

SHOULD CHINA HARMONIZE ITS MERGER ASSESSMENT WITH THE U.S. AND EU?

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I. INTRODUCTION

China's Anti-Monopoly Law (AML) came into force in August 2008, and has been deemed "the equivalent of the United States' (U.S.) Sherman Antitrust Act or the analogous portions of the Treaty Establishing the European Community."¹

From the very beginning, the merger control regime in China has been more intensively scrutinized and analyzed than the enforcement of anti-competitive agreements and abuse of dominance, and many of the merger parties are multinational corporations whose mergers would be notified to multi-jurisdictions. Consequently, there were some controversial decisions, such as P3 Alliance, Google/Motorola, Seagate/Samsung, which are divergent from the decisions of the major merger authorities such as the European Union (EU) Commission or the U.S. FTC for the same cases. Some of the decisions made by the Ministry of Commerce (MOFCOM) were fraught with unusual analytical process and remedies. The Chinese competition authorities have also been involved in international cartels (e.g. LCD panel) as well as abuse of dominance cases (e.g. Qualcomm) that were investigated by a number of major jurisdictions. The international profile of the Chinese antitrust authorities is described as "one of the world's youngest and least understood regulators."²

The AML has substantially adopted the EU legal framework and the U.S. competition regime, including not only the statutes and the regulation system, but also the competition agencies' enforcement experience.³ With regard to the AML's ultimate regulatory framework, it is obvious that the structure is more similar to EU regimes, since the AML also categorizes competition controls into three types: antitrust, abuse of dominance, and concentrations.

As this article will illustrate, a combination, a merger, or an acquisition (concentration) will result in an economic concentration by the absorber or acquiring entity and is one of the means by which a

¹ Salil K. Mehra & Meng Yanbei, *Against Antitrust Functionalism: Reconsidering China's Anti-monopoly Law*, 49 VA. J. INT'L L. 380 (2008), available at <http://ssrn.com/abstract=1266796>.

² Javier Blas, *China Clears Marubeni-Gavilon Deal*, FINANCIAL TIMES (Apr. 23, 2013, 6:37 PM), <http://www.ft.com/cms/s/0/032f2e7c-ac33-11e2-9e7f-00144feabdc0.html#axzz2xWuFputW>.

³ MICHAEL FAURE & XINZHU ZHANG, COMPETITION POLICY AND REGULATION: RECENT DEVELOPMENTS IN CHINA, THE US AND EUROPE (Michael Faure & Xinzhu Zhang eds., 2011).

company may wish to implement a restructuring procedure. Merger control has a significant role in today's economies; a fact that is underlined by the ever-increasing number of concentrations that take place. The purpose of merger legislation is to capture concentrations that may have anti-competitive effects on the market structure.

There are several reasons for firms to engage in concentrations. A merger or an acquisition is a common method that firms choose in order to be profitable and to sustain their viability and profitability through time. Mergers consolidate the ownership and control of business assets, including physical assets (e.g., plant) and intangibles (e.g., brand reputation). They can enhance corporate—and wider economic—performance by improving the efficiency with which business assets are used. Further reasons for firms to engage in combinations, mergers, and acquisitions include economies of scale and economies of scope⁴ from which firms benefit, as well as efficiencies stemming from the tendency of some countries to endorse the concept of “national champions.”⁵ Furthermore, mergers may also satisfy the ambitions of executives for more power and greater control.⁶

The recent financial crisis has illustrated the unprecedented difficulties that companies face, as well as the initiatives adopted at corporate and government level, in mitigating its adverse impact. A strategic response for struggling firms, and one of the means of implementing a successful debt restructuring process, is to combine or merge in order to achieve competitive and necessary efficiencies.⁷

⁴ Economies of scale refer to the situation where long-run average costs of production decrease as output rises, see DAVID BEGG ET AL., *ECONOMICS* 109 (5th ed. 1997), and economies of scope refer to the situation where the joint output of a single firm is greater than the output that could be achieved by two different firms each producing a single product (with equivalent production inputs allocated between the two firms), see ROBERT PINDYCK & DANIEL RUBINFELD, *MICROECONOMICS* 227 (Sally Yaggan et al. eds., 4th ed. 1998). Economies of scope are conceptually similar to economies of scale. Economies of scale apply to efficiencies associated with increasing or decreasing the scale of production and refer to changes in the output of a single product type. Economies of scope refer to efficiencies associated with increasing or decreasing the scope of marketing and distribution, as well as changes in the number of different types of products. In addition, economies of scale refer primarily to supply-side changes (such as level of production), whereas economies of scope refer to demand-side changes (such as marketing and distribution).

⁵ The concept “national champion” refers to domestic firms that are able to successfully compete in international markets post-merger. Ioannis Kokkoris, *Assessment of Efficiencies in Horizontal Mergers: The OFT Is Setting the Example*, 30 EUR. COMPETITION L. REV. 581, 581 n.2 (2009).

⁶ Managers may be interested in the size, growth or risk diversification of the company they run. Owners of firms may sometimes give managers incentives in their contracts to achieve some of these targets (e.g., increasing the firm's size in the marketplace). See MASSIMO MOTTA, *COMPETITION POLICY: THEORY AND PRACTICE* 243 n.34 (2004).

⁷ Debra A. Valentine, Former Gen. Counsel, Fed. Trade Comm'n, *Horizontal Issues: What's Happening and What's on the Horizon* (Dec. 8, 1995), available at <http://www.ftc.gov/public-statements/1995/12/horizontal-issues-whats-happening-and-whats-horizon>.

Either a failing firm within a booming industry or firms in a distressed industry will choose to engage in a merger or acquisition as a means, *inter alia*, to ensure their viability or enhance their profitability. Given these enormous transformations, the applicability and importance of the failing firm and failing division defense⁸ might be crucial across all jurisdictions. As this paper will discuss, MOFCOM has not explicitly introduced such a policy in its merger assessment, which shows a clear lack of harmonization across major jurisdictions.

The importance of mergers (and thus of the failing firm defense) for the restructuring process is indicated, *inter alia*, by the U.S. Supreme Court in *United States v. General Dynamics Corp.*⁹ The Court upheld the proposition that private parties, shareholders, and creditors benefit from the merger of a failing firm. The shareholders are unlikely to lose the investment and likely to obtain additional benefits if the merger proves profitable. The creditors will benefit as a result of retaining their rights against the debtor and are likely to be reimbursed for the credit they have provided to the firm. On the contrary, in the event of bankruptcy, they are not likely to be able to recover their claims or investments.

Thus, the restructuring process can be used as a tool to determine if the whole firm or one of its divisions must be merged or acquired by another undertaking in order to maintain its viability and future prospects for profitability. In such a case, the only possible means of restructuring is through a successful concentration. This concentration may need to be assessed by the relevant competition¹⁰ authorities. If the authorities believe that the concentration will have anti-

⁸ An equivalent term is “failing company defense.” In vigorously competitive markets, mergers involving failing firms may often enhance general welfare, either through increasing the efficiency of existing capacity, redeploying that capacity to socially more valued uses, or preserving jobs and having other socially beneficial advantages. Moreover, there might be beneficial effects on economic grounds resulting from, *inter alia*, economies of scale, economies of scope, or other efficiencies, so that prohibiting the deal would add new detrimental economic and social effects to the effect on competition, which would exist in any case. The burden of proof of such welfare benefits lies with the party that claims the defense. If one of the companies in the merger is a “failing firm” or if a division of a firm is failing and would leave the market anyway, then the merger may be deemed not to significantly impede effective competition. The basic requirement is that the deterioration of the competitive structure that follows the merger cannot be said to be caused by the merger. *See generally* Thomas D. Fina & Vishal Mehta, *The Failing Firm Defense: Alive and Well*, ANTITRUST SOURCE (Aug. 2011), http://www.americanbar.org/content/dam/aba/publishing/antitrust_source/aug11_fina_7_26f.authcheckdam.pdf.

⁹ *United States v. Gen. Dynamics Corp.*, 415 U.S. 486 (1974).

¹⁰ This Article will mainly use the term “competition,” which is interchangeable with “antitrust” as used in the United States for the law or authorities that protect trade and commerce from restraints, monopolies, price fixing, and price discrimination. *See* BLACK’S LAW DICTIONARY 104 (9th ed. 2009).

competitive effects, they may block it, resulting thus in the unsuccessful completion of the restructuring procedure.

This article will address the concept of failing firm defense. In particular, it will deal with the implications of the failing firm defense in the EU and the U.S. The reason for choosing these jurisdictions is that both the EU and the U.S. have developed merger legislation and an extensive practice on the topic.

Each of the abovementioned jurisdictions has its own criteria for assessing the failing firm defense argument. The satisfaction of these criteria is an essential factor for a concentration that is likely to have anticompetitive effects to be allowed to proceed. In addition, each of the above jurisdictions has its own legislation regarding merger assessment. It would be necessary for the purposes of this Article and for a complete understanding of the implications of merger legislation, as they are identified through the failing firm defense, to provide a brief analysis of the legislation concerning the assessment of mergers in these jurisdictions. Thus, for each of the above jurisdictions, an analysis of the relevant legislation will be provided. It is imperative to tie the analysis of this legislation with its actual application in cases where the failing firm defense has been invoked. For each jurisdiction, the landmark cases related to the failing firm defense will be analyzed in order to evaluate how the competition authorities and the courts have assessed the failing firm defense. Apart from the analysis of competition legislation surrounding mergers, this article will also include a brief analysis of the restructuring process during which the failing firm defense may be invoked if it is decided that the means of viability of the firm is through a concentration.

This article will begin with a brief analysis of the main issues that surround the failing firm defense doctrine in the context of a concentration/corporate debt restructuring. Then, the notion of failing firm defense will be analyzed in general terms, since more details will be provided in the relevant section of the article dealing with each jurisdiction. The subsequent sections will deal with the different enforcement practices of the failing firm defense and failing division defense doctrines as these two have been developed in the legislation and case law of the United Kingdom, U.S., and China respectively. The penultimate section will expose some of the controversial issues surrounding the success of the failing firm defense doctrine. Finally, some concluding remarks regarding the failing firm defense, and failing division defense doctrines will be presented.

II. THE FAILING FIRM DEFENSE DOCTRINE: A PRIMER

In times of distress, dealing with debt is a complex matter due to the uncertainties of the outcome and the scarce flow of funds. A corporation that is experiencing liquidity problems could find itself in a position where it fails to fulfill its obligations as they fall due but still remains solvent. In this case, the corporation could resort to some types of reorganization procedure to restore its position by reducing its debt burden and regaining a sustainable path. These reorganization procedures could be carried out under the direction of a court or out of court.¹¹

Court-supervised procedures are usually lengthy and demand detailed financial and commercial disclosure of information about the company.¹² This, in many cases, is a recipe for disaster since often bad publicity resulting from the disclosure requirements and the time between the beginning and the end of the reorganization can worsen the company's state of affairs, leading to an irreversible path that ends in bankruptcy. Importantly, creditors may be better off engaging in swift, voluntary, and less cumbersome reorganizations out of court than actual court-supervised proceedings.

Any type of combination, be it an ad-hoc collaborative agreement, joint venture, merger, acquisition, voting control, etc., will result in an economic concentration by the absorber, acquirer, or controlling party and can be seen as a way by which a company may wish to implement a reorganization or restructuring procedure. The failing firm defense refers to "an otherwise problematic merger that 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."¹³

As mentioned above, a significant reason for engaging in mergers is the restructuring of debt of a company that is on the verge of bankruptcy. The restructuring may entail the sale of a loss-making divi-

¹¹ WORLD BANK, OUT OF COURT DEBT RESTRUCTURING 1 (2012), available at <https://openknowledge.worldbank.org/bitstream/handle/10986/2230/662320PUB0EPI00turing09780821389836.pdf>; PHILIP R. WOOD, PRINCIPLES OF INTERNATIONAL INSOLVENCY 36 (2nd ed. 2007).

¹² Wood, *supra* note 11, at 38.

¹³ GUIDELINES ON THE ASSESSMENT OF HORIZONTAL MERGERS UNDER THE COUNCIL REGULATION ON THE CONTROL OF CONCENTRATIONS BETWEEN UNDERTAKINGS, C 31/5 OFFICIAL J. OF EUROPEAN UNION para. 89 (2004) [hereinafter *Guidelines*], available at http://www.antimon.gov.sk/data/files/150_28guidelines-on-the-assessment-of-horizontal-mergers-under-the-council-regulation-on-the-control-of-concentrations-between-undertakings.pdf; see also Vincenzo Baccaro, *Failing Firm Defense and Lack of Causality: Doctrine and Practice in Europe of Two Closely Related Concepts*, 25 Eur. Competition L. Rev. 11, 11 (2004).

sion and, if the company has subsidiaries, the sale of the subsidiary or subsidiaries as a whole. Thus, the failing firm defense and failing division defense can be invoked in cases where this sale is assessed by the relevant antitrust authorities.¹⁴ However, the failing division defense has not been given much acceptance and accreditation by antitrust authorities and courts.¹⁵

Antitrust authorities have recognized the importance of a concentration in avoiding bankruptcy, as well as the impact of the failing firm defense on entry in the market and the role of potential dynamic or innovative efficiencies. Therefore, antitrust authorities have taken into account companies' financial distress in the assessment of mergers involving these failing companies. Both in the EU¹⁶ and U.S.,¹⁷ the failing firm defense is addressed in the merger guidelines. Case law has provided further impetus to the development of the defense in both jurisdictions.¹⁸ In order to accomplish the target of sustaining the competitive structure of the post-concentration market, the antitrust authority must apply a legal substantive test to determine the likelihood of the anti-competitive impact of the concentration, as well as to determine the level and quality of evidence it needs in its assessment of whether the concentration should be prohibited.

