# COVID-19: THE FAILING FIRM DEFENSE IN THE FACE OF THE COVID-19 OUTBREAK

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As the COVID-19 pandemic causes commercial and financial difficulties, an increasing number of transactions may involve companies in financial difficulty. This may lead to more transactions where antitrust authorities come under pressure to approve acquisitions that would ensure the survival of those companies. In the context of transactions involving distressed targets, the "failing firm defense" (FFD) is often raised but is rarely successful in practice. The rationale of the FFD is that the deterioration of the competitive structure of the market that follows the merger is not caused by the transaction but by the prevailing economic conditions affecting the target.

The European Commission (Commission) relies on three criteria in order to assess whether an FFD is likely to succeed: (i) the failing firm would in the near future be forced to exit the market due to financial difficulties if it is not taken over by another company; (ii) there is no less anticompetitive alternative than the proposed merger; and (iii) in the absence of the proposed merger, the assets of the failing firm would inevitably exit the market.

As an example, in 2013, the Commission cleared the acquisition of a Greek air carrier by another Greek air carrier, taking into account the FFD. In particular, the Commission upheld the argument that the continuous Greek recession had put the company under financial difficulties and that the air carrier to be acquired was likely to exit the market in any event. The Commission's market investigation revealed that there were no operators interested in acquiring the acquired carrier's assets in the event the company would leave the market. Furthermore, the acquired carrier's market shares on the relevant air routes would, in any event, accrue to the acquiring carrier since the parties were already in a quasi-duopoly situation, and entry by a third operator was considered to be unlikely in the foreseeable future.

The standard of proof that the parties must meet for a successful FFD is very high, and the Commission's economic analysis is necessarily complex. To date, the Commission has accepted the FFD in three cases only.

Although there have been calls for the Commission (and other antitrust authorities) to relax their approach to the FFD, it is very unlikely that the Commission will lower its legal standards for the FFD in the context of the COVID-19 outbreak. The Commission made it clear in the context of the 2008 crisis that the proposition that a more lenient FFD 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.

Similarly, in April 2020, Commission's Executive Vice-President and Competition Commissioner Margrethe Vestager excluded a more permissive approach and warned that the crisis "*shouldn't be a shield to allow mergers that would hurt consumers and hold back the recovery*." Significantly, her comments followed guidance issued by the UK Competition and Markets Authority (CMA), which had recently in its provisional decision approved a transaction on FFD grounds but shortly after reiterated its framework and stated that *"[t]he Coronavirus (COVID-*

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*19) pandemic has not brought about any relaxation of the standards by which mergers are assessed or the CMA's investigational standards*."

However, even where an FFD argument is unlikely to succeed, companies may instead want to rely on the availability of a broader set of "counterfactual" arguments regarding the competitive landscape and market position of the merging parties in the absence of the transaction. For instance, the Commission's decisional practice indicates that transactions can be cleared where the alternative counterfactual scenario clearly demonstrates that the exit of the target's assets from the market would be more harmful to competition than allowing the transaction to proceed. This kind of arguments may be expected to play a more pronounced role in the aftermath of COVID-19 where merging parties can demonstrate significant and long-lasting changes in market conditions.

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