵⁷ Therefore, while failing firm claims may in troubled economic times be asserted with greater frequency, antitrust analysis of them should not change. This will ensure that antitrust enforcement takes account of present economic realities and prevents those mergers that harm competition.

⁴⁹ See generally *Merger Review*.

⁵⁰ Shapiro Remarks, p. 12 (emphasis in original).

⁵¹ See *id.* at 13.

⁵² Remarks of Christine A. Varney, Assistant Attorney General for Antitrust, International Competition Network–Merger Working Group, Zurich, Switzerland, June 3, 2009.

⁵³ Shapiro Remarks, p. 21.

⁵⁴ *Merger Review*, p. 1.

⁵⁵ *Id.*

⁵⁶ See Shapiro Remarks, p. 11.

⁵⁷ Statement of Christine Varney, Nominee for Assistant Attorney General for Antitrust Before the United States Senate Committee on the Judiciary, 111th Cong. (Mar. 10, 2009).

EUROPEAN COMMISSION

1. Introduction

Council Regulation 139/2004 on the control of concentrations between undertakings (the "Merger Regulation") does not explicitly endorse the failing firm defence. However, according to the Commission's horizontal merger guidelines, *"the Commission may decide that an otherwise problematic merger is nevertheless compatible with the common market if one of the merging parties is a failing firm. The basic requirement is that the deterioration of the competitive structure that follows the merger cannot be said to be caused by the merger. This will arise where the competitive structure of the market would deteriorate to at least the same extent in the absence of the merger"* (para. 89).¹

Thus the wording of the guidelines reflects that the concept of failing firm is in essence a particular application of the legal standard under Article 2 of the Merger Regulation of *causality* between any given merger and any deterioration of competitive conditions in the market that can be expected to occur in the near future.² The critical factor is whether the ultimate market structure without the merger would be essentially no better than that which would result from the acquisition by the prospective purchaser. Therefore, in the failing firm defence, the lack of causality between the merger and any worsening of competitive conditions is at the heart of the analysis; a merger must be at least "neutral" as regards the development of the market compared to a scenario where the merger would not take place.

2. Criteria Relevant for the Failing Firm Defence

In order for a failing firm defence to be accepted, three cumulative criteria are especially relevant as set out by the horizontal merger guidelines: (i) the allegedly failing firm would, in the near future, be forced out of the market because of financial difficulties if not taken over by another undertaking; (ii) there is no less anti-competitive alternative purchase than the notified merger; and (iii) in the absence of a merger, the assets of the failing firm would inevitably exit the market (para. 90). While especially relevant, these factors are not exclusive and exhaustive in establishing that a merging party is a failing firm. Other factors may be equally relevant depending on the circumstances of the case. The burden of proof to establish these criteria lies with the parties.

2.1 Financial Difficulties

Under the first limb of the test, financial difficulties, it has to be demonstrated that the company is unlikely to meet its financial obligations in the near future. Such difficulties are at hand when no shareholder or other financial investor would be willing to provide the necessary capital for the business to remain in the market as a going concern. It is not required that bankruptcy proceedings or similar

¹ Commission Communication, Guidelines on the assessment of horizontal mergers under the Council Regulation on the control of concentrations between undertakings (Official Journal C 31, 05.02.2004, p. 5-18), available at http://ec.europa.eu/competition/mergers/legislation/notices_on_substance.html#hor_guidelines.

² As explained in the horizontal mergers guidelines, "in assessing the competitive effects of a merger, the Commission compares the competitive conditions that would result from the notified merger with the conditions that would have prevailed without the merger" (para 9).

restructuring proceedings have been initiated for this test to be met, but rather that it is *likely* that, absent the merger, the company will enter into such proceedings in the near future. The forms of liquidation and restructuring of businesses vary significantly between the EU Member States. The Commission therefore does not follow a specific formula to assess the degree of financial difficulties but rather makes a case-by-case assessment. The evidence of acute financial distress is measured by reference to the company's balance sheet in terms of profitability, liquidity and solvency. The assessment of these parameters must depend on the industry characteristics. For example in the banking sector, evidence of acute solvability problems confirmed by a central bank may be sufficient as a clear sign of financial difficulties to exist and being material. The time horizon for this assessment will depend on the specific market characteristics.

2.2 *No Less Anticompetitive Solution*

The second limb of the test is that there is no less anti-competitive solution available. This is a matter of making a counter-factual assessment of what the market structure would look like in case of alternative acquirers. Thus, when assessing whether any alternative less anti-competitive solutions are available, one must assess whether there are alternative purchasers available, which would cause a lesser risk of restrictions to competition. Thus, a buyer which is less of a competitive constraint on the failed business would be the preferred option. In this assessment, efficiencies may also play a role; a merger between the failed business and a smaller actual competitor or a new entrant may not achieve the same efficiencies as a large competitor already active in the market.

The more difficult part of the assessment is to ascertain which credible purchasers are willing to buy the failed business and what efforts were made to reach an agreement with these investors. Thus, while not going as far as to require that formal tender procedures are opened, the parties should establish that they have made all efforts to give alternative interested investors an opportunity to enter into negotiations with regard to the acquisition of the failing firm. Timing is of importance in the assessment. The requirement to enter into negotiations with other potential investors should be carefully balanced against time available before acute solvability problems arise.

2.3 *Exit from the Market*

The third limb of the test concerns the question whether the company in financial difficulties would completely discontinue its business and exit the market in the absence of the merger. In other words, it has to be assessed whether the production assets are likely to remain in the market in their current use or liquidated and re-allocated for another more efficient use. The rationale for this part of the test is that the application of the two previous conditions does not address the possibility of a take-over by third parties of the various production assets of the failing firm in the course of bankruptcy proceedings. If these production assets remain in the market, the effects on competition may be similar to (or more beneficial than) the take-over of the entire failed business by an alternative purchaser. It will therefore have to be assessed whether investors would be prepared to maintain the individual assets in their current use or whether they would prefer to re-allocate them for a better use elsewhere. In this connection it would have to be assessed whether such asset transfer would cause short term supply disruptions which are such as to cause more important harm to customers (and ultimately consumers) than the transfer of the business as a going concern. This part of the test has been applied rather strictly and is in general difficult to fulfil.

3. Some Key Examples of Failing Firm Analysis

The first case where a failing firm defence was examined in detail and where a failing firm was found to exist was the *Kali & Salz*-case.³ This case concerned the concentration of the salt and potash activities of Kali & Salz (a subsidiary of BASF) and MdK (a company owned by the former German Democratic Republic (then transferred to a trustee, the Treuhandanstalt)). The merger would give rise to a monopoly in potash fertilisers and there were significant barriers to entry due among others to customer preferences and transport costs. The transaction was nevertheless considered not to create a dominant position (this was before the introduction of the SIEC-test in EC merger control) taking into account, first, that MdK was highly unlikely to survive given that the State trustee was unlikely to be willing to continue to inject any further capital into the loss-making business. Second, records on file clearly showed that despite significant efforts to divest the business, no other third party had made an offer for the company. The potash market was in a state of over-capacity and there was limited or no scope for efficiencies among companies other than Kali & Salz. Thirdly, it could be reasonably expected that, even in the absence of the proposed merger, all of the market share of MdK would go to Kali & Salz.⁴

The only case since the Kali & Salz case where the Commission found that the failing firm conditions were met was the BASF/Eurodiol/Pantochim-case.⁵ This case concerned the acquisition by BASF of two subsidiaries of the SISAS group, Eurodiol and Patoch, both active in the production of various specialty chemicals. The Commission's analysis showed that the merger would lead to a single firm dominant position on several markets with combined shares well above 40%, and there were high entry barriers and capacity constrained competitors. The Commission then examined whether the failing firm defence was met. First, the Commission found that it was clear that both the SISAS group and its subsidiaries were in financial difficulties. The target companies were subject to bankruptcy proceedings under Belgian law. Second, further to the restructuring efforts under the direction of the Tribunal de Commerce of Charleroi no less anticompetitive solution was found as no company other than BASF was willing to make an offer for the business. The Commission also verified in its market investigation that indeed no other buyer was interested.

Third, the Commission also introduced the requirement (and the parties established) that the failing firm's assets would inevitably exit the market in the absence of the merger.⁶ The Commission considered the fact that the supply situation was already tight. Other suppliers would therefore not be in a position to swiftly increase production and thus capture the failing firms' share of sales. Also, the loss of the target's production capacity was unlikely to be made good through capacity expansion at least for a considerable period of time because of costly environmental standards. Finally, the Commission also took into account the importance of existing spare capacity given the economics of operating a capital intensive plant. Thus cost effective new entry would be difficult. On this basis, the Commission found that the deterioration of the competitive structure through the merger would be less significant than in the absence of the merger.

³ Commission Decision 94/449/EC of 14 December 1993 *Kali & Salz*, upheld by the Court in cases C-68/94 and C-30/95, *France and others v Commission* [1998] ECR I-1375.

⁴ This third part of the test expresses the general requirement of causality between a merger and the deterioration: the absorption of a market share reflects that this dupolistic market was expected to deteriorate in a similar fashion absent the merger.

⁵ Case M.2314 BASF/Eurodiol/Pantochim, Commission decision of 11 July 2001.

⁶ This criterion was introduced since, as opposed to *Kali & Salz*, there were more than two main players and competitors could also be expected to gain parts of market shares. The absorption of market share by the merging party was therefore not considered appropriate.

In a more recent case, involving the acquisition of joint control by Johnson Controls and Robert Bosch of the automotive starter battery business of *FIAMM*,⁷ the merger would lead to a SIEC on several markets raising both unilateral and co-ordinated effects. The parties were successful in establishing that the company was in financial difficulties and that there was no other less anticompetitive solution available. As to the first condition, the company was not yet in bankruptcy proceedings. However, the company was overburdened with debt and had posted negative results over the past years. As to the availability of alternatives less harmful to competition, the Commission found that alternative buyers had not been found in the past and that no buyer could be found within a sufficiently short time period to avoid entering into insolvency proceedings under Italian law.

However, the parties failed to establish the inevitable exit of the firm's production assets absent the merger. The Commission acknowledged that the assets would unlikely be maintained in business as a going concern. However, it was deemed possible that individual assets could be bought by smaller firms in the course of the liquidation process and could be brought back to the market within a relatively short period of time. These smaller producers could thus supply the market to a certain extent with the result that customers could be better off in the absence of the merger. The Commission eventually cleared the merger subject to conditions after a general causality assessment (see below).

4. Failing Division

The Commission's horizontal guidelines do not set out specific guidance with regard to failing parts of businesses. However, the distinction to be made between accounting losses and economic losses are even more important in this context, given that there is more margin for manoeuvre to design the balance sheet of an individual division to match the criteria. In other words, it has to be assessed whether the imminent closure of a given business division is the result of a management decision to withdraw from that market or whether there is a real economic failure at stake. Mergers involving individual divisions of an otherwise healthy company therefore merit a particularly careful scrutiny. This question was examined in cases such as *Bertelmann/Kirch/Premiere*,⁸ *Rewe/Meinl*,⁹ and *NewsCorp/Telepiu*¹⁰ where the parties were unable to establish any of the criteria of the failing firm defence.

In these decisions the Commission held that "[i]n such a case of a 'failing-division defence' and not of a 'failing-company defence', the burden of proving that the defence of lack of causality is valid must be especially heavy. Otherwise, every merger involving the sale of an allegedly unprofitable division could be justified under merger control law by the seller's declaring that, without the merger, the division would cease trading."¹¹ While it is not excluded that a failing firm division defence might apply, the Commission's scrutiny will be particularly strict in such cases. To date, in no case have parties been successful in establishing the existence of a "failing division."

5. General Causality Analysis

As the above discussion shows, it is generally difficult to establish that a firm is failing in the above sense. However, going beyond the fulfilment of the failing firm defence, it is important to bear in mind that this defence is a particular application of the general causality test under Article 2 of the Merger

⁷ Case M.4381 JCI/VB/FIAMM, Commission decision of 10 May 2007.

⁸ Case IV/M.993, Bertelmann/Kirch/Premiere, Commission decision of 27 May 1998.

⁹ Case IV/M.1221 Rewe/Meinl, Commission decision of 3 February 1999.

¹⁰ Case COMP/M.2876 NewsCorp/Telepiu.

¹¹ See, e.g. NewsCorp/Telepiu, para. 212.

Regulation. Applying this test means that, even if it cannot be shown that each of these indicative criteria are met, a counterfactual analysis of what would be the development of the market absent the merger could still lead to the conclusion that the deterioration of competition in the market is not a causal effect of the merger. Thus, there may still be good reasons to consider that consumers are not worse off in a merger scenario based on alternative criteria or because the parties provide remedies.

The Commission undertook a thorough counter-factual analyse in the above-mentioned *FIAMM-case* involving a merger between two producers of car batteries.¹² In this case, the parties were unable to show that production capacity would inevitably exit the market; the third limb of the test was thus not fulfilled. As a result, the Commission undertook a general causality analysis and on this basis found that the conditions of competition could not be expected to deteriorate to the same extent in the absence of the merger, even assuming the total liquidation of the target. A counterfactual analysis was therefore undertaken on the basis of remedies offered by the parties, which led the Commission to clear the transaction.

This case illustrates well how the Commission will regularly undertake a thorough prospective analysis of the market conditions and compare different scenarios, with or without the proposed transaction and, where necessary, taking into account remedies. The outcome of such assessment will depend on all factors normally associated with merger control including supply and demand structure, barriers to entry and expansion, customer countervailing buying-power and efficiencies. There are many other good examples of the Commission applying the counterfactual to companies in difficulties such as, *e.g.* in the *Andersen-cases*¹³ or the *Pirelli cases*.¹⁴

6. Other Considerations

6.1 Economic Crisis & Declining Markets

It should be recalled that when assessing mergers the Commission will make a prospective analysis assessing various chains of cause and effect with a view to ascertaining which of them is the most likely outcome.¹⁵ In this connection, a sudden demand decrease of a cyclical or structural kind must be factored into the competitive assessment of cause and effect. The consequence of a sudden demand decrease is that the prospective competition analysis will be more difficult as historic information on market conditions will provide less guidance (an argument which applies similarly in case of rapidly expanding markets).

By contrast, the proposition that a more lenient failing firm test (or more generally a more lenient SIEC test) should be applied in times of recession must be rejected; just as much as the proposition that a tougher test should be applied in good times. The failing firm test is designed to identify those limited circumstances where a firm's assets would exit the market but for the proposed merger. As noted above, a company in financial difficulties but whose production assets' value is greatest in their current use is unlikely to exit the market. Thus, to be less stringent about the exiting production asset criterion and to allow a merger in such scenario would unlikely allow for efficiencies which could counterbalance the competitive harm caused. Therefore, the proposition that the strict criteria for the failing firm defence

¹² Case M.4381 JCI/VB/FIAMM.