Having introduced the fundamentals of the failing firm defense, the next sections of the article will take into account how the doctrine can be used to influence the assessment of a merger. We will analyze the criteria that need to be satisfied for such a defense to be acceptable, how the defense has been invoked in practice in the assessment of merger cases, and whether it has been successful. The merger legislation analysis provided in this article will focus on UK, U.S. and Chinese laws.

III. UNITED KINGDOM

The UK and US Guidelines provide guidance on how mergers are to be evaluated for potential anticompetitive effect. The analytical framework in all major jurisdictions (e.g., the EU, U.S., UK) that is employed in determining whether to challenge a horizontal merger involves:

¹⁴ *U.S. HM Guidelines* para.11.1, 11.2 & 11.3; *EU HM Guidelines* para. 89-91.

¹⁵ Only a handful of cases exist in Europe, the United Kingdom, and the United States. The seminal cases are analyzed in this note. *See infra* Parts II–IV.

¹⁶ *See EU HM Guidelines*, *supra* note 14.

¹⁷ *See U.S. HM Guidelines*, *supra* note 14.

¹⁸ Ioannis Kokkoris, *Failing firm defense under the Clayton Act*, 28 EUR. COMPETITION L. REV. 158 (2007).

“(1) defining the relevant product market and geographic market and identifying the firms that compete in these relevant markets;

(2) whether the merger, in light of market concentration and other factors that characterize the market, raises concerns about potential adverse competitive effects;

(3) assessing the likelihood of post-merger entry by new firms into the markets;

(4) assessing the likely competitive effects of the merger in light of the market concentration and other factors that characterize the markets; and

(5) considering any significant efficiencies resulting from the merger that could not be achieved by other means.”

In the UK, competition authorities have provided guidance on the applicability of the ‘failing firm’ defense, which it has continued to apply very narrowly. The Office of Fair Trading (the OFT) applied four criteria¹⁹ in assessing the failing firm defense, which resemble the ones applied by the European Commission.²⁰ The UK Competition and Markets Authority (CMA), in forming a view on an exiting firm scenario, will consider:

“(1) whether the firm would have exited (through failure or otherwise); if so, and,

(2) whether there would have been an alternative purchaser for the firm or its assets to the acquirer under consideration; and

(3) what would have happened to the sales of the firm in the event of its exit.”

¹⁹ COMPETITION COMM’N & OFT, MERGER ASSESSMENT GUIDELINES (2010), available at http://www.oft.gov.uk/shared_of/mergers/642749/OFT1254.pdf.

²⁰ The European Commission considers the following three criteria as relevant for the application of a “failing firm defense.” 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. There may be the case that buyers may be interested in buying the failing firm’s assets after the firm exits the market. A firm’s exit may also provide the means for new entry in the market. In addition, it may be more beneficial for competition for more than one firm to acquire the assets of the failing firm rather than a single firm acquiring the total of the failing firm’s assets. Third, in the absence of a merger, the assets of the failing firm would inevitably exit the market. Once the conditions for the application of the failing firm defense are fulfilled the merger would not be considered to cause a significant impediment to effective competition in the common market. The three criteria outlined in the Guidelines appear to be the cumulative requirements in order to prove lack of causality between the merger and the worsening of the competitive structure that it would otherwise create. See also *Guidelines*, *supra* note 13, para. 89-90, and Baccaro, *supra* note 13, at 23. The European Commission has accepted the failing firm defense in a small number of cases. For recent examples of such cases, see Nynas AB, *Commission approves acquisition of Shell’s Harburg refinery assets*, EUROPEAN COMMISSION PRESS RELEASE DATABASE (Sept. 2, 2013), http://europa.eu/rapid/press-release_IP-13-804_en.htm, see also *Commission approves acquisition of Greek airline Olympic Air by Aegean Airlines*, EUROPEAN COMMISSION PRESS RELEASE DATABASE (Oct. 9, 2013), http://europa.eu/rapid/press-release_IP-13-927_en.htm.

To accept an exiting firm argument, it must be inevitable that the firm would exit the market and be confident that there is no substantially less anti-competitive purchaser for the firm or its assets.²¹ In addition, the CMA will assess whether the result of the exit of the firm and its assets would be a substantially less anti-competitive outcome compared to the merger. If the bankruptcy and exit of the firm is a less anticompetitive scenario compared to the merger, the merger will not satisfy the failing firm defense.²² The satisfaction of these criteria is an essential factor for a merger, which is likely to have anticompetitive effects, to be allowed to proceed. The aim of this paper is to provide a comparative perspective of the enforcement of failing firm defense in the UK and assess whether the approach towards the failing firm defense has changed during the recent financial crisis.

The OFT has applied the 'failing firm' defense in a number of cases under the Enterprise Act 2002 ("Act") prior to the recent crisis and during the recent crisis. We shall analyze some of the cases where the failing firm defense was successfully invoked, as well as important cases where the failing firm defense was invoked but not accepted by the UK competition authorities. Finally, the paper shall present some reflections on the application of the failing firm defense in the UK.

A. The UK Approach towards Failing Firm Defense before the Financial Crisis

In the years which preceded the financial crisis, the failing firm defense has been invoked in a number of cases but has been rarely accepted by the UK competition authorities. The criteria for the defense are not easily satisfied, as competition authorities carefully assess transactions in order to examine whether any potential competition harm arises from the imminent exit of the failing firm and in fact arises irrespective of the transaction. This section will present, in chronological order, seminal merger cases in the UK where the failing firm defense was invoked.²³

²¹ See MERGER ASSESSMENT GUIDELINES, *supra* note 19, at para 4.3.10.

²² *Id.*

²³ See also Ioannis Kokkoris & Rodrigo Olivares-Caminal, Antitrust Law Amidst Financial Crises (2010).

1. SCR – Sibelco SA and Fife Silica Sands Ltd and Fife Resources Ltd²⁴

This case involves the acquisition of Fife Silica Sands Ltd (FSS) and Fife Resources Ltd (referred together as “the Fife companies”) by SCR Sibelco, a global producer of silica sand, derived products, and other industrial minerals and clays. It was referred to the Competition Commission (CC) for investigation by the Secretary of State for Trade and Industry.²⁵ In 2000, Sibelco acquired Hepworth Minerals & Chemicals Ltd and renamed it Sibelco Minerals and Chemicals Ltd. The company before and after this latter acquisition was referred to as *HMC/SMC*.²⁶ Before being acquired by Sibelco, the Fife companies were owned by a company called Anglo Pacific Group plc.²⁷

There are two broad types of sand product: construction sand and industrial or silica sand. Silica sand is used for glassmaking, but it also includes grades of sand used for several other industrial purposes. The case revolved around primarily the supply of sand for glass manufacture rather than for other industrial purposes. There are three general types of glass for which this kind of sand is used; they are clear-container glass, float or flat glass (for making windows), and colored-container glass.²⁸ Glass sand is considered to be a scarce resource,²⁹ and the reason why Sibelco acquired the Fife companies was because of the potential of significant glass-sand supplies over the long term. In the parts of Fife companies’ site where Sibelco had mineral extraction rights and planning permission, there were potentially large amounts of sand containing large amounts of glass sand.³⁰

FSS was making losses during the years of 1997-1999, and Anglo Pacific attempted to dispose of the Fife companies via an auction by way of tender. Several companies, including Sibelco, demonstrated an interest, but Anglo Pacific did not accept any of the offers made.³¹

It was decided by the CC that the relevant market was the market for all glass sand. This was because there was no scope for substitution on the supply side and, on the demand side, there was the possibility for substitution between glass sand for some different manu-

²⁴ D.J. Competition Commission & Morris, *Sibelco SA and Fife Silica Sands Ltd and Fife Resources Ltd - a Report on the Merger Situation* (2001).

²⁵ *Id.* at para. 3.1-3.2, 3.5.

²⁶ *Id.* at para. 3.3.

²⁷ *Id.* at para. 3.18.

²⁸ *Id.* at para. 4.3-4.4, 4.6.

²⁹ *Id.* at para. 4.8.

³⁰ *Id.* at para. 4.9-4.10.

³¹ *Id.* at para. 3.10, 3.22.

facturing uses.³² The geographic market was held to be England and Scotland but no further. The main users of glass sand were the glass production plants in Yorkshire, but these had, in the past, been supplied from quarries such as Fife in Scotland and Reigate in Surrey. Due to the costs of transportation, international trade in glass sand between Great Britain and Continental Europe was virtually nonexistent. This meant that there was no constraint on UK glass sand prices from imports.³³

It was argued by Sibelco that FSS had lost almost all of its Yorkshire business and was therefore not an effective competitor to HMC/SMC prior to the merger. Thus, the merger did not result in any loss of competition.³⁴ In the winter of 1999/2000, FSS lost two of its former customers, and a third customer reduced its purchases from the company. The loss of these contracts was a result of quality problems with sand that FSS had delivered to these customers the year before and also rising haulage costs, which were reducing the competitiveness of FSS' sand. The CC rejected this argument and found that, despite the loss of much of its Yorkshire business, FSS was in fact competing with HMC/SMC before the merger. Although it was experiencing quality problems, it was still actively negotiating with its customers for orders in 1999/2000. Competition between HMC/SMC and FSS prior to the merger ensured that HMC/SMC's prices were lower than they otherwise would have been and, without FSS active competition for business in the market, HMC/SMC would not have been able to offer these customers such favorable terms.³⁵

Sibelco additionally argued that FSS was a failing firm prior to the merger and that, absent the merger, Anglo Pacific would have withdrawn financial support, and the company would have failed.³⁶ The CC rejected this argument on the basis that FSS' sand quality problems in 1998/1999 were largely due to failures of management, but by the time of the merger, FSS was beginning to prosper from the new management that was implemented in 1999. In addition, FSS could have continued its operations in the short term on a cash-neutral basis. Moreover, the potential of approximately 50 million tonnes of silica sand resources in the adjacent areas to the Burrowine quarry sit could have contributed to its operations in the medium to long term. These resources would have been suitable for both container and float-glass manufacturing, and would have been present

³² *Id.* at para. 4.33, 4.55.

³³ *Id.* at para. 4.43-4.44.

³⁴ *Id.* at para. 3.40.

³⁵ *Id.* at para. 2.64.

³⁶ *Id.* at para. 3.40, 5.16-5.19.

even absent the merger. The CC found that if the Fife companies had not been acquired by Sibelco, another company would have acquired them, and they would have remained a competitive force in the supply of sand for container glass as well as a new competitive force in the supply of sand for float glass.³⁷

It was concluded that glass-sand prices may have been higher as a result of the transaction than they would otherwise have been. Sibelco (through HMC/SMC) had a 71% share by volume of glass sand supplied to third parties in the UK in 1999/2000. Post-acquisition, those shares rose to 86% and its share by value of glass sand supplied increased significantly as well.³⁸ Given that prices in the UK were negotiated individually, no price lists exist,³⁹ and the fact that there were severe constraints on new entry, the merger would remove the competitive constraint of FSS in the market and would likely raise prices.⁴⁰ The merger was also therefore said to operate against the public interest.⁴¹

The CC found that there were no benefits to be gained from the merger. It assessed factors, some of which were submitted by Sibelco, such as Sibelco's reputation in the silica-sand industry, whether the balance of FSS's production between glass sand and construction sand would have been tipped towards glass sand if Sibelco continued to own the Fife companies compared to if another company acquired them, the environmental benefits brought by the Fife companies' site and surrounding area, and employment prospects.⁴²

The CC did not accept the failing firm defense and finally recommended that the appropriate remedy to redress the loss of competition by the merger would be to require Sibelco to divest the Fife companies to a purchaser approved by the Office of Fair Trading. It would be more likely than not that the new owner would sell FSS's output to third party customers.⁴³

³⁷ *Id.* at para. 2.101.

³⁸ *Id.* at para. 4.55.

³⁹ *Id.* at para. 4.63.

⁴⁰ *Id.* at para. 2.

⁴¹ *Id.* at para. 2.124-2.125.

⁴² *Id.* at para. 2.112-2.123, 5.65-5.69.

⁴³ *Id.* at para. 2.142-2.143.

2. Taminco NV of the European methylamines and derivatives business of Air products and Chemicals⁴⁴

The proposed acquisition which was referred on July 16th to the CC was Taminco NV's (Taminco) acquisition of particular assets from the European methylamines and derivatives business, EM&D (Business) of Air products and Chemicals Inc (APCI), and its subsidiary, Air Products (Chemicals) Teeside Ltd (APCT).⁴⁵ The owners of Taminco were Alpinvest Partners Private Equity Firm, a Dutch private equity investor who were the majority holders of Taminco. Taminco specialized in the production of methylamines and derivatives, which were also produced by Air products EM&D Business. Taminco and Air Products both produced three types of methylamines. Methylamines are chemicals which are used as feedstocks for the production of Methylamine derivatives (derivatives). APCI was publicly owned and was listed on the New York Stock Exchange.⁴⁶

The acquisition of EM&D business by Air products in 1998 included the production facility at Billingham, Teeside.⁴⁷ Subsequently in September 2004, during an inquiry, CC Air products noted the closure of its Billingham facility.⁴⁸ The parties APCI and APCT entered into a business sale agreement with Taminco for purchase of the following assets:

(1) Intellectual property, information and know how, good-will in relation to the business.

