
Merger reviews in the time of Covid-19: the failing-firm defence

1. Introduction

The Covid-19 pandemic and the measures adopted by national authorities to contain it have already caused an economic downturn and put numerous businesses in difficulty – and the outlook for the coming months is far from bright.

The European Commission and national competition authorities will most likely continue to rigorously scrutinize all notified mergers, even when they entail the acquisition of a failing firm at the same time taking into consideration the effect of the Covid-19 crisis, based on a case by case approach.

In fact Competition Commission Vestager recently declared that there is no need to relax the rules even in these uncertain times and that reviews of mergers entailing the acquisition of a failing firm will be scrutinized in accordance with the standard, threefold, failing-firm defence (“FFD”) test on a case-by-case approach.

The UK Competition and Markets Authority (“CMA”) also adopted this approach in its decision of 22 April, which provisionally clears Amazon’s acquisition of a minority stake in Deliveroo because the company would otherwise exit the market. The CMA’s decision of 6 May – although prohibiting the JD Sports Fashion/Footasylum merger – also considered the potential impact of Covid-19 on the merging parties (which did not raise a FFD), leaving the door open to a review of its final decision in terms of remedies implementation.



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2. The Failing-Firm Defence

The Commission may clear mergers based on the FFD regardless of whether the mergers could pose substantial competition issues for the market, because the targets would otherwise exit the market. The rationale behind the FFD is that “the deterioration of the competitive structure that follows the merger cannot be said to be caused by the merger”¹.

¹ European Commission 2004 Horizontal Merger Guidelines, para. 89.

For the FFD to succeed, the merging companies have to demonstrate fulfilment of all the following **three conditions**:

- The allegedly failing firm would, if not taken over, be forced out of the market in the near future because of financial difficulties.
- A less anti-competitive alternative to the proposed merger does not exist.
- The assets of the failing firm would, in the absence of a merger, inevitably exit the market.

This test clearly places a high burden of proof on the merging parties, and **the European Commission and national competition authorities are renowned for being quite strict in assessing whether the three conditions are met**. In fact, despite September 2009–August 2010 being one of the most difficult periods for EU businesses, the FFD never succeeded before the European Commission during that period².

However, two significant clearances were granted based on the FFD in 2013: the **Nynas/Shell/Harburg Refinery deal** was authorised because the target had been loss-making for several years, was likely to remain unprofitable in the future and would therefore have gone bust if the merger had been blocked³.

A month later, the Commission also cleared **Aegean's acquisition of Olympic Air** on the ground that Olympic Air was a failing company that would have exited the market unless acquired by Aegean Airlines.⁴ It is keen to note that the same merger operation was prohibited, two years earlier, in the middle of the economic crisis in Greece, and the FFD raised by the companies was dismissed. At that time the Commission held that: a) Olympic Air would probably have continued its domestic operations in Greece and possibly have retrenched its international operations, and b) the investment group that owned the company had an interest in maintaining its investment in business due to the exit costs and reputational backlash from the airline's bankruptcy⁵.

Although **Commissioner Vestager** recently confirmed the need for a strict application of the three-fold FFD test, she also acknowledged that **the Covid-19 crisis could well drive companies (e.g., in the airline sector) out of business and that national competition authorities should thus carefully assess what the market situation would be**

² GÖTZ DRAUZ, STEPHEN MAVROGHENIS, SARA ASHALL, *Recent Developments in EU Merger Control 1 September 2009 – 31 August 2010*, Journal of European Competition Law & Practice, Volume 2, Issue 1, February 2011, pp 46–61.

³ Commission Decision of 2 September 2013, adopted in [Case No COMP/M.6360 - Nynas/Shell/Harburg Refinery](#).

⁴ Commission Decision of 9 October 2013, adopted in [Case No COMP/M.6796 - Aegean/Olympic II](#).

⁵ Commission Decision of 26 January 2011, adopted in case No [COMP/M.5830 - Olympic/Aegean Airlines](#).

absent the merger.

As mentioned, the **CMA** confirmed the adoption of this approach in the **Amazon/Deliveroo case**. The CMA opened a phase 2 investigation last December because of serious competition concerns, the main one being the risk of the merger discouraging Amazon “from re-entering the online restaurant food market and further developing its presence within the online convenience grocery delivery market in the UK”. However, following the Covid-19 outbreak, Deliveroo informed the CMA that it had been hit so hard by the Covid-19 crisis (due to the large number of its partnering restaurants that have been forced to close) that it would fail without Amazon’s investment. This new evidence led the CMA to conclude that “the imminent exit of Deliveroo would be worse for competition than allowing the Amazon investment to proceed and has therefore provisionally found that the deal should be cleared”. The final decision is expected next month.

However, to make it clear that the Amazon/Deliveroo decision was not to be taken as a sign of the **CMA** becoming more lenient in assessing the FFD, on 22 April the CMA published **guidance on merger assessments**. An annex was dedicated to mergers involving failing firms, which clarifies that the **FFD should be assessed on a case-by-case basis** and that the FDD is only likely to be accepted when “supported by a material body of probative evidence, which the merging parties can expect the CMA to test thoroughly with both the merging parties and their advisers, as well as third parties”.

The CMA’s shift in assessing the Amazon/Deliveroo case is a telling example of how, despite the rigorous approach by competition authorities also in times of economic downturn, competition authorities are open to considering the market consequences posed by Covid-19 in each case. Indeed, although the CMA recently blocked **JD Sports Fashion’s acquisition of Footasylum**, the decision does mention potential detrimental effects of Covid-19 on the parties’ retail businesses in the medium-to-long term, thereby leaving the door open to review its decision, in terms of remedies implementation.

3. Conclusion

Although we cannot expect a more lenient approach by the Commission or national competition authorities, their recent decision-making practice indicates a certain degree of flexibility by them to fully take into account the market conditions and the specificities of merging parties in the time of Covid-19.

The CMA (despite Brexit) still remains a reference point for competition authorities; they might thus use the CMA’s approach in the Amazon/Deliveroo as a benchmark.

The FFD will likely be invoked often in the following months. And although the standard of proof required for the FFD to succeed is high, the Commission and national competition authorities will surely take into account (if duly demonstrated) the economic and financial difficulties caused by the Covid-19 crisis.