¹³ Cases M.2810, DTT/Andersen UK, Commission decision of 20 September 2002; Case M.2824, E and Y/Andersen Germany Commission decision of 27 August 2002; and Case M.2816, E and Y/Andersen France Commission decision of 5 September 2002;

¹⁴ Case M.2574 Pirellia/Edizione/Olivetti/Telecom, Commission decision of 20 September 2001.

¹⁵ Case C-413/06 P Bertelsmann AG and Sony Corporation of America v Independent Music Publishers and Labels Association (Impala), Judgment of 10 July 2008, point 47.

should be softened as they might get in the way of much needed industry rationalisation must be rejected. Finally, as regards the consideration that it is currently difficult to raise capital, this is a matter of factual assessment and does not as such warrant a change of the current approach. For example, less availability of external capital might mean that fewer buyers will present themselves which means that it might de facto be easier for a company to fulfil the "no less anticompetitive solution" criterion.

6.2 *Mergers between Financial Institutions*

With regard to the current particular circumstances on the financial markets, in particular banks, it should be noted that they are characterised by significant externalities. If one bank collapses it may risk bringing down others with it. Thus, as shown by recent events, absent important re-capitalisation (by the state or by private actors), there could be a risk not only of failure of individual banks but also of a *systemic* failure in financial markets. This may cause competitive conditions to deteriorate to an extent similar or worse in the counterfactual, absent a rescue takeover. In particular circumstances, the potential effects of *systemic risks* are therefore a factor that should be taken into account as part of the assessment where required. Thus, where it can be established that the effects of a system failure, if they were to materialise absent the rescue merger, would have at least the same effect on competitive conditions as the merger itself, there is no need for intervention.

It must be stressed however that in order to maintain competitive markets, the strict inevitable business exit criterion must be fulfilled for the defence to be available. For example, it makes sense for a bank to take over another bank in financial difficulties only if that will generate efficiencies. If this is not the case, it is suggested that other means of crisis measures are preferable to rescue mergers. The inevitable business exit test thus distinguishes between banks which are fundamentally healthy and those which are not. It also builds in the efficiencies aspect following the above reasoning. Indeed, recent experience has shown that the preferred option has been to inject capital into individual banks while maintaining their current structure and autonomous commercial conduct.¹⁶ This may be a good illustration of the fact that it simply does not make sense as a matter of crisis measure to combine one or more unhealthy banks.

Against this background, the failing firm defence should be applied strictly independently of short or long term fluctuations in market conditions or industry characteristics.

7. **Concluding Remarks**

So far the failing firm defence has been of limited application in the enforcement history under the Merger Regulation. No particular trend towards an increase of the use of this defence as a result of the economic and financial crisis can be observed. In the financial sector, this is largely explained by the fact that bank failures have been avoided through public recapitalisation efforts. Limited practical experience has therefore been gained with regard to failing firm scenarios. It remains however to be seen whether the financial services sector or other economic sectors will give rise to an increase in this respect. The current framework for the analysis of failings firms is well balanced as it allows for the smooth restructuring of the economy without causing impediments to competition. Loosening the failing firm criteria in times of crisis is therefore not required. Rather, rapidly changing market conditions are taken into account in the competition assessment. The current strict regime should therefore be maintained and applied flexibly to the facts of each case.

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An exception being for example the acquisition by Lloyds of HBOS where, however, the failing firm criteria in the OFT's view were not fulfilled.

ISRAEL

1. Introduction

The failing firm doctrine ("FFD" or "doctrine") is an established defence in Israeli antitrust jurisprudence, yet it is seldom invoked and even when it is relied upon, it is applied only under strict and exceptional circumstances. As in many jurisdictions, merger approvals under the FFD in Israel are quite uncommon – only five mergers were approved based on the FFD. There were other instances in which the merging parties claimed that the FFD applied in their case, but the analysis of the Israel Antitrust Authority ("IAA" or "Authority") found that the conditions were not met in full. As a general rule, the IAA may decide to approve an otherwise anticompetitive merger if one of the merging parties fully meets the strict conditions of the FFD. This doctrine supports the approval of a merger that involves a firm which is facing economic distress and which, for that reason, would inevitably exit the relevant market absent the proposed merger.

It should be noted that the economic crisis does not directly affect the criteria of the FFD or the methodology in which it is being applied. In other words, the substantive merger investigation is conducted without deviation from the general principles which are accepted in Israeli antitrust jurisprudence, and no concessions or exceptions are made in this respect. However, under certain circumstances and according to the timetables and constraints of the relevant legal proceedings, the IAA would be willing to expedite the process and demonstrate flexibility in areas and procedures which do not affect the substantive merger analysis. Recognising the importance of timely decisions in cases that involve firms which are in severe economic distress, significant efforts are allocated to shorten the review period, without compromising on its diligence and professional standards.

Similarly, the size of the market also has a very limited effect on the application of the FFD in Israel. Due to its relatively small size and unique characteristics Israel's economy is generally referred to as a small island economy. The smallness of the market is both in terms of population and land. With about seven and a half million inhabitants, the local market features limited demand and insufficient capacity to accommodate a large number of competitors in various sectors of the economy, particularly with respect to nationwide infrastructures. The island factor stems from a combination of elements, including geographic remoteness from main trading partners; limited degree of trade with close neighbours; language barriers; cultural and historic differences and substantial reliance on foreign trade. Subsequently, and despite the higher openness to trade in recent years, there are still challenges to competition. Israel's small size and relative high entry barriers often make it less attractive to entry by foreign competitors. This results in a significant degree of market concentration in various sectors of the economy. There could be potential implications on the FFD in two different aspects: First, in some cases there may be less potential buyers that could acquire the failing firm, since the pool of interested parties might be smaller. Second, it could be argued that in theory, small economies would tend to be more lenient in applying the FFD in light of the supposedly severe consequences of having a firm exit the market. In practice, however, there is no evidence to support that the FFD has been applied differently in Israel due to the size of the market. As will be explained in the subsequent sections, the application of the FFD in Israel is quite limited and no justifications were found thus far to deviate from the substantive criteria of the doctrine. To this end, the size of the economy is no exception.

This report outlines the main characteristics of FFD in Israel as follows: The first part of the report overviews the developments in application of the doctrine in Israel. It focuses on two cases in which the

FFD was applied by the Authority. The doctrine was never the focus of any Antitrust Tribunal ("AT") decision, and so the common features of the FFD in Israel evolved and were shaped over the years mainly by the IAA Director General's decisions. The IAA is in the process of issuing guidelines regarding the application of FFD for public consultation. The second part of the report outlines the basic themes that are included in the draft guidelines.

2. Developments in Application of FFD

One of the first mergers in which the FFD was relied upon was the merger between "Hashmira" and "Nuriel" in 1997. The two companies were active in the security services market, and the merger was a result of the business failure of Nuriel, which was on verge of economic collapse. The Director General approved the merger in a decision which included a thorough discussion of FFD. The decision set forth the main principles of the doctrine and emphasised that the rationale for approving mergers under FFD is rooted in the lack of causation between the merger and the competitive harm which would follow. It also underscored the rare use of the FFD and the strict examination of its conditions.

The decision portrays the manner in which the FFD is applied in the US and EU. It then sets forth the three cumulative conditions of the FFD under Israeli law, as follows:

- Absent the merger, the failing firm is about to exit the relevant market due to economic failure. Moreover, it has no other alternative of remaining in the market other than the proposed merger;
- There are no other alternative buyers whose merger with failing would create a lesser competitive harm. In this respect, the need for an objective and professional examination of this condition is underscored;
- If the failing firm exits the market, its market share would be transferred to the acquiring company.

In the years following Hashmira - Nuriel decision, two mergers were approved based on the doctrine, but it was only in 2005 where the Director General issued a comprehensive analysis of the FFD in the context of a merger review between "Clubmarket" and "Shufersal" in the food retail market. Shufersal was (and still is) Israel's largest supermarket chain, with a market share of over 30%, while Clubmarket was the third largest chain. The merger took place following Clubmarket's severe economic distress. The merger had clear anticompetitive results, and nevertheless it was approved by the Director General under the FFD.

Compared to Hashmira - Nuriel decision, two issues come to mind as the main developments of the doctrine. The first concerns the FFD third condition according to which if the failing firm exits the market, its market share would be transferred to the acquiring company. In Clubmarket - Shufersal the Director General relaxed the requirement when stating that the condition now focuses on the comparison between the competitive harm caused by the merger and the competitive harm caused by the failing firm exiting the market. Where the merger's competitive result is not worse than the failing firm exit from the market, then the condition is satisfied. In contrast to Hashmira - Nuriel, there is no need to prove that the failing firm's market share will be transferred specifically to the buyer.

The second development regards the possibility of granting a conditional approval to a merger which is being reviewed under the FFD. According to Israeli Antitrust Law, the Director General's authority to impose remedies on a merger depends on the competitive outcome: only a merger which raises a reasonable risk of significant harm to competition may be approved pending conditions. Thus, one might argue that conditions cannot be imposed on merger approved under the FFD, since the merger does not cause a competitive harm. Nevertheless, according to the decision, when taking into account the third

condition (which was just discussed), conditions/remedies may be imposed on a merger where only after fulfilling them is the equation balanced, *i.e.* only the imposition of conditions equalises the post-merger competitive condition with the competitive state of affairs absent the merger.

3. Principles of Draft FFD Guidelines

The IAA is in the process of issuing guidelines regarding the application of the FFD for public consultation. The process included review of past decisions of the IAA and case law, relevant literature and consultations with a number of foreign competition agencies.

The main themes of the draft guidelines could be summarised as follows:

As noted above, the underlying rationale of the doctrine is that the failing firm is in any case expected to cease from being an independent competitive entity. Its certain exit from the market will inevitably bring to a significant harm to competition which is no less than the harm that would result from approving the merger.

When such harm is unavoidable, a merger can no longer be regarded as the only possible cause of harm to competition and hence there would no longer be justification to block the merger. That is so because the harm to competition is generated by the exit of the failing firm from the market due to its unrecoverable economic distress.

The doctrine's point of departure is that a merger which is reviewed under the FFD is likely to result in significant harm to competition. Since the FFD applies when the concern for harm is substantial, all of its conditions need to be satisfied in full. This explains why the application of the doctrine is very limited in Israel as in other jurisdictions.

There is no room to compromise in the merger review process or to turn a blind eye to concerns of harm to competition due to the economic distress of the failing firm. For instance, the role of the antitrust authority may complement the role of the court which oversees the liquidation process. The court is in charge of protecting the interests of the creditors and other relevant stakeholders while the antitrust authority duty is to assure that competition is not harmed and as a result consumers do not bear the anti-competitive costs of the merger. According to the Israeli legislator (Knesset) and Supreme Court, the two functions, *i.e.* protecting creditors' interests and protecting competition, will co-exist without derogating from one another. Therefore, in cases where a merger transaction does not fully comply with the conditions of the doctrine and does not accord with the standards set by the Antitrust Law, it cannot be approved and therefore the creditors are not entitled to potential revenues.

The essence of the first condition is that the acquired firm is about to cease from being an independent competitive entity and that the merger is the only alternative for recovery. This condition has two principal aspects that need to be considered collectively:

The first aspect relates to the current situation of the firm. It must be shown that the acquired firm is indeed failing, *i.e.* about to stop operating in the short run given its inability to pay its debts and commitments. The implications of insolvency, bankruptcy or liquidation proceedings need to be assessed in light of the above criterion. It is not uncommon that firms which enter bankruptcy or otherwise are engaged in legal proceedings due to liquidity problems or even insolvency, continue to operate (and compete) in the relevant market. Therefore, the existence of such proceedings in itself is not necessarily a definite indication that the firm in question is about to exit the market in a near future.

The other aspect concerns the prospect condition of the firm in the future. It must be shown that other alternatives to recover the firm have been considered carefully and no other solution was found, so that the probability of the firm's exit scenario is very high.

According to the second condition of the FFD, as long as there is another alternative potential buyer to the firm, acquisition by which would lead to lesser harm to competition compared to the current buyer, the competitive harm would no longer be considered inevitable and hence the FFD could not justify the merger. Therefore, it is required that the process of seeking alternative buyers would be reasonably thought and in good faith.

An acquisition offer that leads to lesser harm to competition, if any, would always be favoured, even when there is a significant gap between both offers. The threshold which would apply is the value of the firm's assets. Any offer which is higher than the value of the firm's assets would qualify as a viable alternative offer, regardless of how poor it is compared to other offers.

In the absence of an alternative buyer, the third condition requires to demonstrate that the competitive harm associated with the exit of the failing firm from the market is more significant than the harm associated with its acquisition by a competitor.

In order to properly evaluate whether this condition is met, a comprehensive evaluation of competition in the relevant market must be conducted, both static and dynamic. Such an evaluation must include an assessment of the market consequences in the event that the merger is not approved. The Director General is empowered to approve the merger subject to conditions that will mitigate the expected harm to competition, so that in the overall balance, approval of the merger would result in less harm to competition than the alternative of having the merger blocked.

RUSSIAN FEDERATION

The Failing Firm Defence is not stipulated by the Russian competition legislation.

The Federal Law №135 “On Protection of Competition” (hereinafter – the Law on Protection of Competition) of 26.07.2006 establishes general criteria for decision making on approval of transaction submitted in notification.

Thus, according to the point 5 part 2 article 33 of the Law on Protection of Competition the FAS Russia can decline transaction if the transaction could lead to the restriction of competition, including in a result of creation of enhancement of dominant position.

Under consideration of the notifications (pre-merger or post-merger) the antimonopoly authority performs analysis and assessment of competition environment on the relevant product markets, and makes a decision in accordance with the results of conducted analysis.

If it is stated that transactions can lead to restriction of competition the antimonopoly authority can satisfy such transaction together with issuing the instructions on carrying out of activities aiming at competition ensuring.

The criteria based upon the article 13 of the Law can also legitimate the transaction. The transaction could be approved if it does not create an opportunity for individuals to eliminate of competition in the relevant product market and at that no restrictions will be imposed on the participants and other parties as well as if they result or can result in:

- Perfection of production, sale of goods or stimulation of technical, economic progress or raising of competitive capacity of the Russian goods in the world market;
- Obtaining by consumers of benefits (advantages) which are proportionate to the benefits (advantages) obtained by the economic entities in the result of actions (inaction), agreements and concerted practices, transactions, other actions.

In 2008 the Federal Antimonopoly Service of the Russian Federation considered several transactions on capital purchase that occurred due to complicated situation on the Russian financial market.