(2) Stock (raw materials and finished goods), up to a certain monetary amount;

(3) All contracts and arrangements for the sale or swap of methylamines and derivatives, including sale arrangements with customers of the business. Swap agreements with two large chemical producers and the benefit and burden of the toll manufacturing agreement, and business records in relation to the business.⁴⁹

The CC came to the conclusion that the acquisition would result in Air Products ceasing to be distinct. The share and supply test for the supply of derivatives and methylamines was met and the proposed merger would result in a relevant merger situation. The CC

⁴⁴ OFFICE OF FAIR TRADING, THE ANTICIPATED ACQUISITION BY TAMINCO NV OF THE EUROPEAN METHYLAMINES AND DERIVATIVES BUSINESS OF AIR PRODUCTS AND CHEMICALS INC. (2004), available at http://webarchive.nationalarchives.gov.uk/20140402141250/http://www.competition-commission.org.uk/rep_pub/reports/2004/fulltext/495.pdf.

⁴⁵ *Id.* at para. 1.

⁴⁶ *Id.* at para. 5.

⁴⁷ *Id.* at para. 6.

⁴⁸ *Id.* at para. 9.

⁴⁹ *Id.* at para. 7.

added that the geographic market for methylamines was EEA-wide. The CC came to this conclusion on the basis that methylamines and derivatives are hazardous and expensive to transport. As a result there was minimum trading for long distances.⁵⁰ Air products had stated that even if the merger did not take place or there was no sale of any assets, they would still take the decision to withdraw from its E&D business which formed part of that business.⁵¹ An analysis was conducted on the financial performance and the viability of Air Products and EM&D Business, with CC concluding that, in the absence of the merger, Air Products would have closed the Billingham facility and exited its EM&D business.⁵²

The CC also took into consideration the possibility of selling the assets to a third party as part of the exit strategy and came to the view that BASF would be the likely and only party to purchase the assets. In addition, the CC concluded that Air Products would have closed the Billingham facility and exited its EM&D business. In the absence of the merger, it might have had the opportunity to sell its assets only to BASF and not to any other party.⁵³

The CC accepted the failing firm defense and concluded that the merger would not affect competition, as the amount of competitors would remain the same, even absent the merger. The CC's assessment of market shares and market concentration did not indicate that there would be any difference from the counterfactual analysis.⁵⁴ Thus, the CC concluded that as a result of the proposed merger, there would not be any substantial lessening of competition and the merger was cleared.

3. British Salt Limited and New Cheshire Salt Works Limited⁵⁵

On 26 May 2005, the completed acquisition of British Salt Limited of New Cheshire Salt Works Limited was referred to the CC. New Cheshire Salt Works (NCSW) was a small UK producer of vacuum salt, which existed prior to the merger of British Salt and New Cheshire Salt Works Limited. British Salt and Salt Union (limited) were two large UK vacuum salt producers. Prior to the merger, British Salt and NCSW were producers of Pure Dried Vacuum

⁵⁰ *Id.* at para. 11.

⁵¹ *Id.* at para. 17.

⁵² *Id.*

⁵³ *Id.* at para. 19.

⁵⁴ *Id.* at para. 20.

⁵⁵ OFFICE OF FAIR TRADING, BRITISH SALT/ NEW CHESHIRE SALT WORKS LIMITED MERGER INQUIRY (2005), available at <http://webarchive.nationalarchives.gov.uk/20140402141250/http://www.competition-commission.org.uk/our-work/directory-of-all-inquiries/british-salt-new-cheshire-salt-works>.

(PDV) salt and compacted salt. British Salt was also producers of Undried Vacuum salt (UV) and NCSW were producers of pharmaceutical salt. The market analysis used to analyze the effects of competition was the market for PDV and compacted salt.

British salt and NCSW would no longer be distinct, and as a result of the merger, NCSW would cease to exist. Originally, the CC decided that the merger would lead to a substantial lessening of competition, but based upon new evidence this decision was later reversed. The CC concluded that NCSW's former shareholders would have closed NCSW in late 2006 without the merger taking place. Furthermore, following the acquisition of NCSW by British Salt, there was not and was not expected to be a substantial lessening of competition. Thus, the authorities accepted the failing firm defense in this case.

4. James Budgett Sugars Ltd and Napier Brown Foods PLC⁵⁶

This case concerned the acquisition of James Budgett Sugars Ltd (JBS), the second largest non-producing distributor of sugar in the UK, by Napier Brown Foods PLC (NBF), the largest non-producing distributor of sugar in the UK. Because of the transaction, NBF and JBS were no longer distinct. The transaction was referred to the Competition CC by the Office of Fair Trading under section 22 of the Enterprise Act 2002.⁵⁷ The UK turnover of JBS was greater than £70 million, which satisfied the turnover test in section 23(1)(b) of the Enterprise Act, giving rise to a relevant merger situation.⁵⁸ The CC came to the finding that the acquisition had not resulted in a substantial lessening of competition.⁵⁹

NBF acquired the entire issued share capital of JBS from ED&F Man Holdings ("ED&F") Limited and Greencore Group plc. British Sugar plc is the sole UK producer of sugar from beet in the UK. Tate & Lyle plc is the sole UK producer of cane sugar.⁶⁰ This case was considered within the context of the EU sugar regime, established in 1968 as part of the Common Agricultural Policy.⁶¹ The CC's decision also took into account changes that have already occurred in anticipation of the significant reforms, e.g. proposals for future legisla-

⁵⁶ COMPETITION COMM'N, JAMES BUDGETT SUGARS LTD AND NAPIER BROWN FOODS PLC: A REPORT ON THE ACQUISITION BY NAPIER BROWN FOODS PLC OF JAMES BUDGETT SUGARS LTD (2005), available at http://webarchive.nationalarchives.gov.uk/20140402141250/http://www.competition-commission.org.uk/rep_pub/reports/2005/fulltext/500.pdf.

⁵⁷ *Id.* at para. 1.1, 2.4, 2.6.

⁵⁸ *Id.* at para. 3.11.

⁵⁹ *Id.* at para. 6.1.

⁶⁰ *Id.* at para. 3.2, 3.7.

⁶¹ *Id.* at para. 3.1.

tion in May or June 2005 that were announced on 23 November 2004 by the European Commission.⁶²

The product market was said by the CC to be the supply of sugar products to industrial customers.⁶³ Sweeteners were not seen to be included in the same product market due to problems with the technical feasibility of substitution, the economic viability of substitution, and regulatory restrictions.⁶⁴ The supply of sugar to industrial users was considered to be a separate market from retail due to differences in packaging and branding, which enable the two groups to be priced differently.⁶⁵ Different types of sugar, i.e. white granulated sugar, liquid sugar and specialty sugars, were not separate product markets due to the high degree of supply side substitutability.⁶⁶ The geographical market was determined to be Great Britain.

It was found that the most important constraint on imports from other EU countries comes from the pricing policy of British Sugar, which acts as a barrier to entry and ensures that price levels prevent the existence of any sustainable financial incentive for the import of large amounts of sugar into the UK. As a result, the imports of sugar into the UK by other EU sugar producers had not proved to be a significant constraint on sugar suppliers in the UK, and it followed that the geographic market could not be said to be wider than the UK. The CC also followed a decision by the European Commission, which deemed Northern Ireland as a different geographic market from Great Britain.⁶⁷

The CC found that JBS was not a failing firm. NBF argued that JBS purchased sugar from British Sugar and Tate and Lyle at prices that were significantly higher than those of NBF, which made it less competitive in relation to their customers. It had also seen a decline in volumes and total profits over recent years. JBS insisted that it had been following a strategy focused on gross margins and overall profitability, and it believed that, absent the merger, the business would have declined continuously to a certain level but would then continue as a profitable going concern at this level. The CC found that although JBS would have struggled to maintain its previous scale of operation, JBS was competing effectively before the merger, despite its decline in scale.⁶⁸

⁶² *Id.* at para. 3.5.

⁶³ *Id.* at para. 4.10.

⁶⁴ *Id.* at para. 4.8.

⁶⁵ *Id.* at para. 4.9.

⁶⁶ *Id.* at para. 4.11.

⁶⁷ *Id.* at para. 4.14-4.15.

⁶⁸ *Id.* at para. 5.2, 5.3, 5.7.

The competition in the relevant market was such that the extent of competition between the UK sugar producers and resellers was affected by the decisions of the producers, who were relied on for sugar supply by the resellers. Price discrimination existed and UK sugar producers could target customers and impact the ability of resellers to compete with producers as well as with each other.⁶⁹ In this market, resellers negotiated with customers, competing with their suppliers for the sugar they needed to supply to those customers. Although considerations such as the volume of sugar purchased and transport costs were included when establishing prices, there was no real volumetric pricing relationship. Instead, it was a process of bilateral negotiation in which the relative strength of the parties involved could be vital. NBF and JBS would have a competitive advantage over other resellers due to their greater scale of operations if producers chose to price volumetrically.

In assessing the counterfactual to the merger happening, the CC considered the possibility that ED&F might have encouraged JBS to pursue a different strategy and to take advantage of the opportunities that it could provide. It also considered what might have happened if ED&F had partaken in the sale of JBS and what might have happened had there been potential purchasers other than NBF. It was concluded that there was no basis on which it was likely that either of these possibilities would occur in place of JBS continuing to compete under its existing strategy. The relevant counterfactual was found to be that it would have continued to compete with its existing strategy and under the continued ownership of ED&F and Greencore.⁷⁰ Thus, the failing firm defense was not accepted.

The effect of the acquisition was that it would reduce the choice of suppliers that was available to customers. However, the new company would have limited capacity to unilaterally raise prices where it competed with British Sugar and Tate & Lyle. It would also have limited capacity to raise prices in some cases where it would be constrained by competition from other resellers and importers. The CC therefore concluded that the acquisition would have a limited impact on the overall market, there would not be a general rise in prices, and that prices would not be higher than otherwise would have been the case. The CC also found that the merger would not induce a reduction in service, support, product choice or innovation.⁷¹

⁶⁹ *Id.* at para. 5.28.

⁷⁰ *Id.* at para. 5.9, 5.10-5.11.

⁷¹ *Id.* at para. 5.43.

5. Stagecoach Bus and Braddell plc.⁷²

Stagecoach Bus and Braddell completed a joint venture agreement, under which ownership of Scottish Citylink was the subject, with Stagecoach Bus having 35 per cent interest in the company and Braddell having 65 per cent interest. The rights to operate Stagecoach's Motorvator services and Stagecoach's megabus services in Scotland (or originating or terminating in Scotland) were transferred to Scottish Citylink, and Stagecoach became responsible for managing the day-to-day operation of Scottish Citylink.

The CC did not consider that the necessary conditions for a failing firm defense were met, either in relation to Scottish Citylink and the relevant Stagecoach businesses as a whole, or in relation to routes and route groups within those businesses. Based on the financial model of the Scottish Citylink business created by the main parties, it was argued that Scottish Citylink would have become loss-making and unable to meet its financial obligations in 2006, with no viable restructuring options.⁷³ The CC considered that the Scottish Citylink had the financial resources to enable it to fund the cash outflow projected by the main parties for 2006, absent the joint venture.⁷⁴

The CC considered the likelihood of successful restructuring at both the overall business level and on an individual route/route group level. The parties modelled two options for restructuring and argued that Scottish Citylink would not have been able to restructure itself successfully.⁷⁵ The CC noticed that the main parties focused their arguments on Scottish Citylink's ability to restructure through acquisition (with and without overhead reduction) rather than through route reconfiguration. The CC concluded that a fundamental change to Scottish Citylink's subcontracting model was not the only way to restructure the Scottish Citylink business.⁷⁶ As to the Scottish Citylink's service, the CC concluded that the position was unlikely to change within the period relevant to the inquiry.⁷⁷

As regards the restructuring of the Glasgow-Edinburgh route, the CC did not expect that any of these options would have made Motor services profitable. Firstly, the Glasgow-Edinburgh route did not offer much scope for differentiation in terms of stopping patterns,

⁷² Competition Comm'n, *Stagecoach and Scottish Citylink: a Report on the Completed Joint Venture Between Stagecoach Bus Holdings Limited and Braddell Plc in Relation to Megabus.com, Motorvator and Scottish Citylink* (2006).

⁷³ *Id.* at para. 5.13.

⁷⁴ *Id.* at para. 5.14.

⁷⁵ *Id.* at para. 5.17.

⁷⁶ *Id.* at para. 5.18.

⁷⁷ *Id.* at para. 5.20.

routes, interconnections or journey. Secondly, Motorvator had been unable to win a sufficient share of passengers. Thirdly, the Scottish Citylink Glasgow-Edinburgh service appeared to appeal to a broad range of passengers. Therefore, the CC considered it likely that Stagecoach would have withdrawn Motorvator services from the Glasgow-Edinburgh route.⁷⁸

As regards the restructuring of the Saltire Cross route, given the interconnectivity of the route group, Megabus' increasing passenger numbers and revenue, and Stagecoach's statements regarding its intentions, the CC considered that Megabus would have continued to operate at least the same level of services on the Saltire Cross route group.⁷⁹ As to Scottish Citylink's services on the Saltire Cross, the CC considered it likely that Scottish Citylink (or any new owner) would have attempted, and been able, to restructure or reconfigure its business. Thus, failing one of the conditions for acceptance of the failing firm defense the CC rejected the defense.

The reasons upon which the CC based this conclusion included the consideration that the Scottish Citylink might have tried to deal with its profitability problems by restructuring its operations absent the joint venture. In addition, Megabus' share of coach passengers varied considerably across the Saltire Cross flows, which represented a significant demand for Scottish Citylink's services, and this was sufficient for it to make further attempts at reconfiguration. Furthermore, there were some flows and some passengers for which the Megabus model would be unsuitable. Finally, maintaining some services on the Saltire Cross would have brand and reputational benefits for Scottish Citylink.⁸⁰

Regarding the criterion of lack of a less anti-competitive alternative to the joint venture in order to keep competition on the Saltire Cross, the CC considered that a trade sale of Scottish Citylink as a whole to National Express was a possible solution. The reasons were that Scottish Citylink's assets would be attractive to National Express, National Express was released from undertakings not to expand its Scottish scheduled coach services in March 2005, National Express would have had some ability to seek cost savings and additional revenues if it were to acquire Scottish Citylink, and finally the fact that Scottish Citylink was not previously on the market.⁸¹

⁷⁸ *Id.* at para. 5.24-5.25.

⁷⁹ *Id.* at para. 5.27.

⁸⁰ *Id.* at para. 5.33.

⁸¹ *Id.* at para. 5.39.

Following the withdrawal of Motorvator services on the Glasgow-Edinburgh route, the CC concluded that it is more likely that Scottish Citylink would have expanded rather than a third party entering. The CC considered the fact that the withdrawal of Motorvator services would not result in termination of subcontracting arrangements, Scottish Citylink services on this route were well-established, there were no significant seasonal peaks on this route to support temporary entry, potential entrants would be deterred by the history of Stagecoach's failure, any new entrant would be required to make a significant investment in frequent services to compete effectively, and lastly fear of incumbent retaliation would also be a deterrent to entry.⁸²

In the event that Scottish Citylink (or any new owner) were to withdraw Scottish Citylink services from the Saltire Cross, one less anti-competitive option would be to franchise these services. The CC reached this conclusion based on the fact that incumbent subcontractors would have strong incentives to enter as franchisees, franchisees would not have to invest in back-office infrastructure themselves, franchisees would have incentives to maintain services at around the pre-joint-venture levels and network benefits would not be lost.⁸³ Besides, even if Scottish Citylink would not seek to franchise these services, the CC considered that the subcontractors would have incentives, and would be likely, to enter to fill some of the vacuum created in the market.⁸⁴ Thus, the CC did not prohibit the merger on the basis that the merger would not lead to a significant lessening of competition.

6. Anticipated acquisition by Menzies Distribution Limited of Grays Newsagents (York) Limited⁸⁵

This case concerned the acquisition of Grays Newsagents (York) Limited's entire issued share capital by Menzies Distribution Limited.⁸⁶ The former is an independent newspaper wholesaler of national and some regional newspapers while the latter is a leading British newspaper and magazine wholesaler. The OFT had reason to believe that, if this transaction was effected, it would create a relevant merger situation in which the resulting commonly owned wholesale newspaper distribution business would exceed 25% of the supply

⁸² *Id.* at para. 5.44.

⁸³ *Id.* at para. 5.49.

⁸⁴ *Id.* at para. 5.51.

⁸⁵ Office of Fair Trading, Anticipated acquisition by Menzies Distribution Limited of Grays Newsagents (York) Limited (2007).

⁸⁶ *Id.* at para. 1-3.

share in the UK. This satisfied section 23 of the Enterprise Act 2002.⁸⁷ The OFT decided that the merger would not ‘be expected to result in a substantial lessening of the competition within a market or markets in the United Kingdom,’⁸⁸ and that it would therefore not be referred to the CC under section 33(1) of the Act.⁸⁹

In assessing the competitive constraints on the parties, the OFT considered the service market on the basis of newspaper and magazines wholesaling together as well as separately. It decided that the outcome of the assessment would be the same on either basis. It also decided that it was unnecessary to sub-segment newspapers into different types i.e. national, regional, etc., as the outcome would again be the same.⁹⁰ In terms of the geographical market, it was found that the ‘multiples’ (Dawson News, Smiths News, and Menzies) were able to supply wholesaling services across the UK since they had a distribution contract of sufficient scale and duration. The OFT adopted a cautious approach in this case by applying a regional market on the assumption that if there were no concerns regionally in this transaction, then it followed that there would be no concerns nationally.⁹¹

The OFT decided that no competitions concerns arose in regard to magazines since Grays had only bid for two magazine contracts in the York area in 17 years, after which, Grays began to focus on newspapers only.⁹² In regard to newspapers, the OFT concluded that the *‘merger does not present a realistic prospect of a substantial lessening of competition with respect to a large publishers post-merger relative to reasonable definition of the counterfactual, that is the competitive outcome absent the merger.’*⁹³

It was considered that Grays had never competed on a newspaper contract outside of York, so the possible merger effects were limited to the York area. Menzies had only made three bids for newspaper contracts in 12 years, so absent the merger, the constraint imposed by Menzies on Grays wholesaling activity would be relatively limited.⁹⁴ The OFT considered that large publishers would be able to replicate the competitive constraint imposed by Menzies as an alternative bidder on newspaper contracts.⁹⁵ They were able to protect themselves

⁸⁷ *Id.* at para. 6.

⁸⁸ *Id.* at para. 37.

⁸⁹ *Id.* at para. 38.

⁹⁰ *Id.* at para. 10.

⁹¹ *Id.* at para. 14–15.

⁹² *Id.* at para. 18.

⁹³ *Id.* at para. 23.

⁹⁴ *Id.* at para. 19, 32.

⁹⁵ The top four large newspaper publishers account for nearly 75 per cent in terms of Grays’ turnover in the York area.

from adverse merger effects through constraints such as sponsored entry of another multiple, self-supply, and publisher 'change of control' clauses.⁹⁶ The OFT also decided that the critical pre-condition to entry was a wholesaling contract of sufficient scale and duration, and this was left to the large publisher to facilitate new entry.

In terms of competition between the parties for small/medium publishers, the OFT took the view that it was driven by the wholesalers' agreements with large publishers. Negotiations were unlikely to be driven by the small proportion of business that small/medium publishers represent. This limited the parameters of the competition between the parties for this small proportion of business, and therefore the parameters of a possible merger concern were limited. The OFT was concerned, however, about whether these small/medium publishers would have sufficient buyer power post-merger. It was therefore important to consider whether, absent the merger, these publishers would have chosen from two newspaper distributors in York. The OFT concluded there was evidence that this would not occur because Mr. Gray was ill in health and would retire instead of continuing the business and investing capital in new equipment. Finally, the OFT did not consider that the potential buying of the residual Grays business or the liquidation of the business were realistic scenarios, and it would have been inappropriate to adopt a counterfactual in which the Grays business would pass to a supplier other than Menzies.⁹⁷ Therefore '*any reduction in choice for small/medium publishers should not be attributed to the merger as such*'.⁹⁸ Thus, the failing firm defense criteria were taken into consideration in clearing this case but the defense was not formally assessed as a defense to a substantial lessening of competition.

7. Acquisition of GV Instruments Limited by Thermo Electron Manufacturing Limited⁹⁹

GVI and Thermo were the two largest suppliers of Isotope Ratio Mass Spectrometry (IRMS) and there were no other companies of similar size. Mass Spectrometry is an analytical technique used to measure the masses of individual molecules that have been converted

⁹⁶ Office of Fair Trading, *supra* note 85.

⁹⁷ *Id.* at para. 24-26, 35.

⁹⁸ *Id.* at para. 26. In addition, retailers did not have a choice of wholesaler, and this would not change as a result of the merger, so their position would remain unaffected. The OFT also found some benefits of the merger for retailers.

⁹⁹ Diane Coyle, Gr. Brit.: Competition Comm'n, Thermo Electron Manufacturing Limited and GV Instruments Limited merger inquiry: a report on the completed acquisition of GV Instruments Limited by Thermo Electron Manufacturing Limited (2007) [hereinafter Competition Commission].

into ions. This technique has applications in many areas of science and technology, such as in university departments, pharmaceuticals, environmental control, nuclear industry, oil industry, forensic science, and earth science.

The isotope ratio of an element is the quantity of different isotopes in a sample. Measurements of isotope ratios can provide information about a chemical sample, such as its source or age. For example, IRMS can be used to distinguish naturally occurring testosterone from synthetic testosterone for use in sports doping investigations. There are four categories of IRMS instruments: gas IRMS, TIMS, MC-ICP-MS, and Noble Gas MS.

Product specification and functionality play an important role in defining the product market. The IRMS sector is small and mature with global sales of approximately \$50 million a year. GVI, a UK based company, and Thermo, a USA based one, export the bigger percentage of its production. The products in the market under consideration were supplied on a worldwide basis, therefore the CC treated the relevant markets as the global market (each of the four IRMS instruments identifies different markets).

Prior to notification to the competition authorities,¹⁰⁰ Thermo Electron Manufacturing LTD, a subsidiary of Thermo, acquired 100% of the issued share capital of GVI for 11, 6 million pounds. Thermo argued that even though it was already a leading IRMS manufacturer, the acquisition would enable the company to offer additional solutions, in particular, GVI would add the capability of Nobel Gas Isotope Mass Spectrometry to Thermo's product offering. The CC concluded that there was a relevant merger situation within the meaning of the Enterprise Act 2002 (the Act).

In discussing the counterfactual to the merger situation created by Thermo's acquisition of GVI, Thermo submitted that GVI would have failed imminently and gone into liquidation. Thermo recognized the possibility that some of the GVI's assets would have been bought by small UK IRMS competitors, but argued that the increase in the competitive constraints on Thermo which would arise from those acquisitions would not be material. Therefore Thermo believed that its acquisition of GVI did not create substantial lessening of competition compared with the counterfactual.¹⁰¹

As regards the criteria for the failing firm defense, the provided evidence indicated that the business was in rapid decline and led to the conclusion that, in the absence of significant restructuring or sale,

¹⁰⁰ Merger notification is voluntary in the UK.

¹⁰¹ See Competition Commission, *supra* note 99.

it would fail in the near future. In order to survive, GVI needed to enter into two types of restructuring – operational and financial. However, prior to the sale to Thermo, both options were explored but there was no evidence that any decision would occur quickly enough. In CC's view, unless the company received significant equity investments, it remained highly likely that the company would have failed.

As regards the lack of a less-anti competitive alternative, Thermo submitted that it was only approached after a year of discussions that GVI had with other firms. Thermo was the only interested firm in the deal and the most likely prospect of GVI to prevent bankruptcy. In addition, there was no strong prospect that the failure of GVI would have brought a more competitive market structure.¹⁰²

The CC in this case did not accept the failing firm defense and concluded that the acquisition of GVI by Thermo might result in a substantial lessening of competition in two of the concerned markets. It cleared the completed merger after requiring the divestment of the overlap in the two markets concerned.

8. CdMG/Ferryways NV & Searoad Stevedores NV¹⁰³

In June 2007, two wholly owned subsidiaries of CdMG,¹⁰⁴ LineCo NV and TerminalCo NV, acquired Ferryways and Searoad respectively. Although the transactions combined two competitors in the short-sea freight sector routes between UK and Continental ports (with a combined share of approximately 30 per cent), the OFT decided that this merger would not be referred to the CC under section 33(1) of the Act on the ground that the merger would not result in a substantial lessening of competition within a market or markets in the United Kingdom.

The particularly novel circumstances surrounding this transaction was that the financial collapse of the target occurred following its acquisition by Cobelfret, even though Cobelfret claimed that the target was insolvent and had been trading on a fraudulent basis for some time prior to the transaction. Given this special context, the OFT considered whether it would be justified to depart from its

¹⁰² This is due to the rapid growth in oil prices affecting IRMS instruments. Dave Shellock, *Global Overview: Geopolitical Concerns Keep Markets on Edge*, FINANCIAL TIMES (Mar. 30, 2007, 10:10PM), http://www.ft.com/cms/s/0/eba9de10-dee7-11db-b5c9-000b5df10621.html?nclink_check=1.

¹⁰³ Office of Fair Trading, *Acquisition by the CdMG Group of Companies of Ferryways NV and Searoad Stevedores NV* (2008).

¹⁰⁴ The CdMG group of companies (CdMG) is controlled by the Cobelfret group of companies (Cobelfret Group), for the purposes of assessing the relevant market and for the competitive assessment, the OFT has used the term "Cobelfret" to collectively describe both CdMG and the Cobelfret Group.

standard counterfactual of prevailing conditions of competition and assess the transaction on the basis that the target would have stopped trading irrespective of its acquisition by Cobelfret. The OFT requested significant supporting evidence in deciding on this departure from past practice. Cobelfret claimed that the target would have faced serious liquidity issues and could have become insolvent. A number of third parties contacted by the OFT suggested that Ferryways was in a perilous financial position prior to the acquisition.

A post-acquisition audit report undertaken by Ernst & Young supported that there were a number of material irregularities with the financial accounts of the target as of 31 May 2007. Based on this evidence, the OFT concluded that the target would have exited the market regardless of its acquisition by Cobelfret. Based on a series of events, including the loss of loan arrangements, port access arrangements in Belgium and UK, the OFT concluded that there would have been no materially different outcome absent the merger, thus accepting the failing firm defense.

As the analysis of the caselaw in the UK illustrates, the UK competition authorities have been willing to accept failing firm arguments. The approach they follow and the criteria they use are almost identical to the ones that the European Commission uses,¹⁰⁵ although the UK competition authorities frequently frame this analysis in the analysis of the counterfactual of the merger.¹⁰⁶ The UK authorities have been receptive to failing firm defense arguments and have analyzed in detail the criteria that would justify a merger being cleared on the basis of failing firm defense arguments.

After reviewing the “standard” application of the failing firm defense, the next section of the paper will consider the approach of the UK authorities towards failing firm defense arguments during the recent financial crisis. As mentioned above, the failing firm defense concept plays a seminal role in merger assessment, not only at times of economic growth, but also at times of financial crisis.