Such transactions include, in particular, acquisition by the Vneshekonombank (Russian development bank) over than 95% of the voting stocks of the JSC JSCB “Svyaz’-Bank” and over than 90% of the voting stocks of the CJSC “GLOBEKS BANK.”

At the same time the rule of “Failing Firm Defence” was not applied when considering these transactions, and the decision on approval of purchase of shares of these credit companies was adopted under the fact that transactions mentioned in application could not lead to restriction of competition without distinction of financial situation of the JSC JSCB “Svyaz’-Bank” and the CJSC “GLOBEKS BANK.”

It should be noted that in the Russian Federation the special Federal Law №175-FZ of 27.10.2008 “On additional measures for strengthening stability of the banking system during the period till December, 31, 2011” was accepted.

This Law establishes special rules for stocks acquisition (shares of authorised capital) of credit companies in accordance with the measures on prevention of bankruptcy of banks that are parties of system of obligatory insurance of deposits of private persons with banks of the Russian Federation.

Particularly, it is specified that gaining of a preliminary approval of the Bank of Russia for bank's stocks (shares) purchase as well as the FAS Russia's approval for transactions with stocks (shares) by those investors who buy stocks (shares) in accordance with the project participation of state-owned corporation “Agency on deposit insurance” in order to prevent banks bankruptcy is not required.

Within the frameworks of implementation of this Law several transaction on the stocks purchase were concluded without preliminary approval by the FAS Russia, such as: the credit company JSC “Alfa-Bank” bought the Bank “Severnaya kazna” (JSC) which is the largest bank in the Urals.

SOUTH AFRICA

The failing firm defence is set out in the South African Competition Act under Section 12A (2). This section identifies the factors that form part of determining whether a merger is likely to substantially prevent or lessen competition, and includes as subsection (g) *“whether the business or part of the business of a party to the merger or proposed merger has failed or is likely to fail”*. The following subsection (h) further indicates that the evaluation should include whether the merger will result in the removal of an effective competitor.

There have been several mergers evaluated by the South African competition authorities where the failing firm defence has played a role and two decisions by the Competition Tribunal in particular where the issue was material to the decision. We discuss each of these two decisions pertaining to large mergers briefly below.

It should be noted that there have not been significant South African decided cases, where this factor has been important since the global financial crisis began, although such cases are anticipated.

1. Large Merger of Iscor Limited and Saldanha Steel (Pty) Ltd, case no. 67/LM/Dec01

This was the first merger where the failing firm consideration came into play and, as such, the Tribunal set out how it proposed approaching the evaluation, including a review of literature and a discussion of the approaches in jurisdictions such as the US, Europe, Australia and Canada. The Tribunal distinguished between where the acquiring firm gains the market share of the target if the latter exited the market (as in the EU), and the lower threshold of the failing firm’s assets exiting the market absent the transaction (as in the USA). The importance of evaluating whether there were other buyers for the firm’s assets was also emphasised.

The Tribunal further noted that, rather than being a ‘defence’ for an otherwise anti-competitive merger, the failing firm consideration is one factor amongst all the others that must be taken into account when evaluating a merger. This means there is greater flexibility in evaluating the different factors, for example, in taking into account the investment decisions which an acquirer might make.

In applying the test in South Africa, the Tribunal concluded that a merger would not be regarded as lessening competition if it satisfies the more stringent EU test. However, where it falls short of the test that the market share would go to the acquirer in any event but the assets would exit the market (the USA test), the failing firm consideration would still be relevant but weighed up against the likely anti-competitive effect, and taking into account the imminence of failure. The absence of no less an anti-competitive alternative also has to be demonstrated. And, overall the onus rests on the merging firms.

In this Iscor - Saldanha merger, one JV partner was acquiring sole control. The other partner was the state-owned Industrial Development Corporation. The plant had been subject to many problems from the outset and was making substantial losses with little prospect of turnaround without major further investments required. The plant had been targeted at the export market, both by its location and due to a condition placed on its operations so that it would not impact on the local market of Iscor, the supplier of more than 80% of flat steel to the South African market. Alternative buyers had been sought, and evidence was presented about the efforts undertaken in this regard.

The merger was therefore approved on 4 April 2002. It is notable that following a costly relining of the furnace in 2001/2002, and under a 100% Iscor ownership, Saldanha exceeded its design capacity for the year to June 2003.¹ Indeed, the rapidity of the improvement in Saldanha's operations caused the realisation of R2.6bn of goodwill by Iscor in 2002, reflecting the reversal of a negative provision made at the time of acquisition to take account of the difference between the net asset value of Saldanha and the cost of the shares acquired.²

2. Large Merger of Phodclinics (and others) and Protector Group Medical Services (and others), case no. 122/LM/Dec05

This merger was of two hospital groups, and involved the acquisition of the second largest hospital in a particular area by a group including the largest hospital and, in these terms at least, was anti-competitive. The Protector Group was already in liquidation at the time of the merger.

The case turned on the tests as to when a firm is deemed to fail, and the alternatives if it does indeed fail. The Tribunal found that despite extensive attempts by the liquidator there was no other satisfactory offer. While the higher EU test was not satisfied, as there were other hospitals in the area, experienced staff and specialists were being lost to the extent that operational expertise and a substantial capital injection were both required for the assets not to, in effect, be degraded.

At the time of the Tribunal hearings, there were intervening parties who now wished to buy Protector and had previously submitted unsatisfactory bids, which had been dependent on the main financier increasing its exposure (that it was unwilling to do).

In addition, the Tribunal found that the anti-competitive harm was likely to be low due to a range of factors including that there is countervailing power with the medical schemes in national negotiations, the impact of the likely increased tariffs will be low, and that the new investment to be made will be of great benefit to the hospital offerings in the area.

3. Summary

The main challenge in these cases has been ascertaining whether the assets will in fact exit the market, and whether the market share of the target would absent the merger be taken by the acquirer. At the same time, the need for new investments to be made timeously for the recovery of the targets was important in these cases, and was evaluated as part of the overall consideration of the likely effects of the mergers in question.

¹ Iscor, Audited Results Presentation for the year ended 30 June 2003.

² See note 2 to the Audited Group Financial Results for the year ended 30 June 2002.

CHINESE TAIPEI

1. Introduction

The definition of a failing firm is to be found in the Guidelines on Handling Merger Filings. This report will address the definition of the failing firm defence, illustrate FFD by taking the domestic department store market and incinerator market as examples and explain Chinese Taipei's position on mergers between financial institutions involving the failing bank.

2. Definition of the Failing Firm Defence (FFD)

In order to accelerate the review process for mergers, the FTC issued the Streamlining Review Procedure for Mergers on June 9, 1993 and included mergers where "one of the merging parties is a failing enterprise" to be subject to the streamlining review procedure. The reason was that this type of merger possibly does not create, enhance, or facilitate the exercise of market power.

However, a failing firm is not precisely defined in Chinese Taipei's Fair Trade Act and related regulations. Thus, the FTC has determined whether an enterprise was qualified as a failing firm on a case-by-case basis. In response to the 2002 amendments to the Fair Trade Act, the FTC decided to abolish the Streamlining Review Procedure for Mergers on January 17, 2002.

To accommodate industrial restructuring and satisfy the needs of the current economic environment, the FTC referred to foreign merger guidelines and promulgated its Guidelines on Handling Merger Filings on July 6, 2006. With regard to the merger filing suspicious of carrying obvious anticompetitive effects, the filing enterprises shall present the relevant factors related to the overall economic benefits from the merger to the FTC for its deliberation. The FTC would then determine whether the overall economic benefits of the merger outweigh the disadvantages resulting from its restraints on competition. One of the overall economic benefits under the Guidelines with which the FTC is concerned is "one of the merging parties is a failing enterprise."

Pursuant to Subparagraph 3 of Paragraph 13 of the Guidelines on Handling Merger Filings, a failing firm is defined as follows:

- It is unable to pay back the debt within a short period;
- It does not have any other less-restrictive means than merger to be able to survive in the market; and
- It will inevitably withdraw from the market if it cannot merge with other firms.

3. Type and Quantum of Evidence

Before 2006, the FTC did not have a clear definition or criteria for a failing firm. Only after the promulgation of the Guidelines on Handling Merger Filings in 2006 did the FTC have a specific provision regarding the definition of a failing firm. However, the FTC has not published other regulations relating to the definition of a failing firm, and does not have a quantified standard for identifying a failing firm, nor

has it established ways of responding to a failing firm defence. Thus, the FTC determines whether an enterprise was qualified as a failing firm on a case-by-case basis.

4. Selected Merger Cases

4.1 Case 1: Merger between Chung Hsin Electric & Machinery and Weiyu Technology

Chung Hsin Electric & Machinery Mfg. Corp. Ltd. (hereinafter “Chung Hsin Electric & Machinery”) intended to acquire 100% of the shares of Weiyu Technology Co. Ltd. (hereinafter “Weiyu Technology”) in December 1995. Chung Hsin Electric & Machinery’s annual sales volume of 12.2 billion New Taiwan Dollars (NTD) in 1994 had exceeded the threshold amount publicly announced by the FTC. Thus, it filed an application to the FTC for merger approval.

Since the merging enterprise, Weiyu Technology, had a paid-in capital of NTD 40 million, and its accumulated financial losses until the end of 1994 had reached NTD 34.17 million, it qualifies as one of the merger types being “one of the enterprises in the merger is a failing firm” under the Streamlining Review Process for Mergers. Thus, the FTC applied a streamlining procedure to deal with this case.

After review, the FTC resolved that the impacts of the merger on the concentration or competition in the incinerator market and relevant markets were limited. After the above-mentioned merger, the merged parties would be more competitive, and there was no obvious restriction on market competition. Thus, the merger was approved.

4.2 Case 2: Merger between TSMC and Texas Instruments-ACER

Taiwan Semiconductor Manufacturing Company Limited (hereinafter “TSMC”) intended to purchase from Acer Inc., its affiliate, and China Development Industrial Bank, respectively, 23% and 7% of shares issued by Texas Instruments-ACER Inc. (hereinafter “Texas Instruments-ACER”), and acquire 4 of 9 seats on the board of directors and 1 of 3 seats on board of the supervisors of Texas Instruments-ACER. In addition, the sales amount after the merger of TSMC and Texas Instruments-ACER in the previous fiscal year (1998) was going to exceed the threshold amount; thus, TSMC filed a merger application to the FTC for approval in June 1999.

The merging enterprise, Texas Instruments-ACER, specialised in the production of IDM-type IC of DRAM-related products and had a continuous loss of more than NTD 10 billion in the past two years. However, according to the statistics compiled by the Electronics Research Laboratory of the Industrial Technology Research Institute, the Ministry of Economic Affairs, Texas Instruments-ACER was still the fourth largest IC manufacturer in Chinese Taipei in 1997. Besides, even though Texas Instruments-ACER was downgraded to being the tenth largest manufacturer in 1998 due to the low DRAM price, the business of the global IC product market was recovering gradually.

In judging whether Texas Instruments-ACER was a failing firm and the Streamlining Review Procedure for Mergers would be applicable to such a case, the FTC noted that there was no clear definition for a failing firm and this type of merger should be evaluated under the criteria of whether it would possibly will not create, enhance, or facilitate the exercise of market power.

As a result, this case was subject to substantive merger review. The FTC resolved that the merger might cause significant disadvantages resulting from its restraints on competition in the relevant market. However, the FTC found that the overall economic benefits of the merger outweighed those disadvantages and an approval was granted.

4.3 Case 3: The Merger among Uni-President, Tainan Spinning, Nanfan Enterprise, and Wang Computer-Taiwan

Uni-President Enterprise Corporation (UPEC), Tainan Spinning Co. Ltd., and Nanfan Enterprise Co. Ltd. acquired more than one third of the shares with voting rights of Wang Computer Co. Ltd., Taiwan (hereinafter “Wang Computer-Taiwan”) in 1993. The foreign shareholder of Wang Computer-Taiwan and Qware Systems, Inc. (hereinafter “Qware Systems”), Wang Computer Co. Ltd., US (hereinafter “Wang Computer-US”), had filed for reorganisation with the US Federal Bankruptcy Court on August 18, 1992 and was under the protection of the Bankruptcy Law. Besides, Wang Computer-US owed a large amount of debts to Wang Computer-Taiwan; therefore, Wang Computer-Taiwan and Qware Systems were both under an operational and financial crisis. Later, by means of a debt and equity swap, Wang Computer-Taiwan recalled 69.3% of its shares from Wang Computer-US and acquired 51% shares of Qware Systems.

Since Wang Computer-US, the controlling company of Wang Computer-Taiwan and Qware Systems, suffered from the financial crisis, Wang Computer-Taiwan and Qware Systems both lost a lot of customers. In addition, Wang Computer-US still owed debts that exceeded 1.55 times Wang Computer-Taiwan’s capital. Thus this merger involved a failing firm. The FTC found that if the merger were prohibited, it might have a negative impact on relevant companies, affiliated parties, and the domestic information industry. Thus, the FTC approved the merger among UPEC, Tainan Spinning, Nanfan, and Wang Computer-Taiwan.

4.4 Case 4: The merger between Shin Kong Mitsukoshi Co. Ltd. and the Department Store Division of China Rebar Co., Ltd. (i.e. IDÉE fashion store)

China Rebar Co., Ltd. (hereinafter “Rebar”) intended to transfer the operations and assets of its Department Store Division (*i.e.* IDÉE Fashion store) to Shin Kong Mitsukoshi Co. Ltd. (hereinafter “SKM”). After the merger, SKM and Rebar’s annual sales amount in the previous fiscal year were found to exceed the threshold amount. Thus, SKM and Rebar filed a request for merger approval with the FTC in May 2008.

Rebar filed with the court a request for reorganisation in 2007 as a result of its own financial crisis. Article 282 of the Company Act states, “where a company which publicly issues shares or corporate bonds suspends its business due to financial difficulty or there is an apprehension of suspension of business thereof, but there is a possibility for the company to be constructed or rehabilitated, the company or interested parties may apply to the court for reorganisation.” Paragraph 2, Article 211 of the Company Act states that, “subject to the provisions set out in Article 282 of this Act, in case the assets of a company are insufficient to set off its liabilities, the board of directors shall apply to the court for pronouncement of its bankruptcy.” Thus, in case the assets of a company are insufficient to set against its liabilities, it may follow the above-mentioned procedure and apply to the court.

Regarding the reorganisation application, the court has the right either approve or reject it. The FTC may refer to the court judgments in determining whether the merging enterprise is a failing firm which meets the condition “not able to repay its liabilities in a short term.”

Rebar encountered financial difficulties in 2007 and its petitions for reorganisation to the court were rejected twice in the same year. This resulted in the IDÉE fashion store’s having difficulty in dispatching funds and having to provide cash payments to suppliers every 10 days. If the IDÉE fashion store continued to operate, it might not be able to repay the accumulated debts in a short term.

The FTC concluded that SKM would take over the IDÉE fashion store’s operations and assets after the merger. The IDÉE fashion store could thus operate regularly and would not exit the relevant market. In

addition, more than 820 employees of the IDÉE fashion store of Rebar could also retain their jobs. The branded product suppliers in the upstream market could continuously supply products for sale should the IDÉE fashion store operate stably. In its decision, the FTC concluded that the IDÉE fashion store of the Rebar was a failing firm. In considering that the overall economic benefits of the merger outweighed the disadvantages resulting from its restraints on market competition, the FTC did not prohibit this merger.

5. Market Context

Although the Guidelines on Handling Merger Filings has provided a definition of a failing firm, this Guideline has not further identified whether or how the FTC will take into account the factors of product development in a specific industry, the economic cycle, the nature of interactive competition, and the nature of the capital market when deciding mergers involving FFD. However, the impacts on relevant markets and the economy in Chinese Taipei shall also be reviewed in the analysis of the overall economic benefits in an actual case. For instance, in the Chung Hsin Electric & Machinery case, even though Weiyu was deemed to be a failing firm, the impacts of the merger on the incinerator market were also considered. The FTC approved the merger for there were no obvious restrictions on market competition.

6. Mergers between Financial Institutions

Pursuant to Article 62-4 of the Banking Act, Article 13 of the Financial Institutions Merger Act, Article 19 of the Financial Holding Company Act, and Article 149-7 of the Insurance Act, the financial competent authority shall take emergency measures if necessary. In addition, if such a measure does not have any materially adverse effect on the competition in the financial market, an enterprise is exempted from applying to the FTC for an approval in accordance with the Fair Trade Act.

The FTC discussed the exemptions from the Fair Trade Act for mergers between financial institutions at its Commissioners' meeting in June 1998. The FTC resolved that emergent mergers between banks are often mandatory, remedial, and non-voluntary in nature, which differs from regular bank mergers. The main objective is to help problematic financial institutions and maintain financial market order.

In reference to foreign empirical studies, it is generally accepted that a failing firm could be used as a legal defence against a violation of competition law. Thus, a less stringent reviewing standard is often applied to mergers involving a failing bank, while such mergers shall still be subject to the competition law. The FTC respects the decisions of the financial competent authority in implementing necessary measures for failing financial institutions under emergent conditions; however, the FTC recommends that the financial competent authority consider market competition factors when stipulating provisions for exemptions under the Banking Act.

Pursuant to statistics compiled by the Banking Bureau of the Financial Supervisory Commission, there are more than 40 local banks and 30 foreign banks in Chinese Taipei. The domestic market for financial business is moderately or lowly-concentrated. Thus, mergers between financial institutions do not give rise to significant anticompetitive effect on competition. Therefore, FFD asserted in a review of merger between financial institutions has not provoked much controversy in Chinese Taipei.

BIAC

1. Introduction

The Business and Industry Advisory Committee (BIAC) to the OECD appreciates the opportunity to submit these comments to the OECD Competition Committee for its roundtable on the Failing Firm Defence ("FFD") particularly given the relevance of this topic in the context of the current global economic crisis. It was the subject of an OECD Competition Committee Roundtable in May 1995¹ but it is open to question to what extent regulatory practice in such cases has progressed in dealing with the relatively few FFD cases that have arisen in the meantime. Whilst the existence of a "failing firm defence" was well recognised in 1995 it has been notoriously and no doubt, deliberately, difficult for merging parties to benefit from it. The concern of enforcement agencies to avoid Type II errors in this area is reflected in an approach which seems intended to actively deter parties from seeking to rely on this defence except in the most compelling cases. However, the current economic crisis is likely to present a serious challenge to enforcement agencies seeking to hold this line. There is obviously a significant increase in the scale of bankruptcies, layoffs and bailouts across industries and economies in the light of the widespread instability triggered by the financial crisis. Many anticipate that as industries and economies begin to recover from this crisis there will be record levels of insolvencies and restructurings as the economic winners and losers gradually emerge.

Up to now the response from enforcement agencies in various jurisdictions has generally reflected a level of common concern that the current economic crisis will be used as a pretext to dilute merger control with the failing firm defence seen as one of the potential tools with which to crack the regulatory dam. A number of agencies have issued policy statements in one form or another² that they can see no case for adopting a more lenient approach in their assessment of mergers which parties seek to justify under the failing firm defence on the basis that "the applicable principles are capable of being applied whatever the economic and market conditions".³ BIAC notes that this robust standpoint is reflected in many of the discussion papers contributed by national delegates to this roundtable. This is in rather marked contrast to the expectations arising from various rather more positive public pronouncements by the European Commissioner for Competition Policy over the last twelve months or so.⁴

¹ OECD.Failing Firm Defence, Paris, 2006. Doc.OCDE/GD(96)23.

² For example the Restatement of OFT's position regarding acquisitions of "failing firms". December 2008. OFT1047.

³ *Op cit.*

⁴ Speech given to the Economic and Monetary Affairs Committee of the European Parliament on 6th October 2008. "The Commission is committed to continue applying the existing rules, taking full account of (the) economic environment. That means the Commission can and will take into account the evolving market conditions and, where applicable, the failing firm defence" (Speech/08/498).

Speech given at the 13th Annual Competition Conference of the International Bar Association on 11th September 2009 "As regards mergers, the Commission is continuing to apply the existing rules, taking full account of the economic environment. Our rules provide the necessary flexibility to deal with decisions that require fast treatment such as transactions which are part of rescue operations, in order to enable immediate implementation of those transactions. On substance EU merger control rules allow the commission to take into account the failing firm defence, so the existing merger regulations offer sufficient flexibility to deal with today's situations" (Speech/09/385).

2. Business Concerns

The business community is not looking for "leniency" or a "soft approach" or any "loosening" of the applicable key principles of merger control, let alone any explicit re-writing of the rule book. What is expected, however, is that mergers should continue to be evaluated realistically in the light of the market conditions which currently apply and taking into account that, given the serious disturbance of the economy which has occurred, historical data is likely to be a less reliable guide to future outcomes. Otherwise the risk is increased of Type I errors with businesses which could have otherwise survived the current economic crisis being unnecessarily lost with all of the wider economic consequences (*e.g.* loss of innovation employment and skills) which that would entail.

Business also has other more prosaic concerns. What is needed is a review system which can assess failing firm cases sufficiently quickly to reduce the risk of the firm actually failing and the transaction in question becoming moot. This need for speed also drives the need for some clarification of key FFD ingredients such as:

- What constitutes “failing” in the context of merger control and should it also include so-called “flailing” firms?
- At what point should the burden of proof transition from the parties to the enforcement agency?
- What should be the standard of evidence required?
- Are divisions or businesses covered or only standalone enterprises?⁵
- Should it make a difference if the failing company/business is in a declining industry?
- Can the failing company/business be either the acquirer or the acquired?

The existing tests are seen as notoriously elusive and difficult to satisfy which as a minimum raises a doubt as to whether they are fit for purpose in the current unprecedented environment. From the perspective of business there is uncertainty as to what would pass or fail under the current tests and in the view of BIAC this needs to be addressed and quickly.

Above all there needs to be transparency and consistency in the application of the applicable rules and across all jurisdictions on a convergent basis. Disparate treatment will only result in further economic instability and market disturbance in what is, after all, a global economic crisis. This would be the consequence of jurisdictions taking either a particularly strict or an unduly lenient approach.

This paper briefly reviews existing failing firm defence policies and key issues such as the burden of proof and the counterfactual analysis before considering the impact of the current economic crisis and possible alternative approaches.

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The Principles of German Interpretation of Market Dominance in German Merger Control issued by the Bundeskartellamt in 2005 Rules explicitly exclude divisions or businesses from the ambit of FFD though it is understood that this stance is currently under review.

3. Existing FFD Policies

As explained in the Background Note by the OECD Secretariat⁶ the criteria under which a failing firm defence will be accepted are quite similar across OECD countries. By way of an example the criteria applied by the European Commission can be summarised as follows:

- The target business would be forced out of the market in the near future because of financial difficulties if not taken over;
- There is no less anti-competitive alternative purchaser; and
- In the absence of a merger the assets of the failing firm would inevitably exit the market.⁷

These criteria have to be applied, of course, on a case by case basis and both the European Commission and other enforcement agencies applying similar tests freely acknowledge the difficulty in doing so. This negative bias reflects an obvious concern that such cases are vulnerable to self serving speculative justifications for not applying the prevailing conditions of competition to assess the effects of such a merger. The enforcement agencies maintain that it is difficult for them to verify such arguments independently and that this requires a heavy evidential burden to be placed on the merger parties.

The Background Note points out, however, that there are a number of differences in the application of the FFD criteria in different jurisdictions. Whilst in certain jurisdictions such as the US and EU there is a clear emphasis on financial difficulties in several others there is a broader focus on wider industry problems, *e.g.* over capacity in declining industries. There are also significant differences in approach to the counterfactual analysis with some jurisdictions,⁸ but not others, requiring the parties to show that the anti-competitive effects of the merger will not be more severe than those that would follow from the reorganisation or restructuring of the failing firm. There are also differences in the level of effort that failing firms are required to make in order to try and find alternative and potentially less anti-competitive acquisition offers.⁹ Other jurisdictions simply investigate the existence of such alternative propositions without a formal requirement on the failing firm to demonstrate that it contemplated, analysed and discarded other options. These differences of approach on key issues cannot be described as trivial.

4. Burden of Proof

As it stated in the Background Note,¹⁰ "The criteria for a successful failing firm defence in all jurisdictions reviewed are very demanding and, consequently, the burden of proof placed on the merging parties is very high". In many cases there will be considerable scope for argument as to whether it would be more economic to liquidate rather than to continue a business particularly given the assumptions that need to be made in any such analysis as to future cash flows, levels of sales, margins and other variables. The issue for business is that in the context of a failing firm there may be relatively little time to conduct

⁶ DAF/COMP(2009)23.

⁷ European Commission. 2004. Guidelines on the assessment of horizontal mergers under the Council Regulation on the control of concentrations between undertakings (2004/C 31/03), p. 90.

⁸ For example the US, UK and Ireland.

⁹ The OFT will take into account any realistic prospect of alternative offers above liquidation value. *Op. cit.* at footnote 2. In the US and Ireland the level of proof required seems particularly wide ranging.

¹⁰ *Op. cit.* at footnote 6.

exhaustive analysis of all possible alternatives before reaching the point at which the directors of the target company are required under applicable legislation or forced by their secured or preferred creditors to cease trading and/or commence insolvency proceedings thereby crystallising a significant loss of value for the owners of the business.

The additional requirement that the parties show that there is no alternative transaction with less anti-competitive effects involves that most demanding challenge to advocacy - the proof of a negative. In this instance it is made worse by the need to assess the competitive effects of not just one merger, which can be difficult enough, but potentially also that of others. That in itself is not generally feasible without entering into detailed discussions with other potential bidders since otherwise the level of information required is not likely to be available in order to conduct the necessary analysis.

In many cases there will be considerable scope for analysis of various scenarios and, indeed, sub-scenarios but at what point should commercial reality prevail taking into account the damage to value which can result from a business being marketed to a number of actual and potential competitors not to mention the resources and time required to conduct such exercises with any thoroughness? If the target business has made reasonable efforts to market itself, having retained appropriate advisers to do so, as opposed to dealing unilaterally with its closest competitor, then arguably it should be unnecessary for the enforcement agencies to "second guess" the outcome of such efforts.

On top of this there is the need under the FFD criteria to show that the target firm's assets will exit the market in the absence of a merger. It is unclear how this hypothetical can ever be established beyond doubt given the possibility of selective acquisition of assets or parts of the business by one or more competitors in the course of insolvency proceedings.

Several agencies refer in their guidelines or policy statements to the need for a high level of evidence in such cases.¹¹ In common law jurisdictions, there is the well known distinction between the burden of proof in criminal cases which is "beyond reasonable doubt", and that in civil cases which is "on a balance of probabilities". It is not clear where "sufficient compelling" evidence fits against this scale but it seems to go beyond the usual standard of evidence in civil cases and therefore should be considered to be onerous. At the end of the day it should be for the Courts to determine what constitutes sufficient evidence in failing firm cases, though, of course, it is highly unlikely that such cases would ever reach a court. In the meantime, it is within the discretion of the regulatory agencies as to what kind of evidence they consider to be sufficient but this is obviously affected by any bias towards avoidance of Type I or Type II errors. In exercising its discretion it is BIAC's view that the enforcement agencies should take due account of and to be prepared to rely to a reasonable extent on the evidence submitted by the parties unless there is substantive conflicting evidence available to them.

5. Counterfactual Analysis

Unlike in other merger cases in FFD merger cases the pre-merger conditions of competition are unlikely to be the appropriate benchmark for assessing the competitive effects. This is because in a failing firm situation the target business would exit the market anyway, and the current market conditions would not continue to hold in the counterfactual. The entire argument consequently relies on establishing the correct counterfactual.¹²

¹¹ The OFT adopts a "sufficient compelling evidence" standard - see *op. cit.* at footnote 2.

¹² www.oxera.com/cmsdocuments/agenda.

The stringent approach adopted by enforcement agencies to this counterfactual analysis has already been noted and in their view is justified by the incentives for a firm to exaggerate the extent of its weakness.¹³ The enforcement agencies may also have in mind that a close competitor may be willing to pay the best available price for a weak competitor to secure market share and on the basis of synergies which may be uniquely available to it and that the FFD should not simply be a means of obtaining the highest price for the target business regardless of potentially anti-competitive consequences.

The burden of proof in identifying the appropriate counterfactual scenario lies with the enforcement agency and this is not easy where, as in failing firm cases, the status quo ante is unlikely to provide a valid approximation of the competitive structure of the affected markets in the absence of the merger. Identifying the most appropriate counterfactual will necessitate investigating the options open to the failing firm to determine which ones represent real possibilities. However in dealing with a firm in financial distress the information likely to be available may be limited and yet choosing one counterfactual scenario against another could well produce significantly different answers. One example is the assessment of the scope for a failing firm absent a merger to linger on for a period under lenient bankruptcy laws offering lower prices in the hope of better days to come compared with the negative consequences of an increase in concentration should the proposed merger proceed. In other words how realistic is it to assume that a failing firm would be able to continue in business without the merger and for how long?