B. Failing Firm Defense Amidst Financial Crises

The recent financial crisis caused a number of mergers to occur so as to avoid a potential bankruptcy of the target. This led to the reassessment of a number of arguments on which merger assessment was based. One of the most important arguments that were tested was the failing firm defense.

¹⁰⁵ See Ioannis Kokkoris, *Failing Firm Defense in the European Union: A Panacea for Mergers*, 27 EUR. COMPETITION L. REV., 494-509 (2006).

¹⁰⁶ See OFFICE OF FAIR TRADING, *MERGERS: SUBSTANTIVE ASSESSMENT GUIDANCE* (2003).

In a speech concerning the financial crisis, Neelie Kroes,¹⁰⁷ European Commissioner for Competition Policy said the following:

“The Commission is committed to continue applying the existing rules, taking full account of economic environment.

That means the Commission can and will take into account the evolving market conditions and, where applicable, the failing firm defense.

The existing rules allow the Commission to permit take-overs to be implemented without having to wait for the Commission’s approval in cases where there is urgency and where there are no ‘a priori’ competition concerns.

The Commission can indeed grant derogations from the standstill obligation, pending a definitive outcome of the proceedings, so as to enable the immediate implementation of the transactions which are part of rescue operations”.

During the recent financial crisis, the OFT in the *Restatement of OFT’s position regarding acquisitions of ‘failing firms’*¹⁰⁸ clarified the application of the ‘failing firm’ criteria. Firstly, the OFT will consider the inevitability of the target business exiting the market, such as cash flow difficulties or an inability to raise capital. In addition, the OFT needs to consider the realistic availability of alternative purchasers for the target business. These two criteria will not be relaxed due to prevailing economic and market conditions.

The OFT adds that 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. Where the target business is failing and there is genuinely only one purchaser for the business in question, merging parties

¹⁰⁷ Neelie Kroes, *European Comm’n for European Policy, Dealing with the Current Financial Crisis* (Oct. 6, 2008) (transcript available at http://europa.eu/rapid/press-release_SPEECH-08-498_en.htm?locale=en).

¹⁰⁸ OFFICE OF FAIR TRADING, *RESTATEMENT OF OFT’S POSITION REGARDING ACQUISITIONS OF ‘FAILING FIRMS,’* (2008), available at http://webarchive.nationalarchives.gov.uk/20140402142426/http://www.offt.gov.uk/shared_offt/business_leaflets/general/offt1047.pdf.

must be aware that they will need to provide compelling evidence of this to the OFT if they are to avoid a reference to the CC.

This section will present a number of merger cases that occurred during the crisis where the failing firm defense was invoked and will assess whether the policy of the UK competition authorities towards the failing firm defense changed as a result of the recent financial crisis.

1. Smiths News Trading Limited of Certain Assets of Surridge Dawson Limited

In this merger, the OFT accepted the failing firm defense.¹⁰⁹ Smiths News Trading Limited (Smiths) was active in the supply of wholesale newspaper and magazine distribution in the UK, with 44 distribution centers throughout England and Wales. It delivered newspapers and magazines to approximately 25,000 retail customers daily. Surridge Dawson Limited (Dawson) was also active in the supply of wholesale newspaper and magazine distribution in the UK, with 15 full branches and 14 sub-depots. The merger involved the acquisition by Smiths of the physical assets required to supply newspaper and magazine distribution services in the territories in which Smiths had been awarded the future distribution contracts.

Smiths and the Dawson Assets overlapped in the supply of wholesale newspaper and magazine distribution services to publishers and to retailers. Magazine and national newspaper wholesaling differed on the demand-side mainly in terms of delivery time, with newspaper delivery being much more time sensitive. There were also some important supply-side differences in terms of the more sophisticated systems required to process magazine orders but the OFT argued there was supply-side substitution. The OFT assessed the transaction under the frame of reference of magazine wholesaling services to retailers, as well as newspaper and magazine wholesaling services to publishers.

The OFT took into account the failing firm defense arguments and considered the transaction's impact relative to the situation that would prevail absent the transaction. The OFT considered that the possible range of counterfactuals to the acquisition might be that Dawson would be preserving the Dawson Assets until the next tender round, another entrant would acquire the Dawson Assets and preserve them until the next tender round, or that the Dawson Assets

¹⁰⁹ OFFICE OF FAIR TRADING, COMPLETED ACQUISITION BY SMITHS NEWS TRADING LIMITED OF CERTAIN ASSETS OF SURRIDGE DAWSON LIMITED, ME/4179/09, available at http://webarchive.nationalarchives.gov.uk/20140402142426/http://www.oft.gov.uk/shared_oft/mergers_ea02/2009/smiths.pdf.

would exit the market. The OFT has in essence applied the same criteria used in a failing (or exiting) firm case and to the same evidentiary standard to determine whether there is causation between the transaction itself and any potential lessening of competition. With the lack of these two factors, the transaction should be cleared on the basis of the failing firm defense.

The OFT concluded that due to the Dawson's inability to continue servicing the remainder of the contracts, combined with its severe financial difficulties and the lack of ability or incentive to maintain the Dawson Assets, Dawson would not have retained the Dawson Assets until the next tender round in 2014 and it was unrealistic to expect that an alternative entrant would purchase the Dawson Assets and maintain them until the next tender round. In addition, Dawson's administrators had confirmed that any assets not acquired by Smiths were in the process of being disposed. Thus, the OFT concluded that this acquisition met the failing firm defense criteria, and the deal was cleared.

2. HMV/ZAVVI

In this case, the OFT cleared HMV plc's purchase of 15 former Zavvi stores under the "failing firm defense."¹¹⁰ HMV Group plc was active in selling entertainment products. It retails pre-recorded music, films, electronic games and peripherals, MP3 players and a small range of books. Zavvi Retail Limited was also active in the sale of a broadly similar range of entertainment products to those sold by HMV as described above.

The OFT reviewed this case on its own initiative. The OFT deemed that each individual Zavvi store was an enterprise and also applied its discretion to treat the acquisition of all 15 stores together, as a single merger.

Zavvi entered into administration on 24 December 2008. Zavvi (and its predecessor, Virgin Megastore) traded at a loss for a number of years. Its business was highly seasonal, with peak demand occurring across November and December. However, it experienced considerable cash flow difficulties when the sole supplier of Zavvi, went into administration on November 27, 2008. As a result, Zavvi was not able to source stock in its usual way and faced difficulty obtaining stock at acceptable prices or on favorable credit terms. The OFT considered that an appropriate candidate frame of reference could be the bricks and mortar retailing of entertainment products including

¹¹⁰ See *OFT clears acquisition of Zavvi stores by HMV under 'Failing Firm' Analysis*, BLOOMBERG (Apr. 28, 2009), http://www.bloomberg.com/apps/news?pid=newsarchive&sid=a.tj5tn_3zXw.

pre-recorded music, films, electronic games and peripherals on both a national and local basis with competition taking place at a local as well as national level.

The OFT considered it appropriate in this case to focus on the applicability of an exiting firm analysis (also known as failing firm defense). It considered that it would be disproportionate to require the parties to carry out an in-depth analysis in relation to each of the overlap stores, given the clarity of evidence indicating the application of the failing firm defense that the OFT was able to attain at an early stage of the investigation. The OFT noted though that this will clearly not be the case in all failing firm type situations.

The OFT investigated carefully with the administrator of Zavvi whether there was any prospect that Zavvi could have emerged from administration, potentially in a re-organized form. Zavvi had been experiencing significant losses for a number of years, and failure was a possibility even before the collapse of its supplier. The OFT was informed by the administrator that a going concern sale was not achievable for a variety of other reasons, including the difficult economic and market conditions and the prohibitive level of investment required to turn around the Zavvi business. The OFT further believed that there was an absence of liquidity in funding markets to support an acquisition by trade, private equity style interest.

As regards availability of alternative purchasers, the owners of the overlap stores informed the OFT that they did not undertake a public marketing campaign for the stores given that they were city center locations, and only a limited number of parties were likely to be interested in them. The OFT did not believe that the closure of the overlap stores and the exit of the assets in the local markets would have been a substantially better outcome than the acquisition of the stores by HMV. The OFT would not accept that a lower purchase price is sufficient to render an alternative purchaser “unrealistic.” As mentioned above, the OFT may also consider that failure of the business, leaving the remaining competitors to compete for its assets and market share, is a more competitive outcome.

The HMV/Zavvi merger was cleared on the basis of failing firm defense although, in accordance with its restated policy,¹¹¹ the CC had decided not to accept the failing firm defense in an earlier case – the *Holland&Barrett/Julian Graves* merger.¹¹² In that case, the OFT believed that the merger would result in a substantial lessening of competition as the OFT found evidence of other viable purchasers.

¹¹¹ OFFICE OF FAIR TRADING, *supra* note 108.

¹¹² OFFICE OF FAIR TRADING, *HOLLAND&BARRETT/JULIAN GRAVES MERGER* (Aug. 20, 2009).

3. Stagecoach Group plc / Eastbourne Buses Limited, and Cavendish Motor Services¹¹³

Stagecoach Group PLC (Stagecoach) was a wholly-owned subsidiary of the Stagecoach Group, an international public transportation group, with operations in the UK, USA and Canada. Eastbourne Buses Limited (Eastbourne Buses) provided local bus services in the town of Eastbourne, the neighbouring town of Hailsham, and East Grinstead. Cavendish Motor Services (Cavendish) provided local bus services in the town of Eastbourne and neighbouring town of Hailsham. Cavendish was a wholly-owned subsidiary of Renown Coaches Limited (Renown), a bus operator based in Bexhill, East Sussex. The OFT argued that Eastbourne Buses and Cavendish overlapped in the supply of local bus services. It added that Eastbourne Buses and Cavendish were the only suppliers of commercial local bus services in Eastbourne, with Eastbourne Buses operating 13 routes and Cavendish operating eight. The mergers therefore resulted in a merger to monopoly ratio, on all but three overlap flows, of 67 altogether. The OFT believed that competition between Eastbourne Buses and Cavendish occurred on a network-wide basis within the town of Eastbourne rather than on a flow-by-flow basis. A 'flow' was defined as a connection between two specific points.

The OFT emphasized that it requires strong and compelling evidence in any merger where the parties invoke the failing firm defense.¹¹⁴ This evidentiary standard is required in relation to 'failing firm' cases and is applicable also in cases where parties claim that competition that existed pre-merger would not in any event have been 'sustainable' going forward such that one party would have exited the market.

The OFT could not conclude that only one operator would have remained in Eastbourne absent the mergers and added that Stagecoach's rationale in buying both companies was that it believed Cavendish was viable and would continue to operate as a competitor, at least in the short-term. The OFT added that there were rival bidders for both the Eastbourne Buses and Cavendish businesses. Thus, the OFT could not conclude that absent the acquisitions by Stagecoach there would inevitably have been only one bus operator in Eastbourne and rejected the failing firm defense referring the mergers to the CC.

¹¹³ OFFICE OF FAIR TRADING, COMPLETED ACQUISITION BY STAGECOACH GROUP PLC OF EASTBOURNE BUSES LIMITED AND CAVENDISH MOTOR SERVICES LIMITED, ME/4030/09 & ME/4031/09 (Oct. 22, 2009).

¹¹⁴ OFFICE OF FAIR TRADE, *supra* note 108.

4. Stagecoach Group/Eastbourne Buses Limited-Cavendish Motor Services, Stagecoach Group/Preston Bus Limited

In two other merger cases in the market for local bus services, the OFT referred both to the CC.¹¹⁵ Stagecoach acquired first Eastbourne Buses and Cavendish Motor Services. Then in January 2009, Stagecoach also acquired Preston Bus. The OFT methodology to study the competitive effects of transport mergers is a flow-by-flow-analysis, accompanied by the use of filters to screen out the flows on which anticompetitive effects are unlikely to be felt.

Stagecoach unsuccessfully invoked the failing firm defense to have the Preston Buses and Eastbourne Buses mergers cleared. In the absence of the merger Preston Bus might have probably stayed in the market, though in a reduced size, or its assets might have bought by another bus operator. In Eastbourne Buses the failing firm defense was not accepted as Stagecoach considered Cavendish as a viable concern, which, absent the merger would have continued on trading, albeit less frequently.

5. Stagecoach Group Plc / North Devon business and assets of First Devon And Cornwall Limited¹¹⁶

Stagecoach Group plc (Stagecoach) operated registered local bus services of a commercial and tendered nature. First Devon and Cornwall Limited (First) was a wholly owned subsidiary of First-Group PLC. The parties were both active in the supply of local bus services in the relevant area. The parties overlapped in the provision of local bus services (commercial and tendered) and competition for tender contracts in North Devon. The OFT assessed the impact of the transaction on a flow-by-flow basis, where a 'flow' was defined as a connection between two specific points. This approach was taken because passenger demand was for travel between two points.

The OFT considered that the balance of the evidence supported First's argument that it would have exited the North Devon area absent the merger. However, given the OFT's findings on the potential for alternative purchasers for the North Devon Business, the OFT did not conclude whether an exit would have been inevitable.

Three bus operators in the region informed the OFT in its market testing that they might have been interested in acquiring the whole or part of the North Devon Business had they been offered the opportunity of doing so. These expressions of interest casted doubt on

¹¹⁵ OFFICE OF FAIR TRADE, *supra* note 108.

¹¹⁶ OFFICE OF FAIR TRADE, ANTICIPATED ACQUISITION BY STAGECOACH GROUP OF THE NORTH DEVON BUSINESS AND ASSETS OF FIRST DEVON AND CORNWALL, ME/5435-12 (Aug. 28, 2012).