The underlying concern of business is that the unduly stringent application of the failing firm criteria by regulators may block failing firm transactions which are, in reality, the least anticompetitive solution for the failing firm's problems. In such cases is it relevant that the post merger scenario is less competitive than the pre-merger scenario. Is it right that being a financially distressed firm in the market is better for consumers - surely not at least in the longer term. Giving the parties the burden of proof in demonstrating the absence of more competitive alternatives when they do not have the powers or resources of regulators to investigate such issues is clearly burdensome particularly where the standard of evidence required is at the level of "sufficiently compelling". In any case, is it necessarily correct that a market structure where the assets of the failed firm are shared among a number of actual or potential competitors is more competitive? What if the purchasing entities remain minnows less able to compete with incumbent larger players? Merger control is forward looking but the potential competitive effects of a failing firm in a declining industry are particularly difficult to predict with any certainty particularly as in such cases the status quo ante is at best an uncertain guide to future market conditions. In such cases the ambition of the enforcement agencies is inevitably constrained by economic reality and the objective can only be to maintain the highest level of competition in the market post merger as is reasonably achievable in the circumstances rather than trying to preserve the status quo ante. In seeking to achieve this more limited objective the enforcement agencies have access to a tool box of potential remedies which can be used to mitigate any particularly adverse consequences of an FFD merger.

6. The Impact of the Current Economic Crisis

The current crisis is often described as a financial crisis but its consequences are not limited to the financial sector. The ensuing credit crunch has adversely affected most economies and industries globally. The damage caused is structural and may take a considerable period to recover from with recovery unlikely to be a return to the economic situation applying prior to the downturn. Indeed whole industries are facing the need for significant restructuring through forced or voluntary bankruptcy in many cases whilst preserving enterprise value to the maximum possible extent through restructurings which will necessarily

¹³ The (Irish) Competition Authority (2002) Notice in Respect of Guidelines for Merger Analysis page 26.

involve extensive M&A activity. The approach of regulators to failing firm transactions is likely, therefore, be a factor in determining the success of such efforts.

Enforcement agencies need to take into account that in this economic crisis even efficient and competitive firms with excellent products or service offerings, and valuable innovative technology may be facing acute financial difficulties. It is of key importance therefore that the FFD regime does not unnecessarily foreclose the option of firms in financial trouble merging with competitors in order to remain active in their markets. The key consideration in blocking such transactions should be if there is clear evidence that there are less anticompetitive options and those options are indeed realistic.

Another unique feature of the current crisis is that entire industries are in distress on a global scale, *e.g.* the steel industry¹⁴ and the automotive industry. In such cases there is a clear need for greater flexibility and creativity in merger control as a matter of economic necessity notwithstanding the possible increase of entry barriers in such cases and the possibility of downstream mergers as restructuring progresses.

Regulators also need to distinguish between long term decline of industries and a relatively short lived downturn given that mergers result in long term changes to market structure. Equally nobody would argue that competition policy alone is the answer to long term economic crises and there is a range of more flexible tools available to governments to address such issues. However if a merging firm is in financial distress then time is of the essence with "flailing" firms rapidly transitioning to "failing" firms which of itself can make the analysis of potential alternative transactions less relevant. In the current economic crisis the rationale of mergers also needs to be carefully considered in the context of access to funding which would not otherwise be available to the failing firm so that it can continue to invest and innovate and possibly also to pursue dynamic pricing strategies all of which benefit consumers. Consolidation is also a significant response to negative demand shocks.

7. Alternatives

Many firms are likely to find themselves in financial distress when capital markets are tight and the economy is in recession. Merger policy needs to take account of this reality and move, as appropriate, with the times, particularly in the context of the FFD where existing generally applied criteria either produce an undue deterrent effect or may not necessarily produce the most pro-competitive answer.

Enforcement agencies can take a number of practical steps to alleviate some of the problems such as fast tracking failing firm cases, concentrating on testing the business rationale for the merger regardless of pre-existing market conditions and identifying possible remedies which in their view would mitigate the worst anti-competitive effects for the acquiring company to consider.

The current bias towards avoiding type II errors would seem to be based on a presumption that it is preferable from a competition standpoint to retain a handicapped failing company in the market rather than allowing it to merge with a competing healthier company but even if this were correct at least in some cases (which we do not necessarily accept) then this can result in prohibiting mergers which in fact, represent the least anticompetitive option. Hence an overly strict FFD policy may deter efficient mergers from being proposed.

One alternative suggested in the Background Paper is to consider such mergers simply on an effects basis without any presumption that the post-merger scenario is necessarily more harmful than other possible counterfactual scenarios. On this basis a merger would only be blocked if the facts show that it is

¹⁴ "Now, US steel industry asks for government bailout", 2 Jan 2009

likely to lessen competition relative to the level of competition that would obtain under the most likely counterfactual scenarios. The evidential burden on the parties would be to prove that the target firm is in financial distress and that there is a significant risk it will exit the market without the merger. They would also need to produce evidence to allow the likelihood of alternative counterfactual scenarios to be assessed. It will be for the enforcement agency to determine the relevant counterfactual and to weigh the anti-competitive effects of each scenario.

Such an approach would involve case by case factual analysis in difficult circumstances and within tight timeframes and would be inherently less predictable but it would be likely to reduce Type I errors which are likely to become increasingly unacceptable in terms of addressing the structural issues arising from the current economic crisis. However BIAC would find it helpful if, in the course of the roundtable, Dr Jorge Padilla of LECG could further explain this interesting potential alternative approach so that participants can better understand how it differs from what the enforcement agencies would otherwise do in the usual course of a merger review.

8. Conclusions

The review of various jurisdictions as set out in the Background Note confirms that in most jurisdictions the FFD criteria are both strict, strictly applied and as a consequence, rarely used. The Background Note also points that there are good arguments for a less stringent approach to be taken towards FFD in the current economic environment in order to avoid letting efficient firms with products for which there is a significant demand exit the market because of the defective functioning of the capital markets. This cannot be in the best interests of consumers and yet we see in the public pronouncements of various enforcement agencies, and in their submissions to this roundtable, a marked reluctance to contemplate any adjustment to the stringent FFD criteria previously applied in more normal economic conditions.

It can be understood that this strict approach was originally conceived as a deterrent in order to strictly limit the number of cases in which merger control might be bypassed. This objective has certainly been achieved with very few FFD cases arising in any jurisdictions over the last decade. However it should be considered whether this policy of deterrence is still relevant in the current economic circumstances (with potentially many thousands of corporate failures being caused by the defective functioning of the capital markets) or justified on the basis of the actual limited case experience in various jurisdictions. Utilisation of FFD arguments, in most cases, is likely to be a last resort for the parties in any event given the wide discretion which it gives to the enforcement agencies to "second guess" whether the business concerned is actually likely to fail and whether sufficient efforts have been made to find a less anti-competitive purchaser. The picture of a distressed business being effectively marketed by an enforcement agency is not one to commend itself to many Board Rooms.

BIAC is not proposing that the regulatory floodgates should be opened to allow parties to acquire failing let alone flailing competitors. However BIAC considers that the existing FFD criteria are unduly difficult to satisfy and unduly stringently applied and BIAC is concerned that this may be driven by a negative bias rather than by any objective justification that such a stance is required in all such cases in order to avoid a significant lessening of competition.

Competition policy has a positive role to play in helping to resolve the difficulties resulting from the current economic crisis but in order to reduce the harm that it has caused only those transactions which are likely to result in significant adverse effects on future competition should be blocked. Expecting mergers in which FFD arguments apply to have a "neutral" effect on competition at most may not produce the optimum results either in terms of consumer welfare or the wider interests of the economy in what are quite extraordinary times.

It is key that whatever policy is followed should be applied transparently and consistently across all jurisdictions. The number of issues raised in the Background Note and in this paper demonstrates the need for additional guidelines to deal with such cases rather than short restatements of pre-existing policies based on a small number of actual historical cases. BIAC believes that OECD has made an excellent contribution to this requirement through staging this roundtable but further and urgent action would be justified to develop best practice guidelines aimed at reducing some of the current variances and inconsistencies in dealing with FFD cases.

In the meantime in the face of the current crisis BIAC asks each jurisdiction to take full account of the issues with the current approach to the FFD criteria as identified so clearly in the Background Note by applying realistic standards in assessing evidence of business failure, the availability of alternative transactions and the likelihood of exit of the failing firm's assets from the market. Conclusive evidence at least in relation to the second or third criteria may not be fully available even in what is otherwise a meritorious case and accordingly BIAC believes that enforcement agencies should be more prepared to rely to a reasonable extent on the evidence submitted by the parties.

SUMMARY OF DISCUSSION

This roundtable was organised around four main themes:

- What are the FFD standards and elements of proof in general?
- How should competition authorities look at the FFD in times of crisis? Should adjustments be made because of the crisis situation?
- Does the special case of the possible failure of financial institutions require different criteria?
- How do approaches toward the FFD differ among OECD jurisdictions?

Chairman Jenny opened the roundtable by asking guest speaker Dr. Jorge Padilla, Managing Director of LECG Europe, to introduce the FFD and the difficult issues it raises.

Dr. Padilla explained that the FFD provides an exception to allow a merger that would normally be anti-competitive and would result in a reduction of competition. The exception can only be provided (i) if the firm is likely to exit the market absent the merger and (ii) if the post-merger scenario is less anticompetitive than the counterfactual scenario in which the target firm would leave the market.

Three main questions are central to assess whether the FFD should succeed.

First, will the target firm exit the market absent the merger? This requires corporate finance analysis, a good understanding of the restructuring possibilities of the firm under bankruptcy laws and an analysis of the economic and regulatory context in which the firm operates.

Second, are there any less anticompetitive merger solutions? It is not easy to answer this question. Firms in financial distress are often reluctant to shop around as this may bring them closer to collapse. Furthermore, the comparison of one merger against alternative mergers requires that a series of prospective analyses are put together, but even one such prospective analysis is difficult to do.

Third, what would happen to the assets of the target firm once exit has taken place? The assets might all go to the firm that is proposing to be the acquirer. Although this would provide simple answers to a comparison of scenarios with and without the merger, it is unlikely to happen. If the assets would not all be appropriated by the acquirer, the presumption is that the post-merger scenario is likely to be more anti-competitive than the counterfactual. However, this is not necessarily true from an economic point of view.

FFD policies are, like any other antitrust or merger policy, likely to produce Type 1 and Type 2 errors, which refer to false convictions and false acquittals respectively. Policies that are for good reasons aimed at minimising Type 2 errors can nevertheless create bias in favour of Type 1 errors.

Given the limited use of the failing firm defence, Dr. Padilla raised the question whether competition authorities should focus more on the definition of appropriate counterfactuals, rather than spending time and resources on the application of the FFD.

1. FFD Fundamentals

The Chairman mentioned Dr. Padilla's point that requiring a firm to be unable to reorganise in bankruptcy for it to qualify as a failing firm seems to presume that the post-merger scenario is necessarily less competitive than what would happen if the firm emerging from bankruptcy remained independent. The Chairman asked the US whether that is sound economic analysis.

A delegate from the US replied that the condition in the US that a firm should not be able to reorganise under Chapter 11 of US bankruptcy laws requires proof that a firm is really failing. This decreases the margin of error in the application of the FFD compared to other countries in which there is less or no emphasis on the possibilities of reorganisation. Lax FFD standards should not give a safe harbour to firms that otherwise could not have merged.

The Chairman then noted that the EU's contribution summarises the three conditions that are applied to the FFD by the European Commission: (i) the failing firm would in the near future be forced out of the market; (ii) there is no less anticompetitive alternative purchase than the notified merger; and (iii) in the absence of a merger the assets of the failing firm would inevitably exit the market. The contribution furthermore points out that these conditions are not exclusive or exhaustive. The Chairman asked the EU whether competition authorities need special criteria for the FFD or whether a better set of counterfactuals is needed for mergers in general.

The EU first pointed out that the limited use of the FFD in times of economic and financial crisis is partially due to the availability of other policy instruments, including the state recapitalisation of banks. Measures such as Chapter 11, to which the US referred, and state aid in the EU, should be seen as changing the rules of the FFD game and make a counterfactual analysis quite complex. They also make clear that the current crisis presents limits to the strict application of the conditions for a successful FFD and demands flexibility from competition authorities. However, a loosening of the criteria is not required for the same reasons that the defence would not be made stricter in good times.

1.1 *FFD as a Special Case of the General Causality or Counterfactual Analysis*

Another delegate from the EU added that the FFD is a special framework in the general causality test, which in any case requires causality based on counterfactual analysis. However, in addition to the standard merger guidelines, the FFD provides pedagogical value and predictability for companies. A delegate from Spain also recognised the FFD as a particular case of a counterfactual analysis and provided an example of a merger between satellite pay TV platforms in which it took into account, amongst other factors, the weak financial situation of the merging companies.

In reaction, Dr. Padilla pointed out that, although the FFD can indeed be perceived as a particular case of a counterfactual analysis which increases predictability, it should be kept in mind that the burden of proof in both instances is allocated in a very different way, which has significant implications for the conduct of the investigation and possibly on its outcome. In a normal merger investigation, the burden of proof lies on the competition authority to show that the merger is anti-competitive. However, in a FFD-merger, it is the merging parties that have to show that their merger is less anti-competitive than initially perceived.

A delegate from Ireland considered that, because of this inverse burden of proof, merging parties that invoke the FFD are at a disadvantage since they have to admit the existence of a significant lessening of competition. However, at a later point in the discussion, the delegate returned to this subject and argued that the merging parties should carry the burden of proof because they, not the government, are the ones

who are best informed about the market. Their best strategy is therefore to start talks with the competition authority at an early stage.

Dr. Padilla agreed that the burden of proof regarding collection of evidence, including putting forward potential serious alternative offers, should be on the merging parties. This is referred to as evidentiary burden of proof. However, the substantive burden of proof, which deals with the balancing of pro-competitive and anti-competitive effects, should be on the competition authority.

The delegate from Ireland considered the term ‘burden of proof’ to be overplayed, given that the FFD is invoked only after the preliminary determination that there is a significant lessening of competition. Later in the discussion, a delegate from the US pointed out that shifting the burden of proof regarding the collection of evidence to the government is likely to create more errors. In addition, the delegate remarked that allowing mergers that would otherwise not have been allowed may imply ‘paying a price down the road’, which may turn out to be high.

1.2 FFD-Condition: No Less Anti-Competitive Alternative Mergers

The discussion turned to the condition of the FFD that requires that there are no less anti-competitive alternative mergers. The EU’s contribution notes that implementing the FFD criteria is difficult, particularly in times of crisis. The requirement that there should be no less anti-competitive alternative mergers is especially burdensome. On that topic, France’s contribution indicated that only ‘credible offers’ of alternative acquirers will be taken into account to test this criterion. However, the Chairman said, it is not completely clear when an offer is considered ‘credible’.

A delegate from France explained that the credibility of an offer from a potential acquirer increases when it has been submitted to a commercial court as compared to a simple expression of interest in the press. However, it does not mean that any offer submitted to a commercial court is deemed to be credible. An example of this is provided in the SEB/Moulinex case, in which, e.g., some offers were limited to such a small part of the business that they were not considered serious. Later in the discussion, a delegate from Switzerland pointed out that when dealing with bankruptcy proceedings and the comparison of alternative offers, the competition authority does not judge the seriousness of the offers. They leave that task to the merging parties.

A delegate from the UK said that it is common to consider alternative mergers with parties that have submitted an offer with a price above liquidation value. If offers below liquidation value are less anti-competitive than offers above liquidation value, should they be taken into account? Dr. Padilla said that from a competition policy point of view, such offers should not be taken into account. It would mean that merger control is used to allow access to assets at below market prices and hence distort competition.

1.3 No Explicit FFD Policies

A number of countries do not have explicit FFDs. For example, New Zealand relies on their counterfactual analysis in which several situations can be compared, Poland could use a public interest test and Russia has recently introduced a law that exempts financial institutions from going through merger control. The Chairman asked for clarifications of these approaches and whether an explicit FFD would be more valuable.

A delegate from New Zealand explained that following their new guidelines, the Commerce Commission will review trends of cash flows, prospects of restructuring and possible unsuccessful attempts to rescue the firm. A merger analysis will include a comparison of the factual with all likely counterfactuals, even if the focus is typically only placed on the most competitive counterfactual. For instance, in the Southern Cross merger, the Commission concluded that the most likely counterfactual

included Southern Cross hospital staying in the market given recent investment in the hospital and no signs of exit discussions whatsoever.

A delegate from Poland remarked that a flexible interpretation of their public interest test will be sufficient to deal with mergers in which one of the parties is a failing firm. Considering the low number of merger applications relying on such an argument, there is no need to introduce formal FFD guidelines. Dr. Padilla expressed his concerns towards such a public interest test, which may result in a too lenient application of the FFD, especially in times of crisis. It risks leading to too many type 2 errors.

A delegate from Russia explained that his agency does not see the need to introduce any general exemption for merger control rules based on a FFD, either, as it would create a sort of unnecessary safe harbour for companies, which can be abused given the difficulties of correctly detecting whether a firm is failing or not. The Russian law that introduces special rules for the purchase of failing bank assets is an exception to that stance. However, the law is temporary and has been enacted only to address the crisis conditions. As a result of the strict data collection system of the Central Bank of Russia, it is easier to verify whether a bank is failing than an industrial firm. Industrial firms would possess a considerable information advantage regarding their likelihood of failing and hence Russia prefers the continued application of their general merger control rules. The delegate also stated that the rule of reason principle in merger control enables the FAS to make the correct decision. The likelihood of exit is examined under general principles rather than on the basis of an exemption such as the FFD. Later in the discussion, Dr. Padilla pointed out that standard merger control tools can be applied in situations of financial distress, as Russia proposed for industrial firms. However he underlined the fact that competition authorities have to be careful not to apply the pre-merger scenario as the counterfactual, as is done in standard merger reviews, since otherwise this would result in an incorrect assessment of the competitive effects and hence too many Type 1 errors.

1.4 FFD-Condition: Exit of the Firm

The Chairman continued the discussion by enquiring how competition authorities determine whether a firm will exit the market. He referred to the vast experience of the KFTC in applying the FFD, including the KFTC's decision in the Samick/Young Chang merger. In that decision, the KFTC determined that Young Chang had a high potential to turn around despite its financial position at the time of the merger.

A delegate from Korea explained that it is common practice to analyse the firm's financial position, including balance sheet, production capacity and information obtained from investors and shareholders. In the Young Chang case, its financial difficulty was not caused by a comparative disadvantage but by a temporary shortage of liquidity and a labour management dispute. This assessment was proven to be right given the fact that a third firm took over the famous piano maker for a price 5 times higher than that offered by the initial merging party.

The Chairman then raised the question of the timeframe for the exit of a failing firm. Do competition authorities care about both the short and the long term, or is only the short term relevant?

A delegate from Switzerland pointed out that the relatively low frequency of FFD cases may be borne out by the fact that merger notification thresholds are in place and that European countries will see big cases being referred to the European Commission. He then answered that the exit of a firm should be assessed in the short to medium run, which implies less than 2 years.

Dr. Padilla replied that from an economic point of view, only the very short term should be taken into account, mainly because otherwise the conditions of urgency, which justify the exception, would be absent.

At a later point in the discussion, a delegate from Turkey indicated that only the very near future is taken into account in Turkey to assess a firm's potential exit as several factors are variable and thus unpredictable in the medium and long term. Moreover, for the Turkish Competition Authority (TCA), it is sufficient that there is a strong likelihood that exit will take place in the short run and the presence of reliable financial evidence implying that the firm in question will not be able to pursue its operations for long is an indication of this likelihood.

1.5 Other Remarks

The Chairman asked Chile for an explanation of its plan to add a new condition to the FFD. A delegate from Chile explained that in Chile it is common to consider previous competition infringements by the transaction parties. This is a standard step in merger control and by no means specific to occasions in which the FFD is invoked. However, the following question is raised: Should a firm that is liable for exclusionary abuse in a concentrated market be allowed to try to buy the victim and invoke the FFD a few months later?

One of the conditions for the FFD in Germany is that absent the merger, the whole of the market share of the target firm would go to the acquirer. A delegate from Germany acknowledged that the criteria of Germany's FFD are too stringent. For that reason, there have been discussions about the options for modifying the policy for quite some time already. In addition, the likely outcome of the coalition treaty between the political parties will include a sentence that Germany should try to have a more level playing field with merger control.

1.6 Failing Division Defence

The Chairman summarised the position of jurisdictions regarding the failing division defence (FDD), remarking that Germany takes a very strict stance since it does not recognise the defence at all. A quite different position is adopted by Switzerland, which has even considered a failing product defence in a merger case, although expressed along different terms. Other countries do not rule out the possibility of a FDD either, although they acknowledge that such a defence would be difficult to uphold given the possibilities of creative accounting.

The delegate from Germany said that the Bundeskartellamt's strict stance can be explained by the fact that assessing a FDD in an appropriate way is particularly difficult for any outsider (including a competition authority), even more so than a FFD.

The delegate from Ireland pointed out that the comparison of a 'division' failure scenario with a post-merger scenario should provide clear answers regarding possible deteriorations in competition and hence a FDD analysis should not be very different from an analysis regarding a FFD. Even if most competition authorities do not have a lot of experience with the FDD, what matters is whether there is a loss of competition.

A delegate from Portugal stated that the financial position of a failing division should be assessed on a stand-alone basis, without possibilities for internal transfer pricing. In addition, he raised the issue of whether when dealing with failing firms, we should not be more concerned with the liabilities of a firm and hence its creditors, rather than its assets. Competition may be the least concerned when dealing with failing firms.

Then a delegate from the UK asked why 'inevitable exit' does not come within the failing firm defence as well. 'Inevitable exit' refers to a situation in which a business is either sold or closed down.

A delegate from New Zealand provided an example in which the Commerce Commission considered such an ‘inevitable exit’ in the market for radiology services.

2. FFD in Times of Crisis

The Chairman drew attention to the Millway Dairy Crest case in the UK, noting that the Office of Fair Trading (OFT) and the Competition Commission (CC) appraised the business’ ability to meet its financial obligations in the near future differently. The UK’s contribution states that the variance can be explained by the difference in timeframe and hence the information gathering ability of the two authorities. The fact that time determined the result of a merger review may imply that competition authorities miss failing firm cases in times of crisis, when there is less time available to investigate mergers. The Chairman asked for clarification.

A delegate from the UK considered that the Millway Dairy Crest case should be seen differently given that the merging parties did not invoke the FFD before the OFT but only in the second phase before the CC. More generally, the time aspect will not affect the competitive outcome of a merger, at least not in the UK, given that merging parties may complete their deal before approval by the competition authority, as the merger control regime in the UK is a voluntary one.

Canada’s contribution centred on the improved efficiency of merger control in terms of procedure and organisation in times of crisis. A delegate from Canada said that the Competition Bureau has recently undertaken various initiatives to improve efficiency in the procedural aspect of its merger review framework. First, legislative amendments have been implemented that provide for a more efficient and flexible means of information gathering. Second, the Bureau has prioritised the analysis of failing firm issues over the full assessment of potential competitive effects of the transaction. Third, the Bureau is focussed on improving its expertise in reviewing failing firm issues, including through proactive identification of industries where failing firm claims are likely. Fourth, the Bureau explores creative merger remedies. Fifth, there will be more direct alignment with foreign counterparts on multi-jurisdictional reviews that have a failing firm component.

A delegate from Israel addressed the question of how the limited availability of credit in the current crisis can affect the outcome of a FFD. In his view, the limited availability of funds is a standard consideration when determining the likelihood of exit for a firm. He also pointed out that dynamic market conditions associated with the crisis should not interfere with the substantive criteria of the competition assessment. Nevertheless, he acknowledged the need for a shorter merger review period in times of crisis. Despite the already short merger review period in place in Israel, the competition authority increases efficiency further by prioritising failing firm cases and by demonstrating flexibility in areas and procedures which do not affect the substantive merger analysis.

3. FFD and Financial Institutions

The Chairman described the issues raised by the possible application of the FFD to financial institutions. Some delegations were of the opinion that mergers involving a failing bank are “business as usual”; others said it is impossible to apply the FFD to the financial sector because the assets will not exit the industry; still others said that we should also take into account the systemic risk related to failing banks; and finally, some say that the criteria of the FFD should be relaxed when applied in the financial sector. These views have been explained by the different jurisdictions in their written submissions.

The delegate from New Zealand argued that prudential objectives are the responsibility of the central bank and not of the competition authority. In contrast, Belgium’s delegate was of the opinion that any systemic risk considerations should be taken as an additional test in the competition authority’s assessment.

On this point, a delegate from Denmark acknowledged that someone should handle the risk of systemic failure following from one bank's exit, but that this should not be done by loosening merger control. The FFD cannot be applied to financial institutions because Denmark defines bank assets as a portfolio of debtors and hence banks' assets can never exit the market.

A delegate from Chinese Taipei contended that mergers in the financial industry are more complicated than those in non-financial industries. This is a result of a number of special laws that apply to mergers between banking or financial institutions, especially when the mergers involve a firm that qualifies as failing. Once a financial institution is found to be in an emergency situation, it can be exempted from the obligation to file a pre-merger notification. Hence, rather than applying a more lenient standard to financial institutions, the competition agency is likely not to have the power to review cases involving such banks. The different stance taken towards (failing) financial institutions is inspired by the idea of sectoral regulators that a bank must not fail. The very low concentration level in the banking sector makes the approach relatively unproblematic for the moment. However, Chinese Taipei acknowledges that their standards should become more stringent once the market becomes more concentrated.

A delegate from Japan, which has applied the FFD to banking mergers, explained that poor business results can be taken into account in a merger review if certain conditions are met. In the merger between Iyo bank and Toho Sogo Bank and the merger between Hokuyo Bank and Hokkaido Takushoku Bank, both Toho Sogo Bank and Hokkaido Takushoku Bank were on the brink of bankruptcy. However, these were not true FFD cases in the sense that the poor financial condition of the banks was only one of the factors that were taken into account. In any case, the JFTC applies basically the same ideas and analytical framework to mergers involving failing firms in the financial sector as it does in any other sector.

4. International Comparison of FFD

A delegate from South Africa said that the FFD is not treated as a defence in South Africa, but rather as one of the criteria that is taken into account to assess the effects of a merger. For the application of the FFD, South Africa compares different approaches used abroad, such as those from the US and the EU. However, even if other jurisdictions would conclude that all conditions of the FFD are fulfilled and thus approve the merger, this will not necessarily be the case in South Africa. It depends on the weight that is assigned to the FFD as compared to other criteria. This approach has advantages, such as flexibility, and disadvantages, such as the limited certainty provided to merging parties.

5. Final Remarks

Finally, a delegate from the EC added that the competition assessment and the FFD should not be perceived as two separate parts of merger review. Rather they should be seen as an integrated assessment of the effects of mergers. As a result, it does not matter what title we give to the defence, 'FFD' or 'integrated competition analysis on a prospective basis', since in any case, it is part of the prospective analysis of what the sustainable alternatives are to the merger.

Second, the delegate accepted that if there are other policy considerations to be taken into account, it should be done, but not in the context of a competition analysis. In the context of the financial crisis, competition authorities should have full understanding for regulators and central banks when they are concerned about the effects of a certain merger decision on the financial system. However, regulators and central banks should also see that their public policy objective of financial stability may cause permanent damage to the competitive structure of the banking sector. The reaction by central bankers to prevent competition agencies from intervening is ironic: banks that are too big will impose an even greater threat on financial stability.

COMPTE RENDU DE LA DISCUSSION

Cette table ronde s'articule autour de quatre grands thèmes :

1. Quels sont les normes et éléments de preuve en général concernant l'argument de l'entreprise défaillante ?
2. Comment les autorités de la concurrence devraient-elles considérer l'argument de l'entreprise défaillante en période de crise ? La situation de crise justifie-t-elle la réalisation d'ajustements ?
3. Le cas particulier de la faillite éventuelle d'établissements financiers exige-t-il des conditions distinctes ?
4. En quoi la façon d'envisager l'argument de l'entreprise défaillante varie-t-elle d'un pays membre de l'OCDE à l'autre ?

Le Président, M. Jenny, ouvre la Table ronde en demandant à l'orateur invité, le Dr. Jorge Padilla, Directeur général de LECG Europe, de présenter l'argument de l'entreprise défaillante et les difficultés qu'il soulève.

Le Dr. Padilla explique que l'argument de l'entreprise défaillante permet, à titre dérogatoire, de procéder à une fusion qui, dans des circonstances normales, s'avérerait anticoncurrentielle et se solderait par une réduction de la concurrence. La dérogation peut uniquement être accordée : i) s'il est probable que l'entreprise sorte du marché en l'absence de fusion ; ii) si le scénario d'après-fusion s'avère moins anticoncurrentiel que le scénario contrefactuel dans lequel l'entreprise cible sortirait du marché.

Il convient de se poser trois grandes questions pour déterminer si l'argument de l'entreprise défaillante est recevable.

Tout d'abord, l'entreprise cible sortira-t-elle du marché en l'absence de fusion ? Pour le déterminer, il faut examiner sa situation financière, bien connaître les possibilités de restructuration qui lui sont offertes en vertu du droit des faillites et analyser le contexte économique et réglementaire dans lequel elle opère.