First's submission that it was abundantly clear no one else would have wished to acquire the North Devon Business. Each of these three operators had very limited overlaps with the North Devon Business (in contrast to Stagecoach's own position).

Accordingly, the OFT considered that any of these operators would have been a substantially less anti-competitive purchaser than Stagecoach. Since the OFT was unable to conclude that there would not have been a substantially less anti-competitive purchaser for the North Devon Business absent the merger, it adopted prevailing competitive conditions as the appropriate counterfactual for assessing the transaction. The OFT did not accept the failing firm defense and referred the acquisition to the CC pursuant to section 33(1) of the Act.

6. Anticipated acquisition by Lloyds TSB Group plc (Lloyds) of sole control of HBOS plc (HBOS)¹¹⁷

This merger involved an unexpected "intrusion" of the OFT. The proposed merger was announced on 18 September 2008. On the same date, the Secretary of State, under Section 42 (2) of the Enterprise Act 2002, issued a notice of public intervention to the OFT. The OFT received an informal merger submission from the parties on October 8. On the same date, the Treasury announced some further measures concerning the stability of the financial system, stating that it was the government's intention to provide liquidity, make available capital, and any other measure required to ensure that the banking system was able to overcome the crisis. On October 13, Her Majesty's Treasury (HMT) announced that it would implement these measures, particularly to help support the long-term strength of the economy. In particular, it stated that capital investments were going to be made in HBOS and Lloyds, subject to the completion of their proposed merger.¹¹⁸

On 24 October, the specification of the stability of the financial market as a public interest came into force through Section 58 of the Enterprise Act. The UK government introduced this Section in order to deprive the designated competition authority of the power, i.e. the OFT, to be the decision maker in this merger.

The OFT considered that there was a prospect of substantial lessening competition in three areas, namely personal current accounts,

¹¹⁷ OFFICE OF FAIR TRADE, ANTICIPATED ACQUISITION BY LLOYDS TSB GROUP PLC OF HBOS PLC, ME/3862/08 (Oct. 31, 2008) (The full report has been archived, introduction available at http://webarchive.nationalarchives.gov.uk/20140402142426/http://www.of.gov.uk/advice_and_resources/resource_base/Mergers_home/LloydsTSB).

¹¹⁸ IOANNIS KOKKORIS & OLIVARES-CAMINAL R., ANTITRUST POLICY IN THE WAKE OF FINANCIAL CRISES (2010).

SME banking and mortgages. Moreover, the OFT had medium to long-term concerns in relation to these product areas, and short term concerns in relation to the first two areas. The OFT considered mainly the two counterfactual situations to this merger going ahead¹¹⁹:

(1) HBOS would not have been allowed to fail, and the UK Government (“Government”) would have intervened with some form of aid. In this case, the OFT considered that HBOS would still represent an important competitive force in the market.

(2) However, the Government would have eventually withdrawn such support, either leaving HBOS independent or in the hands of a third party. In such case, the OFT considered that it would still represent a significant competitive force in the market.

In case one of the parties involved in a merger is failing, certain pre-merger conditions of competition may not prevail. In this regard, the parties argued that particular care should be taken regarding HBOS, whose failure would have disastrous consequences in financial stability. The parties stated that it was impossible to evaluate the possibility that HBOS would be allowed to fail. The OFT decided that it was not appropriate in this case to apply the failing firm defense, since it was realistic that HBOS would have been allowed to fail or its assets allowed to exit the market. The parties argued that it was not realistic either to consider the prospect of reorganizing HBOS’ business. In this regard, they also stated that it would have been possible to sell off its assets; however, such measure would have necessarily meant incurring substantial losses.

The OFT also analyzed the possibility of a third party other than Lloyds purchasing HBOS. The OFT considered that any purchaser of the bank would be a “no overlap” bidder, and any merger which could give rise to competition problems could be cleared with remedies. The parties further argued that a more realistic counterfactual scenario (to HBOS remaining independent) was that the Government would have intervened absent the proposed merger (most likely by nationalising HBOS), and that this would probably have led to structural limitations on the ability of HBOS to compete. In this regard, the OFT considered, despite the fact that some state aid restrictions could be applied with a negative impact in HBOS’s competing ability, that it would still be an effective competing force in the market, even in the case of receiving such Government aid.

¹¹⁹ OFFICE OF FAIR TRADE, OFT REPORT TO THE SECRETARY OF STATE ON LLOYDS/HBOS MERGER, *available at* http://webarchive.nationalarchives.gov.uk/20140402142426/http://www.oft.gov.uk/advice_and_resources/resource_base/Mergers_home/LloydsTSB.

The OFT considered that in the short or medium term the Government would have withdrawn its financial support to HBOS once the financial crisis was over, leaving HBOS as an independent entity again. The OFT added that HBOS would have represented a significant competitor in the market in the case of being owned by a no overlap third party, after the Government aid.

The OFT advised the Secretary of State under section 44 of the Act that the test for reference is met on competition grounds. Thus, the merger should be referred to the CC for a detailed assessment which could last up to 6 months, a timeframe within which HBOS would not be viable. The Secretary of State did not adopt the OFT's recommendation and instead cleared the merger in order to enhance the stability of the financial market. This merger did not satisfy the failing firm defense criteria, although such criteria were eloquently made by the parties.

In this case, the UK government intervened in the absence of the merger satisfying the failing firm criteria, and approved this merger as it considered failure of this deal would be detrimental for financial stability in the UK. The *HBOS/Lloyds* merger is a clear example of the direct and unprecedented intervention of the UK government in the assessment of mergers during the recent financial crisis. Prior to this merger, mergers in the financial sector were strictly within the remit of the OFT and the CC. In this case, the UK government intervened¹²⁰ and allowed the merger despite the fact that the merger was giving rise to competition concerns. In fact, the Government enabled the Secretary of State to decide on the merger and suspend competition rules in order to maintain general financial stability. The merger was cleared on the basis of the severe financial situation of HBOS along with the disadvantages that a failure of a bank entails in terms of consumer confidence.¹²¹

In the aftermath of this merger, and a result of the state aid assessment by the European Commission, the European Commission imposed a divestiture plan of 600 branches and an asset reduction programme by 181 billion pounds as a result of the state aid that was granted by the UK Government to Lloyds in order for the latter to acquire HBOS.

¹²⁰ The UK government could intervene in merger control decisions only in respect to national security and media-related mergers, but in this case the government decided to extend the situations where it could intervene by including the category of 'maintaining the stability of the UK financial system' in order to be able to intervene in the *Lloyds TSB/HBOS*.

¹²¹ It has to be stressed though that in the particular case the failing firm defense was not accepted and therefore was not the basis for the clearance of the merger. The OFT provided a detailed analysis of the failing firm defense.

7. University College London Hospitals / NHS Foundation Trust

In the acquisition University College London Hospitals NHS Foundation Trust (UCLH)/ Foundation Trust of Royal Free London NHS Foundation Trust's neurosurgery services¹²² the OFT considered and rejected the application of the failing firm defense (or exiting firm defense).

UCLH NHS Foundation Trust was a foundation trust based in London. It provided a range of acute and specialist healthcare services from eight hospitals with neurosurgery services provided at the National Hospital for Neurology and Neurosurgery (NHNN). Royal Free London NHS Foundation Trust (RFH) was a foundation trust based in London. It provided acute and specialist healthcare services including neurosurgery. The neurosurgery unit at the RFH included intracranial, complex and routine spinal work, and all acute neurosurgery activity.

The parties are both acute hospital service providers with activities in neurosurgery. Neurosurgery is a clinical specialty related to the surgical treatment of disorders of the brain, spinal cord, and other parts of the nervous system. Neurosurgical services in the UK are provided from regional neuroscience centers servicing populations of between 1 and 3.5 million.

The OFT's starting point was to consider the narrowest set of substitute clinical services from the demand-side (patient/commissioner perspective) in which the merger parties overlap and then to consider the incentives of a hypothetical monopolist to raise prices, lower quality or reduce access. As the OFT mentioned, in the case of NHS hospital mergers, demand-side substitution may relate to decisions by the patient or the GP making the referral to the secondary care provider (secondary care), the consultant/trust making a referral for a tertiary (or specialist) treatment (tertiary/specialist care), or the payer (the NHS commissioners).

Then, an analysis of the supply-side was conducted, which involves an examination of the extent to which a supplier of alternative clinical services would have the ability and incentive to switch, in an easy and timely manner (typically within two years), to the provision of a service or procedure in response to a decrease in the quality of the services provided by a hypothetical monopolist supplier.

¹²² OFFICE OF FAIR TRADE, ACQUISITION BY UNIVERSITY COLLEGE LONDON HOSPITALS NHS FOUNDATION TRUST OF ROYAL FREE LONDON NHS FOUNDATION TRUST'S NEUROSURGERY SERVICES, ME/5574-12 (Mar. 6, 2013).

A simple way to describe this segmentation is by reference to the suppliers / parties involved at each stage of the provision of a clinical service to a patient, namely:

(1) primary care, where a patient presents to a GP with a medical problem (patient and GP);

(2) secondary care, where the patient is referred from a GP to a consultant (patient, GP or other healthcare professional and consultant); and

(3) tertiary (or specialist) care, where the patient is referred from a consultant to a specialist consultant (patient, consultant and specialist consultant).

Consistent with the OFT's approach in its decision in *Royal Bournemouth/Poole*,¹²³ the OFT asked the parties to provide catchment area analysis for 80 per cent of their neurosurgery activity. In addition, by way of a sensitivity check, the OFT also asked the parties to provide the 70 per cent and 90 per cent catchment areas for their activities. The OFT considered that the narrowest relevant geographic scope was the Primary Care Trust (PCT) areas in North London and Hertfordshire. It was not necessary to define a relevant geographic market for UCLH because the OFT's main theory of harm pertained to the constraint the merger removed on RFH.

The OFT was concerned about the loss of the constraint that UCLH places on RFH. It analyzed the following elements in assessing the level of closeness between the parties: the geographic proximity of the parties' neurosurgery units, parties' internal documents, the level of care quality and likely diversion (switching) between the parties.

The OFT believed that there would be sufficient remaining competitive constraints post-transaction with a comparable neurosurgery offering to mitigate any unilateral effects. The parties submitted that there would have been a transfer to UCLH in an unplanned way in the absence of a structure/planned transfer of neurosurgical services. The parties stated that a structured transfer of these specialist services was required for patient safety.

As mentioned above, in assessing the 'failing firm' defense, the OFT will consider¹²⁴:

¹²³ OFFICE OF FAIR TRADING, ANTICIPATED MERGER BETWEEN POOLE HOSPITAL NHS FOUNDATION TRUST AND ROYAL BOURNEMOUTH AND CHRISTCHURCH HOSPITALS NHS FOUNDATION TRUST, ME/5351/12 (Feb. 7, 2013), available at http://webarchive.nationalarchives.gov.uk/20140402142426/http://www.offt.gov.uk/shared_offt/mergers_ea02/2013/NHS-foundation-trusts.pdf.

¹²⁴ COMPETITION COMM'N & OFT, *supra* note 19.

- (1) whether the firm would have exited (through failure or otherwise); and if so,
- (2) whether there would have been an alternative purchaser for the firm or its assets to the acquirer under consideration; and
- (3) what would have happened to the sales of the firm in the event of its exit.

The OFT mentioned that the exiting firm scenario may be satisfied where an entity is likely to exit for financial or other strategic reasons. In many cases, an entity can show that it is failing financially but there will be other cases where exit is inevitable for strategic or other reasons. The parties stated that there were strategic reasons, based on clinical and funding concerns, for exit of the RFH neurosurgery services being a likely possibility within the foreseeable future.

Even if the OFT could predict that exit of RFH's neurosurgery services would have occurred absent the merger, the OFT would need to satisfy itself that there was no less anti-competitive purchaser who could have credibly acquired the services. The evidence indicated that other potential hospitals were not considered and therefore it had not been possible to satisfy this limb of the test. Thus, the OFT rejected the failing firm defense argument.

C. The UK approach to Failing Firm Defense amidst crises

Mergers and joint ventures in impacted industries are a necessary part of this world, and if the antitrust laws are perceived to be an undue barrier to such combinations, then a legislative affirmation that this is not the case would be desirable. The courts, mainly in the EU, have in most instances been negative towards the failing firm defense.¹²⁵ However, there have been some landmark cases, analyzed in this paper, which have formulated the development of the concepts of failing firm defense. These decisions by the competition authorities and courts, along with the guidelines issued by the competition authorities, have provided the framework within which the request for such a defense must be assessed.

As this paper has indicated, the failing firm defense is part of competition law jurisprudence. With increased globalization of the marketplace and the increased competitive pressures as a result of it,

¹²⁵ Albeit a small number of cases where the defense has been invoked. Cases where the defense has been invoked and not accepted by the European Commission include: Case No IV/M.890 - Blocker/Toys 'R' Us, OJ [1998] L 316/1, Case No IV/M.877 - Boeing/McDonnell Douglas, [1997] OJ L336/16, Case No IV M.1221 Rewe/Meinl, [1999] OJ L 274/1, COMP/M.2810 Deloitte & Touche/Andersen UK, COMP/M.2824 Ernst & Young/Andersen Germany, COMP/M.2816 Ernst & Young/Andersen France.

failing firm defense will arise more frequently. Especially at times of financial crises, competition authorities should take into account the viability and profitability of the merging firms and assess the transaction accordingly. The rigorous competitive effects analysis undertaken by the enforcement authorities is sufficient to ensure that valid claims of failure and changing market conditions are carefully considered and evaluated.¹²⁶

1. The Approach during Financial Crisis

The assessment of a merger involving a failing firm should not be assessed in the same way as a merger which does not involve failing firms. As mentioned above, where a merging firm is failing, pre-merger competitive conditions should not be used as a benchmark. If the competition authorities reject one or more mergers falling below an unsustainable benchmark, the result could well be a liquidation expected to produce greater harm to competition than is predicted to result from one or more of the rejected mergers. If one of the parties to a merger is failing, pre-merger conditions of competition might not prevail even if the merger was prohibited. In such case, the counterfactual might need to be adjusted to reflect the likely failure of one of the parties and the resulting loss of rivalry.¹²⁷

Any difference in the approach of the UK competition authorities towards the failing firm defense in periods of financial crises is illustrated by the assessment of the *Lloyds/HBOS* merger. It cannot be emphasized more that once a bank or a financial institution of the size of HBOS or Lehman Brothers is involved, there are very few banks big and strong enough to act as an acquirer and hence the choice open to the authorities is extremely limited. Thus, the strict application of failing firm defense criteria becomes more complicated and likely to be unsuccessful, resulting in the bankruptcy of the failing undertaking and in the ensuing adverse implications for the relevant market.

In *Lloyds/HBOS* merger, the UK competition authorities did not amend their policy and approach towards failing firm defense. The OFT in the *Restatement of OFT's position regarding acquisitions of 'failing firms'*¹²⁸ clarified the application of the 'failing firm' criteria amidst the recent financial crisis. However, the UK government in-

¹²⁶ LIZABETH LEEDS, ASS'T ATT'Y GEN, FA, THE FAILING FIRM DEFENSE, FEDERAL TRADE COMMISSION HEARINGS ON CHANGING NATURE OF COMPETITION IN A GLOBAL AND INNOVATION-DRIVE AGE (Nov. 14, 1995).

¹²⁷ OFFICE OF FAIR TRADING, *supra* note 106, at 34.

¹²⁸ OFFICE OF FAIR TRADING, *supra* note 108.

tervened and approved this merger as it considered failure of this deal would be detrimental for financial stability in the UK.

In order to emphasize the importance of the involvement of the UK government, in 2001 the Secretary of State adopted a diametrically opposite view in the planned acquisition of Abbey National by Lloyds. The merger would lead to efficiency gains but it is believed that these would not be passed on to consumers in the form of reduced prices. The merger would, moreover, have an adverse effect on consumer choice, which would be material in relation to the Personal Current Accounts and SME markets.¹²⁹ The concern at the time was that no remedies could have offset the potential anticompetitive effects deriving from this acquisition due to the highly oligopolistic structure of the British banking sector. In that case, *inter alia* the post-merger entity would have lower market share than Lloyds/HBOS. As the OECD Report states, the dramatic shift observed in the case of Lloyds/HBOS is witness to the extraordinary difficulty of the situation and the consequent subordination of competition concerns to stability concerns, at least in the short run.¹³⁰

A lenient approach towards mergers involving failing and financially distressed firms can balance the losses from increasing concentration post-merger with the gains from hastening entry and competition.¹³¹ Considering the likely anti-competitive outcome of allowing a merger involving a failing firm and the counterfactual of blocking the merger and the firm exiting the market, an argument can be made in favor of a more lenient policy towards the failing firm defense. It could be characterized as permitting the defense to be used by severely distressed as well as by imminently failing firms, and it may yield social benefits resulting in more effective competition in the long run.

Thus, UK competition authorities might consider being less restrictive and more likely to accept the defense, not only to mergers involving failing firms, but also to mergers involving divisions of failing firms, as well as failing divisions of firms. However, some assurance may be needed that the division's failing status is not

¹²⁹ PRESS NOTICE, DEP'T OF TRADE & INDUS., EXCERPTS FROM THE REPORT SUMMARY (FEB. 23, 2001); REPORT OF THE COMPETITION COMMISSION ON THE PROPOSED MERGER OF LLOYDS TSB GROUP PLC AND ABBEY NATIONAL (July 10, 2001).

¹³⁰ OECD, COMPETITION AND FINANCIAL MARKETS 32 (2009), available at <http://www.oecd.org/regreform/sectors/43046091.pdf>.

¹³¹ The assessment of the failing firm defense in merger cases should take into account the effect of the policy on the incentives for entry (and ex ante investment decisions in general). ROBIN MASON & HELEN WEEDS, THE FAILING FIRM DEFENSE: MERGER POLICY AND ENTRY 33 (2003), available at repec.org/res2003/Mason.pdf.

merely a reflection of creative accounting, as regards issues like transfer payments and the allocation of common costs. It is emphasized that no clear change in the UK authorities' approach to the failing firm defense has been identified in merger enforcement during the recent financial crisis.

D. The UK approach to Failing Firm Defense

As the above analysis has illustrated, the application of the failing firm defense in the UK is highly controversial. The role of antitrust legislation in taking into consideration the phenomenon and consequences of failing firms in assessing transactions involving such firms is important in safeguarding and advancing the aims of competition law. The approach of the UK competition authorities towards the failing firm defense has not changed during the recent financial crisis, even in cases where the target company had been severely affected by the crisis.

After showing in detail the UK perspective and enforcement in relation to the failing firm defense, this article turns briefly to the U.S. approach.

VI. UNITED STATES OF AMERICA

The assessment of whether a planned merger would significantly increase concentration in the market and whether the merger, in light of concentration, raises concern about potential harmful competitive effects, is based on the substantial lessening of competition test (SLC test). The 1992 *Horizontal Merger Guidelines* (U.S. Guidelines)¹³² reflect the analytical framework of analysis of horizontal mergers under U.S. merger law. Section 7 of the 1914 Clayton Antitrust Act (the Clayton Act)¹³³ (15 U.S.C. § 18) prohibits mergers and acquisitions that may substantially lessen competition or tend to create a monopoly.¹³⁴ The government gains its authority to review mergers and acquisitions before the parties are allowed to consummate the transaction under section 7A of the Clayton Act (15 U.S.C. § 18a), or the Hart-Scott-Rodino Antitrust Improvements Act of 1976 (HSR).¹³⁵ Although section 7 of the Clayton Act refers to mergers

¹³² DEP'T OF JUSTICE & FTC, HORIZONTAL MERGER GUIDELINES (2010), available at <http://www.ftc.gov/sites/default/files/attachments/merger-review/100819hmg.pdf>.

¹³³ The Clayton Antitrust Act, 15 U.S.C. §§ 12–27 (2012), is comprised of Sections 12–27 of Title 15 of the U.S.C. Some sections have been edited or eliminated because of space concerns.

¹³⁴ *Id.*

¹³⁵ *Id.* § 18a; see also Robert W. Doyle, Jr., *Hart-Scott-Rodino Antitrust Improvements Act Pre-merger Notification*, FINDLAW, http://profs.lp.findlaw.com/mergers/mergers_2.html (last visited Dec. 8, 2014).

that may “lessen” competition, mergers that worsen the competitive situation of markets that already exhibit weak competition and mergers that, while preserving the status quo, forestall future competition, will also be prohibited.¹³⁶ Under the wording of section 7, it is not necessary to prove that the competition has been restrained. It is enough that it “may” tend to substantially lessen competition.¹³⁷ “A transaction could also be challenged on the basis that it is an agreement in restraint of trade (section 1 of the 1890 Sherman Antitrust Act¹³⁸) or alternatively that it is an ‘unfair method of competition’ (section 5 of the Federal Trade Act).”¹³⁹

“[The U.S. Congress] recognized a failing firm exemption in the legislative history to the 1950 amendments to Section 7 [of the Clayton Act]...Some have suggested that Congress intended to exempt failing firms from section 7 [of the Clayton Act] merger analysis in order to protect private interests, such as shareholders and employees, when firms are failing”,¹⁴⁰ while others argue that “while Congress was perhaps concerned about private interests in the failing firm situation, it did not intend to override” the primary concern of antitrust which is competition.¹⁴¹

The U.S. Guidelines contain a specific section on the issues of failing firm defense and failing division defense. The antitrust authorities assess whether either party to the transaction would be likely to fail, causing its assets to exit the market if the merger is blocked.¹⁴² The theory is that:

“[a] merger is not likely to create or enhance market power or to facilitate its exercise, if imminent failure . . . 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

¹³⁶ OECD, SUBSTANTIVE CRITERIA USED FOR THE ASSESSMENT OF MERGERS 295 (2003), available at <http://www.oecd.org/dataoecd/54/3/2500227.pdf>.

¹³⁷ *Id.*

¹³⁸ 15 U.S.C. § 1.-7.

¹³⁹ KOKKORIS & OLIVARES-CAMINAL, THE EUROPEAN AND US MERGER CONTROL RULES: ISSUES FOR PRIVATE EQUITY INVESTORS 58–59 (2006).

¹⁴⁰ 1 FED. TRADE COMM’N, COMPETITION POLICY IN THE NEW HIGH-TECH, GLOBAL MARKETPLACE 4 (1996), available at http://www.ftc.gov/system/files/documents/reports/anticipating-21st-century-competition-policy-new-high-tech-global-marketplace/gc_v1.pdf.

¹⁴¹ *Id.*

¹⁴² KOKKORIS & OLIVARES-CAMINAL, *supra* note 139.

performance had the merger been blocked and the assets left the market.”¹⁴³

A merger is not likely to create or enhance market power or facilitate its exercise if the following circumstances are met¹⁴⁴:

(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.¹⁴⁵

These criteria are less stringent than the equivalent criteria under EU legislation (EUMR), since they do not require that the target company’s market share must be obtained by the acquirer if the failing firm exits the market.

A similar argument to the one made for the failing firm defense can be made for the failing division defense. The antitrust authorities will allow the acquisition of a failing corporate division if:

(1) the division has a negative cash flow on an operating basis; there is evidence that, absent the acquisition, the assets of the division would exit the market in the near future; and

(2) 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 and have complied with the competitively preferable purchaser requirements of section 5.1 of the U.S. Guidelines.¹⁴⁶

Although the U.S. Guidelines “do not recognize a distressed industry defense, they do suggest that distressed industry conditions may be considered when assessing the degree to which a merger would create or enhance market power.”¹⁴⁷

¹⁴³ HORIZONTAL MERGER GUIDELINES, *supra* note 132, at 33.

¹⁴⁴ *Id.*

¹⁴⁵ *Id.*

¹⁴⁶ *Id.* at 34.

¹⁴⁷ BERNARD A. NIGRO, JR. & JONATHAN S. KANTER, THE EFFECT OF MARKET CONDITIONS ON MERGER REVIEW—DISTRESSED INDUSTRIES, FAILING FIRMS, AND MERGERS WITH BANKRUPT COMPANIES 3, available at <http://apps.americanbar.org/antitrust/at-committees/at->

It is worth noting that bankrupt entities are subject to the standard pre-merger notification thresholds under the HSR Act.¹⁴⁸ However, “Section 363(b) of the Bankruptcy Act provides for special treatment when the target company is in bankruptcy.”¹⁴⁹ The Bankruptcy Act alters the HSR Act filing requirements in regards to who and when to file the notification form, as well as the waiting periods before the closure of the transaction.¹⁵⁰

One exemption for the violation of section 7 of Clayton Act is thus the failing firm defense. A merger is not deemed to substantially lessen competition if one of the merging firms is failing and absent the merger the assets would exit the market.¹⁵¹ The rejection of the proposed merger when the target is failing might lead to the liquidation of the productive assets.¹⁵² The failing firm defense was created by the case law rather than by statute. The U.S. Supreme Court first recognized this defense in 1930 in the leading case *International Shoe Co. v. FTC*.¹⁵³ The Supreme Court allowed the merger of two firms, one of which was facing grave financial difficulties. This judgment laid down the cornerstone for the failing company defense. The Court aimed at a broad analysis of the competitive and the anti-competitive effect of the acquisition of the company on the edge of the bankruptcy.

The legislative history of the Clayton Act by the Celler-Kefauver Act of 1950 eliminated any doubts concerning the validity of the failing firm defense.¹⁵⁴ The *International Shoe* case was the base for the abovementioned amendment. The U.S. Supreme Court subsequently reaffirmed the validity of the defense in case law.¹⁵⁵

A failing company claim presents a large number of variables for consideration, as well as uncertainty about the allegedly failing firm’s future viability. For example, the possibility of failure may be likely but not imminent; reorganization cannot be ruled out and thus the eventual viability of the company may be very uncertain. Fur-

telecom/pdf/distressedindustry.pdf (last visited Dec. 13, 2014); see also U.S. Guidelines, *supra* note 132, at 17 (describing the recent or ongoing).

¹⁴⁸ *Id.* at 11; see also Douglas Broder, Brian McCalmon & Kenneth Knox, *US Mergers: HSR threshold—Annual Adjustment*, 34(4) EUR. COMPETITION L. REV., n.67-n.68 (2013).

¹⁴⁹ NIGRO & KANTER, *supra* note 147, at 11.

¹⁵⁰ *Id.*

¹⁵¹ *Id.*

¹⁵² Kokkoris, *supra* note 18.

¹⁵³ *Int'l Shoe Co. v. FTC*, 280 U.S. 291, 302-03 (1930).

¹⁵⁴ Kokkoris, *supra* note 18.