Ensuite, existe-t-il des options moins anticoncurrentielles en matière de fusion ? Il n'est pas simple de répondre à cette question. Les entreprises en difficulté financière sont souvent réticentes à faire le tour des repreneurs potentiels de peur que cette démarche les rapproche de la faillite. De plus, la comparaison d'une fusion donnée avec d'autres fusions envisageables exige une série d'analyses prospectives, mais la moindre analyse de ce type est difficile à réaliser.

Enfin, qu'advierait-il des actifs de l'entreprise cible après sa sortie du marché ? Ils pourraient revenir dans leur totalité à l'entreprise qui se propose comme acquéreur. Ce cas de figure permettrait d'apporter des réponses simples dans le cadre d'une comparaison des scénarios avec et sans fusion, mais il y a peu de chances qu'il se réalise. Lorsque l'acquéreur ne reprend pas l'ensemble des actifs, on part de l'hypothèse que le scénario d'après-fusion devrait être plus anticoncurrentiel que le scénario contrefactuel. Or, ce n'est pas nécessairement vrai d'un point de vue économique.

Il est probable que les dispositions régissant l'argument de l'entreprise défaillante, comme toute autre règle en matière de concurrence ou de fusion, donnent lieu à des faux positifs et des faux négatifs, c'est-à-dire à des condamnations à tort et des acquittements à tort, respectivement. Les règles qui, pour des motifs légitimes, visent à réduire au minimum les faux négatifs risquent néanmoins de créer un déséquilibre propice aux faux positifs.

L'argument de l'entreprise défaillante étant peu invoqué, le Dr. Padilla se demande si les autorités de la concurrence ne devraient pas concentrer davantage leurs efforts sur l'identification de scénarios contrefactuels valables, plutôt que de consacrer du temps et des ressources à l'examen de cet argument.

1. Éléments fondamentaux concernant l'argument de l'entreprise défaillante

Le Président cite le Dr. Padilla sur le fait que l'incapacité d'une entreprise à se réorganiser en vertu du droit des faillites comme condition à remplir obligatoirement pour se prévaloir du statut d'entreprise défaillante semble reposer sur l'hypothèse selon laquelle le scénario d'après-fusion est nécessairement moins concurrentiel que le cas de figure où l'entreprise s'étant relevée d'une procédure de faillite resterait indépendante. Il interroge les États-Unis sur la pertinence de cette analyse économique.

Un délégué des États-Unis répond que dans son pays, la situation d'incapacité d'une entreprise à se réorganiser en vertu du chapitre 11 de la loi sur les faillites américaine exige la preuve que ladite entreprise est réellement défaillante. Cette condition réduit la marge d'erreur dans l'examen de l'argument de l'entreprise défaillante par rapport à d'autres pays où l'on insiste moins, voire pas du tout, sur les possibilités de réorganisation. Les normes laxistes concernant l'argument de l'entreprise défaillante ne doivent pas offrir un régime de protection aux entreprises qui, normalement, n'auraient pu fusionner.

Le Président note ensuite que l'Union européenne (UE), dans sa contribution, résume les trois conditions associées par la Commission européenne à l'argument de l'entreprise défaillante : i) l'entreprise défaillante serait, dans un proche avenir, contrainte de quitter le marché ; ii) il n'existe pas d'autre solution de rachat envisageable moins dommageable pour la concurrence que la concentration notifiée ; iii) si la concentration n'était pas réalisée, les actifs de l'entreprise défaillante sortiraient inévitablement du marché. Il est par ailleurs signalé dans la contribution de l'UE que ces conditions ne sont pas exclusives ou exhaustives. Le Président demande à l'UE si les autorités de la concurrence ont besoin de critères particuliers d'examen de l'argument de l'entreprise défaillante ou si une meilleure panoplie de scénarios contrefactuels est nécessaire pour les fusions en général.

L'UE indique tout d'abord que le recours limité à l'argument de l'entreprise défaillante en période de crise économique et financière est dû en partie à l'existence d'autres moyens d'action, notamment la recapitalisation des banques par l'État. Les mesures telles que la protection du chapitre 11, à laquelle les États-Unis ont fait référence, et l'aide publique, dans l'UE, devraient être considérées comme des éléments qui modifient les règles du jeu concernant l'argument de l'entreprise défaillante et rendent toute analyse contrefactuelle fort complexe. Elles mettent également en évidence le fait que la crise actuelle restreint la stricte application des conditions requises pour que l'argument de l'entreprise défaillante soit recevable, et exige de la flexibilité de la part des autorités de la concurrence. Toutefois, un assouplissement des critères d'examen n'est pas nécessaire, de la même façon que l'argument de l'entreprise défaillante ne ferait pas l'objet d'un durcissement en période de conjoncture favorable.

1.1 *Argument de l'entreprise défaillante : un cas particulier de causalité générale ou d'analyse contrefactuelle*

Un autre délégué de l'UE ajoute que l'argument de l'entreprise défaillante définit un cadre particulier dans l'analyse de causalité générale, pour lequel le lien de causalité doit systématiquement reposer sur une

analyse contrefactuelle. Néanmoins, outre les lignes directrices relatives aux fusions classiques, l'argument de l'entreprise défaillante présente un intérêt pédagogique pour les entreprises et leur garantit une certaine prévisibilité. Un délégué de l'Espagne reconnaît également dans cet argument un cas particulier d'analyse contrefactuelle et prend l'exemple d'une fusion entre des bouquets payants de chaînes de télévision par satellite lors de laquelle il a été tenu compte, entre autres, de la fragilité de la situation financière des entreprises impliquées.

Le Dr. Padilla réagit en signalant que si l'argument de l'entreprise défaillante peut effectivement être considéré comme un cas particulier d'analyse contrefactuelle renforçant la prévisibilité, il ne faudrait pas perdre de vue que la charge de la preuve dans les deux cas est répartie de façon très différente, ce qui a des implications non négligeables pour la conduite, voire l'issue, de l'enquête. Normalement, lors d'une enquête sur une fusion, c'est aux autorités de la concurrence qu'il incombe de prouver que la fusion est anticoncurrentielle. Toutefois, lors d'une fusion dans laquelle l'argument de l'entreprise défaillante est invoqué, c'est aux parties à l'opération de montrer que leur fusion est moins anticoncurrentielle qu'elle ne l'était considérée à l'origine.

Un délégué de l'Irlande estime qu'en raison de cette inversion de la charge de la preuve, les parties à la fusion qui invoquent l'argument de l'entreprise défaillante sont désavantagées dans la mesure où elles doivent admettre l'existence d'une réduction significative de la concurrence. Néanmoins, le délégué revient ultérieurement sur ce point et indique que les parties à la fusion devraient supporter la charge de la preuve car ce sont elles, et non les pouvoirs publics, qui disposent des meilleures informations sur le marché. Elles ont donc tout intérêt à entamer des pourparlers avec les autorités de la concurrence à un stade précoce.

Le Dr. Padilla est d'accord sur le fait qu'il devrait incomber aux parties à la fusion de collecter des éléments de preuve, notamment en mettant en avant d'autres solutions sérieuses envisageables. C'est ce qu'on appelle la charge factuelle de la preuve. Toutefois, sur le fond, c'est aux autorités de la concurrence que revient la charge de la preuve, qui repose sur la mise en balance des effets proconcurrentiels et anticoncurrentiels.

Selon le délégué de l'Irlande, on accorde une importance excessive au terme « charge de la preuve », car l'argument de l'entreprise défaillante est invoqué seulement après la mise en évidence d'une réduction importante de la concurrence. Plus tard au cours de la Table ronde, un délégué des États-Unis signale que le fait de transférer la charge de la preuve vers les pouvoirs publics en ce qui concerne la collecte d'éléments de preuve pourrait accroître le nombre d'erreurs. En outre, il fait observer que l'autorisation de fusions qui, dans d'autres circonstances, auraient été interdites risque à terme de se payer, et peut-être cher.

1.2 Condition associée à l'argument de l'entreprise défaillante : aucune autre fusion moins anticoncurrentielle n'est envisageable

La Table ronde porte à présent sur la condition associée à l'argument de l'entreprise défaillante en vertu de laquelle aucune autre fusion moins dommageable pour la concurrence ne doit être envisageable. Dans sa contribution, l'UE note qu'il est difficile de réunir les critères d'examen de l'argument de l'entreprise défaillante, surtout en période de crise. La condition selon laquelle aucune autre fusion moins anticoncurrentielle ne doit être envisageable est particulièrement contraignante. À ce sujet, la France indique dans sa contribution que seules les « offres crédibles » formulées par des acquéreurs de substitution seront prises en compte pour l'évaluation de cette condition. Néanmoins, le Président dit que les critères permettant de juger de la « crédibilité » d'une offre ne sont pas totalement clairs.

Un délégué de la France explique que l'offre d'un repreneur potentiel acquiert, lorsqu'elle est soumise à un tribunal commercial, une crédibilité plus grande que si elle se réduit à une simple manifestation d'intérêt

dans la presse. Il ne suffit pas toutefois de saisir un tribunal commercial d'une offre pour qu'elle soit jugée crédible. Dans le cas SEB/Moulinex, par exemple, certaines offres étaient limitées à une part si faible de l'activité qu'elles n'étaient pas considérées comme sérieuses. Ultérieurement, un délégué de la Suisse signale que les autorités de la concurrence ne jugent pas le sérieux des offres de substitution dans le cadre des procédures de faillite et de la comparaison de ces offres, tâche qu'elles laissent aux parties à la fusion.

Un délégué du Royaume-Uni indique qu'il est courant d'envisager des fusions de substitution avec les parties ayant présenté une offre d'un montant supérieur à la valeur de liquidation. Si les offres d'un montant inférieur à la valeur de liquidation sont moins dommageables pour la concurrence que les offres d'un montant supérieur à cette valeur, doit-on en tenir compte ? Selon le Dr. Padilla, qui se place du point de vue de la politique de la concurrence, la réponse est négative, car en tenir compte signifierait que le contrôle des fusions permet l'acquisition d'actifs à des prix inférieurs à leur valeur marchande et, partant, qu'il fausse la concurrence.

1.3 Absence de politiques formelles en matière d'argument de l'entreprise défaillante

Dans un certain nombre de pays, l'argument de l'entreprise défaillante n'existe pas en tant que tel. Par exemple, la Nouvelle-Zélande a recours à sa procédure d'analyse contrefactuelle, qui permet de comparer plusieurs cas de figure, la Pologne pourrait procéder à une évaluation de l'intérêt général, et la Russie vient d'introduire une loi qui dispense les établissements financiers de se soumettre au contrôle des fusions. Le Président demande des précisions sur ces approches et s'interroge sur le fait de savoir si l'existence formelle d'un argument de l'entreprise défaillante présenterait plus d'intérêt.

Un délégué de la Nouvelle-Zélande explique qu'en application de ses nouvelles lignes directrices, la Commission du commerce se penchera sur l'évolution des flux de trésorerie, les perspectives de restructuration et les éventuelles tentatives infructueuses de sauvetage de l'entreprise en difficulté. Une analyse portant sur la fusion consistera notamment à comparer les faits avec tous les scénarios contrefactuels envisageables, même si l'accent est généralement mis uniquement sur le plus favorable à la concurrence. Par exemple, lors de la fusion Southern Cross, la Commission a conclu que l'hôpital Southern Cross resterait sur le marché, scénario contrefactuel le plus probable, étant donné les investissements dont il avait récemment fait l'objet et le fait que rien n'indiquait de quelconques discussions sur une sortie du marché.

Un délégué de la Pologne fait remarquer qu'une interprétation souple de son analyse de l'intérêt général suffira à traiter les fusions dans lesquelles une des parties est une entreprise défaillante. Compte tenu du faible nombre de demandes de fusion s'appuyant sur cet argument, il est inutile de mettre en place des lignes directrices formelles à cet égard. Le Dr. Padilla exprime ses craintes quant à cette analyse de l'intérêt général, qui risque de se traduire par un examen trop laxiste de l'argument de l'entreprise défaillante, en particulier en période de crise, et par un nombre excessif de faux négatifs.

Un délégué de la Russie explique que les autorités de la concurrence de son pays ne jugent pas non plus nécessaire d'instaurer une quelconque exemption générale au titre des règles de contrôle des fusions sur la base de l'argument de l'entreprise défaillante, car cette mesure créerait une sorte de régime de protection inutile dont les entreprises pourraient faire un usage abusif, étant donné la difficulté à déterminer de façon convenable si une entreprise est défaillante ou non. La loi russe prévoyant des dispositions particulières pour l'acquisition des actifs d'une banque défaillante fait exception à cet égard. Toutefois, elle est temporaire et n'a été promulguée que pour faire face à la situation de crise. Grâce au système rigoureux de collecte de données de la Banque centrale de Russie, il est plus facile de vérifier si une entité est défaillante dans le cas des banques que dans celui des entreprises industrielles, lesquelles posséderaient un avantage considérable en matière d'informations sur la probabilité de leur défaillance. Aussi la Russie préfère-t-elle continuer d'appliquer ses principes généraux de contrôle des fusions. Le délégué indique par ailleurs que,

dans le cadre du contrôle des fusions, la règle de raison permet aux autorités fédérales de la concurrence russes (FAS) de prendre la bonne décision. La probabilité de sortie du marché est examinée selon des principes généraux et non sur la base d'un mécanisme dérogatoire tel que l'argument de l'entreprise défaillante. Plus tard au cours de la Table ronde, le Dr. Padilla signale que les outils ordinaires de contrôle des fusions peuvent être utilisés lorsqu'il existe des difficultés financières, comme la Russie l'a proposé pour les entreprises industrielles. Il souligne néanmoins que les autorités de la concurrence doivent veiller à ne pas appliquer le scénario d'avant-fusion en tant que scénario contrefactuel, comme c'est le cas lors des examens de fusion classiques, sous peine d'aboutir à une évaluation incorrecte des effets sur la concurrence et, partant, d'obtenir trop de faux positifs.

1.4 Condition associée à l'argument de l'entreprise défaillante : l'entreprise sort du marché

Le Président poursuit le débat en cherchant à savoir comment les autorités de la concurrence déterminent si une entreprise sortira ou non du marché. Il fait référence à l'expérience considérable de la Commission coréenne de la concurrence (KFTC) en matière d'examen de l'argument de l'entreprise défaillante, notamment à sa décision concernant la fusion Samick/Young Chang, dans laquelle la KFTC a jugé que Young Chang avait un fort potentiel de redressement malgré sa situation financière au moment de la fusion.

Un délégué de la Corée explique qu'il est courant d'analyser la situation financière de l'entreprise considérée, notamment son bilan, ses moyens de production et les informations obtenues auprès des investisseurs et des actionnaires. Dans le cas Young Chang, les difficultés financières de l'entreprise n'étaient pas dues à un désavantage comparatif mais à une pénurie temporaire de liquidités et à un différend entre les partenaires sociaux. Cette analyse s'est révélée exacte étant donné qu'une troisième entreprise a racheté le célèbre fabricant de pianos pour un montant cinq fois supérieur à celui que proposait la partie initiale à la fusion.

Le Président s'interroge alors sur les délais de sortie du marché d'une entreprise défaillante. Les autorités de la concurrence s'intéressent-elles au court et au long terme, ou prennent-elles en compte seulement le court terme ?

Un délégué de la Suisse fait remarquer que la fréquence relativement faible des cas dans lesquels l'argument de l'entreprise défaillante est invoqué s'explique peut-être par le fait que des seuils de notification des fusions sont en place et que les pays de l'UE verront la Commission européenne être saisie des cas importants. Il répond ensuite que la sortie du marché d'une entreprise devrait être évaluée sur le court à moyen terme, c'est-à-dire sur une période de deux ans maximum.

Le Dr. Padilla répond que d'un point de vue économique, il conviendrait de ne tenir compte que du très court terme, essentiellement parce que si tel n'est pas le cas, la situation d'urgence qui justifie la dérogation n'existerait pas.

Un délégué de la Turquie indique ultérieurement que seul l'avenir très proche est pris en compte dans son pays pour déterminer si une entreprise risque de sortir du marché, plusieurs facteurs étant variables et donc imprévisibles à moyen et long terme. En outre, pour l'autorité de la concurrence turque (TCA), la forte probabilité d'une sortie du marché à court terme est suffisante, et l'existence de données financières fiables laissant supposer que l'entreprise en question ne pourra poursuivre longtemps ses activités dénote cette probabilité.

1.5 Remarques diverses

Le Président demande au Chili d'expliquer son projet d'association d'une nouvelle condition à l'argument de l'entreprise défaillante. Un délégué du Chili explique que dans son pays, il est courant de prendre en

considération les précédentes violations du droit de la concurrence commises par les parties à l'opération. Cette mesure est classique dans le cadre du contrôle des fusions et n'est aucunement spécifique aux cas dans lesquels l'argument de l'entreprise défaillante est invoqué. Se pose toutefois la question suivante : devrait-on laisser une entreprise coupable de pratiques d'exclusion sur un marché peu concurrentiel tenter d'acheter l'entreprise qui en est victime et invoquer l'argument de l'entreprise défaillante quelques mois plus tard ?

En Allemagne, une des conditions devant être remplie pour invoquer l'argument de l'entreprise défaillante est qu'en l'absence de fusion, la totalité de la part de marché de l'entreprise cible reviendra à l'acquéreur. Un délégué de l'Allemagne reconnaît que les critères d'examen de l'argument de l'entreprise défaillante en vigueur dans son pays sont trop stricts. C'est pourquoi des discussions sur les possibilités de modification sont en cours depuis un certain temps déjà. De plus, le traité de coalition entre les partis politiques comprendra probablement une phrase indiquant que l'Allemagne devra essayer d'instaurer plus d'équité en matière de contrôle des fusions.

1.6 *Argument de la division défaillante*

Le Président récapitule les positions des pays concernant l'argument de la division défaillante, faisant observer que celle de l'Allemagne est très stricte dans la mesure où ce pays ne reconnaît pas du tout l'argument en question. La Suisse a adopté une position sensiblement différente, ayant même pris en compte dans un cas de fusion un « argument du produit défaillant », exprimé toutefois en d'autres termes. D'autres pays n'écartent pas non plus la possibilité d'un argument de la division défaillante, tout en étant conscients qu'un tel argument serait difficile à faire valoir étant donné les possibilités d'artifices comptables.

Selon le délégué de l'Allemagne, la position stricte du Bundeskartellamt (autorité de la concurrence allemande) peut s'expliquer par le fait qu'il s'estime incapable d'évaluer convenablement un argument de la division défaillante, s'abstenant donc d'approuver des fusions sur cette base.

Le délégué de l'Irlande signale que la comparaison d'un scénario de défaillance d'une « division » avec un scénario d'après-fusion devrait apporter des réponses claires concernant d'éventuelles dégradations des conditions de concurrence et, par conséquent, une analyse de l'argument de la division défaillante ne devrait pas être très différente d'une analyse portant sur l'argument de l'entreprise défaillante. Même si la plupart des autorités de la concurrence ont peu d'expérience en matière d'argument de la division défaillante, l'important est de savoir s'il existe ou non une réduction de la concurrence.

Un délégué du Portugal dit que la situation financière d'une division défaillante devrait être évaluée de façon indépendante, sans qu'aucune pratique de prix de transfert internes soit possible. Il soulève par ailleurs la question de savoir s'il ne conviendrait pas, dans le cas d'une entreprise défaillante, de se préoccuper du passif, et donc des créanciers de l'entreprise, plutôt que de l'actif. En définitive, la concurrence est peut-être une préoccupation secondaire dans les affaires d'entreprise défaillante.

Un délégué du Royaume-Uni demande alors pourquoi la notion de « sortie inévitable » n'est pas également prise en compte au titre de l'argument de l'entreprise défaillante. La « sortie inévitable » renvoie à la situation dans laquelle une entreprise est soit vendue, soit fermée.

Un délégué de la Nouvelle-Zélande donne un exemple dans lequel la Commission du commerce a pris en compte cette « sortie inévitable » dans le cadre du marché des services de radiologie.

2. L'argument de l'entreprise défaillante en temps de crise

Le Président attire l'attention sur l'affaire Millway Dairy Crest au Royaume-Uni, en soulignant que le Bureau de la concurrence (OFT, *Office of Fair Trading*) et la Commission de la concurrence (CC, *Competition Commission*) ont évalué différemment la capacité de cette entreprise à satisfaire à ses obligations financières dans un proche avenir. Il est indiqué dans la contribution du Royaume-Uni que cette divergence peut s'expliquer par le fait que ces deux organismes ont réalisé leur évaluation avec des horizons temporels différents et, partant, qu'elles n'ont pu collecter les mêmes informations. Le fait que le facteur temps ait déterminé l'issue d'une procédure de contrôle de fusion peut laisser penser que les autorités de la concurrence rejettent parfois indûment l'argument de l'entreprise défaillante en période de crise, où elles disposent de moins de temps pour examiner les fusions. Le Président demande des éclaircissements.

Un délégué du Royaume-Uni estime que l'affaire Millway Dairy Crest devrait être vue sous un angle différent, étant donné que les parties à la fusion n'ont pas invoqué l'argument de l'entreprise défaillante devant l'OFT et ne l'ont mis en avant que dans un second temps, devant la CC. De manière plus générale, le facteur temps n'influe pas sur le résultat d'une fusion en termes de concurrence, tout au moins pas au Royaume-Uni, étant donné que les parties à une fusion peuvent conclure leur transaction avant qu'elle ne soit approuvée par l'autorité de la concurrence, le régime de contrôle des fusions britannique étant facultatif.

La contribution du Canada est centrée sur l'amélioration de l'efficacité du contrôle des fusions en termes de procédure et d'organisation en temps de crise. Un délégué du Canada indique que le Bureau de la concurrence a récemment pris différentes initiatives pour améliorer l'efficacité des procédures dans le cadre du contrôle des fusions. Premièrement, la législation a été modifiée de manière à offrir des modalités de collecte d'informations plus efficaces et plus souples. Deuxièmement, le Bureau fait passer l'examen de l'argument de l'entreprise défaillante avant l'évaluation approfondie des effets potentiels sur la concurrence de la transaction considérée. Troisièmement, le Bureau étudie des possibilités originales de mesures correctives en matière de fusions. Quatrièmement, le Bureau de la concurrence procédera à une harmonisation plus directe avec ses homologues étrangers lorsque l'argument de l'entreprise défaillante est invoqué dans le cadre du contrôle d'une fusion relevant de plusieurs juridictions.

Un délégué d'Israël aborde la question de savoir quelle incidence la rareté du crédit au cours de la crise actuelle peut avoir sur l'examen de l'argument de l'entreprise défaillante. De son point de vue, la rareté des ressources en capital disponibles constitue un élément classique à prendre en compte pour déterminer la probabilité de sortie d'une entreprise du marché. Il souligne également que l'évolution des conditions de marché associée à la crise ne doit pas influencer sur les critères de fond qui sous-tendent l'évaluation des conditions de concurrence. Néanmoins, il reconnaît la nécessité de raccourcir la durée du contrôle des fusions en temps de crise. Bien que la procédure de contrôle des fusions soit déjà brève en Israël, l'autorité de la concurrence renforce encore son efficacité en examinant en priorité les affaires d'entreprises défaillantes et en faisant preuve de souplesse dans les domaines et les procédures qui sont sans incidence sur l'analyse au fond des dossiers de fusions.

3. Argument de l'entreprise défaillante et établissements financiers

Le Président décrit les questions soulevées par l'éventuelle invocation de l'argument de l'entreprise défaillante pour des établissements financiers. Certaines délégations estiment que les fusions impliquant une banque défaillante relèvent de leur « activité normale » ; d'autres affirment qu'il est impossible d'appliquer la théorie de l'entreprise défaillante au secteur financier, car les actifs considérés ne sortiront pas de cette branche d'activité ; d'autres encore considèrent qu'il convient également de prendre en compte le risque systémique lié aux banques défaillantes ; et enfin, certains indiquent que les critères d'examen de

l'argument de l'entreprise défaillante devraient être assouplis pour le secteur financier. Ces points de vue ont été expliqués par les différentes juridictions dans leurs communications écrites.

Le délégué de la Nouvelle-Zélande fait valoir que les objectifs prudentiels relèvent de la compétence de la banque centrale, et non de l'autorité de la concurrence. En revanche, le délégué de la Belgique estime que les éventuelles considérations de risque systémique devraient constituer un critère supplémentaire d'évaluation pour l'autorité de la concurrence. Sur ce point, un délégué du Danemark convient que quelqu'un doit se charger de la question du risque de défaillance systémique à la suite de la sortie d'une banque du marché, mais il estime que cela ne doit pas se traduire par un assouplissement du contrôle des fusions. L'argument de l'entreprise défaillante ne s'applique pas aux établissements financiers, car le Danemark définit les actifs bancaires comme un portefeuille de débiteurs, ce qui implique que les actifs bancaires ne peuvent jamais sortir du marché.

Un délégué du Taipei chinois conteste l'idée que les fusions soient plus complexes dans le secteur financier que dans les autres branches d'activité. Cela tient à l'existence de lois spécifiquement applicables aux fusions entre banques ou autres établissements financiers, en particulier lorsque ces opérations de concentration concernent une entreprise reconnue comme défaillante. Une fois qu'il a été établi qu'un établissement financier se trouve dans une situation d'urgence, il peut être exonéré de l'obligation de présenter une notification préalable en cas de fusion. Par conséquent, au lieu d'appliquer des règles plus souples aux établissements financiers, il est probable que l'autorité de la concurrence ne soit tout bonnement pas en position d'examiner le cas de ce type de banque. Cette approche différente adoptée à l'égard des établissements financiers (défaillants) repose sur l'idée des autorités de régulation sectorielles qu'une banque ne doit pas faire faillite. Compte tenu de la très faible concentration du secteur bancaire, cette approche ne pose guère de problèmes pour le moment. Toutefois, le délégué du Taipei chinois reconnaît que les règles qui y sont appliquées devraient se durcir si le marché se concentrait.

Un délégué du Japon, où l'argument de l'entreprise défaillante a été pris en considération dans le cadre de fusions bancaires, explique que les résultats dégradés des entreprises sont pris en compte dans toute procédure de contrôle de fusion. Dans le cadre de la fusion entre la banque Iyo et la banque Togo Soho, ainsi que de la fusion entre la banque Hokuyo et la banque Hokkaido Takushoku, tant la banque Iyo que la banque Hokkaido Takushoku étaient au bord de la faillite. Néanmoins, il ne s'agissait pas de véritables affaires d'entreprise défaillante, puisque la situation financière dégradée des banques ne constituait que l'un des facteurs pris en compte. Quoi qu'il en soit, la Commission de la concurrence japonaise (JFTC, *Japan Fair Trade Commission*) applique en substance les mêmes principes et cadres d'analyse aux fusions impliquant des entreprises défaillantes dans le secteur financier que dans les autres branches d'activité.

4. Comparaison internationale de l'argument de l'entreprise défaillante

Un délégué de l'Afrique du Sud indique que l'argument de l'entreprise défaillante n'est pas un moyen de défense en Afrique du Sud, mais plutôt un des critères pris en compte pour évaluer les effets d'une fusion. Pour examiner l'argument de l'entreprise défaillante, l'Afrique du Sud compare différentes approches adoptées à l'étranger, telles que celles des États-Unis et de l'UE. Néanmoins, même si d'autres juridictions concluraient que toutes les conditions nécessaires sont réunies pour qu'il soit fait droit à l'argument de l'entreprise défaillante, et approuveraient en conséquence la fusion considérée, tel ne sera pas nécessairement le cas en Afrique du Sud. Cela dépend de l'importance accordée à l'argument de l'entreprise défaillante par rapport à d'autres critères. Cette approche présente des avantages, tels que la souplesse, et des inconvénients, tels qu'une forte incertitude pour les parties à la fusion considérée.

5. Remarques conclusives

Enfin, un délégué de la Commission européenne ajoute que l'évaluation des conditions de concurrence et l'examen de l'argument de l'entreprise défaillante ne doivent pas être considérés comme deux composantes distinctes du contrôle des fusions. Il convient au contraire de les considérer globalement comme une évaluation intégrée des effets des fusions. En conséquence, la désignation retenue importe peu, qu'il s'agisse de l'« argument de l'entreprise défaillante » ou de l'« analyse intégrée de la concurrence sur une base prospective », puisque en tout état de cause, cet élément fait partie intégrante de l'analyse prospective des options viables autres que la fusion.

Deuxièmement, le délégué convient que la prise en compte d'autres éléments doit avoir lieu si elle s'impose, mais pas dans le contexte d'une analyse de la concurrence. Dans le contexte de la crise financière, les autorités de la concurrence doivent faire preuve de la plus grande compréhension à l'égard des préoccupations des autorités de régulation et des banques centrales qui s'inquiètent des effets que pourrait avoir sur le système financier une décision relative à une fusion. Néanmoins, les autorités de régulation et les banques centrales doivent également comprendre que leurs objectifs en matière de stabilité financière peuvent nuire durablement à la structure concurrentielle du secteur bancaire. Il est paradoxal que les responsables des banques centrales aient réagi en s'opposant à l'intervention des autorités de la concurrence : les banques qui sont de trop grande taille représentent en effet une menace encore plus grande pour la stabilité financière.