¹⁵⁵ *Id.* See also *Citizen Publ'g Co. v. United States*, 394 U.S. 131, 138-39 (1969); Agnieszka Zwirska, *Failing Firm Defense* (Spring 2003) (Master thesis, Lund University), available at <http://lup.lub.lu.se/luur/download?func=downloadFile&recordId=1554682&fileId=1563408>.

thermore, there may be an alternative purchaser but the price to be offered may be so low that it is arguably unfair or inconsistent with the goal of preserving competition.¹⁵⁶

The *General Dynamics* case¹⁵⁷ provided the definition of the “failing,” “quasi-failing,” or “weak competitor” defense, which was first applied by the lower courts in *United States v. International Harvester Co.*¹⁵⁸ The Court held that the acquisition did not violate section 7 of the Clayton Act because the acquired company did not have sufficient financial resources to compete effectively.¹⁵⁹ The claim that the firm to be acquired is a weak competitor was made in order to show that the merger is less troubling than the combined market shares.¹⁶⁰ A “weak competitor claim” can be made in the circumstances that are difficult to evaluate. In the case of *United States v. International Harvester Co.*, the acquired company’s weak competitor claim arose from its difficulty in borrowing the capital.¹⁶¹ The court allowed the acquisition because the acquired company lacked financial resources necessary to operate competitively.¹⁶² Nevertheless, a weak competitor claim does not circumvent the requirement of the alternative purchaser. In *FTC v. Warner Communications Inc.*¹⁶³ the court noted that a weak company defense would expand the strict limits of the failing company doctrine.¹⁶⁴

“The spirit of the *General Dynamics* decision has been incorporated into the [U.S.] Guidelines”¹⁶⁵ by language acknowledging that “recent or ongoing changes in the market may indicate that the current market share of a particular firm either understates or overstates the firm’s competitive significance”¹⁶⁶ and committing to take into consideration “reasonably predictable effects of recent or ongoing

¹⁵⁶ Edward O. Correia, *Re-Examining The Failing Company Defense*, 64 ANTITRUST L.J. 683, 698 (1996), available at <http://www.jstor.org/stable/40843345?seq=3>.

¹⁵⁷ *United States v. Gen. Dynamics Corp.*, 415 U.S. 486, 506 (1974).

¹⁵⁸ *United States v. Int’l Harvester Co.*, 564 F.2d 769, 773–74 (7th Cir. 1977). See also Mason, *supra* note 128, at 2; see also OECD, FAILING FIRM DEFENSE 23, Gen. Distribution OCDE/GD(96)23 (1996), available at <http://www.oecd.org/competition/mergers/1920253.pdf>.

¹⁵⁹ *Id.* art. 22.

¹⁶⁰ Kokkoris, *supra* note 18.

¹⁶¹ *Id.*

¹⁶² *Id.*

¹⁶³ *FTC v. Warner Comm’n Inc.*, 742 F.2d 1156, 1164 (9th Cir. 1984) (per curiam); see also Correia, *supra* note 152, at 688.

¹⁶⁴ *Warner*, *supra* note 163.

¹⁶⁵ Nigro B., Kanter J., *The Effect of Market Conditions on Merger Review -- Distressed Industries, Failing Firms, and Mergers with Bankrupt Companies*, <http://apps.americanbar.org/antitrust/at-committees/at-telecom/pdf/distressedindustry.pdf>.

¹⁶⁶ *Id.* at 10.

changes in market conditions in interpreting market concentration and market share data.”¹⁶⁷

In *General Dynamics*, although the U.S. Supreme Court rejected a distressed industry defense, it emphasized the importance of considering all relevant facts, especially in cases where the relevant market or industry exhibits fluctuations, as well as dynamic features.¹⁶⁸ Antitrust authorities could also consider industry conditions as an argument in favor of approving a transaction. In spite of that, antitrust authorities take into account the impact of economic conditions on the ability of firms to raise capital and make investments, which are needed to be more effective competitors.¹⁶⁹

The presence of distressed industry conditions could also affect the speed of the investigation as a prolonged merger review, which may harm the firm to be acquired, and could weaken it to a point that the merger no longer makes sense to the purchaser.¹⁷⁰ The U.S. Supreme Court rejected the failing industry defense in *United States v. Socony-Vacuum Oil Co.*¹⁷¹ However, the U.S. Department of Justice (the DOJ) in *United States v. LTV Corp.*, considered the weakened state of the companies and the efficiencies that would result from the transaction.¹⁷²

The failing firm defense has mostly been rejected in the contested proceedings in which it was raised. However, the failing firm defense was held to justify the merger in *United States v. Maryland & Virginia Milk Producers Ass’n*.¹⁷³ In this case an agricultural cooperative association acquired the capital stock of Embassy Dairy, the largest milk dealer in the area, which competed with the association’s dealers.¹⁷⁴ Finally, the failing firm defense justified allowing the merger in *Union Leader Corp. v. Newspapers of New England*.¹⁷⁵

VII. CHINA

Since the AML came into force in 2008, MOFCOM has reviewed over 750 merger cases. It is noteworthy that there have been a number of merger cases that show the “mis-use” of antitrust law. In 2013,

¹⁶⁷ NIGRO, *supra* note 147, at 10.

¹⁶⁸ Gen. Dynamics Corp., *supra* note 9, at 504–06.

¹⁶⁹ Kokkoris, *supra* note 18.

¹⁷⁰ NIGRO, *supra* note 147.

¹⁷¹ *United States v. Socony-Vacuum Oil Co.*, 310 U.S. 150 (1940). See also Valentine, *supra* note 7.

¹⁷² *United States v. LTV Corp.*, 1984-2 Trade Cases 66, 235, *aff’d*, 746 F.2d 51 (D.C. Cir. 1984).

¹⁷³ *United States v. Md. & Va. Milk Producers Ass’n*, 167 F. Supp. 799, 808 (D.D.C. 1958), *aff’d*, 362 U.S. 458 (1960).

¹⁷⁴ *Id.*

¹⁷⁵ *Union Leader Corp. v. Newspapers of New England*, 284 F.2d 582, 588-89 (1st Cir. 1960).

the MOFCOM published four conditional clearance decisions: *Glencore/Xstrata*, *Marubeni/Gavilon*, *Baxter/Gambro* and *Mediatek/MStar*. Each decision turns on its own facts but recurring themes have been identified, namely:¹⁷⁶

(1) MOFCOM has shown itself prepared to find market power notwithstanding relatively low market share levels;

(2) there has been a continued attraction for the imposition of elaborate and onerous hold-separate arrangements as a condition for clearance;

(3) as a precondition to clearance, MOFCOM has sought commitments to supply key products to the Chinese market on favorable terms;

(4) MOFCOM has not shied away from imposing extraterritorial remedies even where the competition economics basis for seeking the commitment might not be that clear-cut; and

(5) coordinated effects theories of harm have arisen with some regularity in the published decisions.

All the above enforcement features do not exist in EU and US case law and create worrying concerns amongst the international legal, economic as well as business community on how international M&A deals will be assessed by MOFCOM.¹⁷⁷ Large international mergers (e.g. Samsung/Seagate, Hitachi/WD) were cleared with remedies across the major international jurisdictions. MOFCOM imposed some behavioral remedies, including a two-year hold separate agreement in one case (and 18 months in the other), which implied a de facto prohibition of the deal for two years, at which point parties need to ask MOFCOM for a removal of these barriers. This type of remedy resulted in a USD 400 million annual operation cost to the parties.

¹⁷⁶ Hannah C. L. Ha & John M. Hickin & Philip F. Monaghan, *China: Merger Control*, ASIA-PAC. ANTITRUST REV. §1 (2014), available at <http://globalcompetitionreview.com/reviews/60/sections/206/chapters/2337/china-merger-control>. This note also adds that although neither Glencore nor Xstrata own or operate productive assets in the relevant markets in China, MOFCOM took great interest in the transaction, focusing on the importance of China as a major market for the parties and China's reliance on imports of raw materials of central importance to the wider Chinese economy.

¹⁷⁷ George S. Cary & Elaine Ewing, *Divergence Then and Now: What Does the U.S./EU Experience Tell Us About Convergence With MOFCOM*, in 2 WILLIAM E. KOVACIC: AN ANTITRUST TRIBUTE LIBER AMICORUM 20 (N. Charbit, E. Ramundo, A. Chehtova & A. Slater, eds. 2013). In June 2014, MOFCOM blocked the proposed P3 Network shipping alliance between Denmark's AP Møller-Maersk A/S, Switzerland's Mediterranean Shipping Company and France's CMA CGM. This is MOFCOM's second prohibition decision, and the first time that MOFCOM has blocked a global foreign-to-foreign deal. This case is a clear divergence from the EU and US competition enforcement. (http://www.freshfields.com/en/knowledge/MOFCOM_blocks_the_proposed_P3_Network_shipping_alliance/?LangId=2057).

The AML enables MOFCOM to take account of both competition and non-competition factors in its analyses.¹⁷⁸ As such, close attention is paid to the impact of a transaction on national economic development, industrial policy and, generally, the Chinese social and economic fabric even in cases with a global dimension. We should add that the IT sector is particularly sensitive in China, which is home to the world's largest consumers of PCs and the manufacturing facilities of the world's major computer manufacturers. The technology sector is also regarded as a key sector for national security purposes in China.¹⁷⁹

Although China's AML was adopted in 2007, it is largely compatible with the European competition policy framework. Interestingly, however, MOFCOM has blocked two mergers and required commitments in 20 others, all involving foreign companies. The rate of merger activity in China is comparable to that in Europe, but the majority (about 60%) of the mergers was cleared with conditions by the European Commission involve only European companies.¹⁸⁰

Over the last 5 years, the majority of concentrations notified to MOFCOM were cleared without modification conditions, as showed in the following table.

Year	Cleared	Conditional	Prohibited
2008	15	1	
2009	68	4	1
2010	112	1	
2011	164	4	
2012	148	6	
2013	211	4	
2014	42(Q1)	3(to date)	1(to date)

¹⁷⁸ Li Kevin X., Che Pizhao & Du Ming, *Antitrust Control of Mergers and Acquisitions: A Case Study of China*, BUS. L.J. 597-616 (Sept. 2005).

¹⁷⁹ Yo Sop Choi & Sang Youn Youn, *The Enforcement of Merger Control in China: A Critical Analysis of Current Decisions by MOFCOM*, 44(8) IIC 948, 948-972 (2013), available at http://download.springer.com/static/pdf/663/art%253A10.1007%252Fs40319-013-0128-0.pdf?auth66=1416820583_64b4913e7bb8a62cfb3e81b1802c77ab&ext=.pdf.

¹⁸⁰ Mario Mariniello, *China's catching up on competition policy enforcement*, BRUELGEL (Oct. 20, 2014), <http://www.bruegel.org/nc/blog/detail/article/1183-chinas-catching-up-on-competition-policy-enforcement>.

Although these decisions issued by MOFCOM contained limited analysis, the outcomes were primarily consistent with the other major jurisdictions' decisions.

There are 23 conditional approval cases covering a variety of industries, ranging from manufacturing, energy, information and mining. Among them, there were 3 conglomerate mergers, 5 pure vertical mergers, 14 horizontal mergers and one merger with both horizontal and vertical issues. In 9 mergers there were structural divestiture imposed, either solely or combined with behavioral commitments.

On the basis of the case law analysis, there are three conclusions that can be drawn regarding the potential outcome of a case. The first is that if merging parties, either solely or combined, have market shares higher than 50%, it is very likely that MOFCOM will find competitive harm, on the basis of a unilateral theory of harm. In addition to that, provided the merged group is operating in a sector that is critical for domestic consumers MOFCOM is likely to impose behavioural remedies, such as supplying quantity guarantees or price-caps, to protect the Chinese market.

The last conclusion relates to the high-tech industry. Chinese economy is at a competitive disadvantage in technology-oriented sectors. The background reasons are complicated. Lacking of sufficient Intellectual Property rights to develop the competitive IT industry may be one of the substantial weaknesses for the future growth of Chinese economy. These years' decisions on Sanyo, Seagate, WD, Google, and Microsoft have raised concerns that the Chinese merger authority has been using the competition policy as a tool to facilitate its industry development. Thus, in concentrations in industries with heavy R&D, there may be more behavioral commitment imposed by the MOFCOM.

In relation to the failing firm defense concept, although it has not been included in the AML, Article 12 of the AML refers to a number of other factors such as economic efficiency and the possibility of the firm to be in financial difficulties (i.e. failing firm defense or flailing firm defense) as well as countervailing buyer power that can affect the merger assessment.¹⁸¹ In addition, Article 27 (6) of the AML explicitly gives the Chinese authorities the possibility of considering "other elements that may have an effect on market competition". It

¹⁸¹ MOFCOM's *New Interim Provisions on the Assessment of Anti-Competitive Effects of Mergers*, LINKLATERS.COM, <http://www.linklaters.com/Insights/AsiaNews/LinkstoChina/Pages/MOFCOMs-new-interim-provisions-on-assessment-of-anti-competitive-effects-of-mergers.aspx#sthash.WxLs5wAX.U5SMdgvF.dpuf> (last updated Sept. 20, 2011).

has been argued¹⁸² that if the same conditions as in the EU are applied, the concentration is not having the effect of eliminating or restricting competition in the sense of Article 28 AML and therefore should not be forbidden; and also, because, applying the second sentence of Article 28 AML, the concentration scenario might be better (positive impact) than the non-clearance scenario.

Recently, the decisions have been increasing in length and analysis, which showed an improved level of transparency. However, even taking these merits into account, such trivial progress can hardly cover the substantial weakness in MOFCOM's analytical framework, and some remedies imposed by it are difficult to be explained from a competition analysis perspective.

The non-technical analysis that MOFCOM has in its decisions makes them somewhat unconvincing. In the relatively recent decisions, MOFCOM normally takes into account the specific market concentration data, the market shares of the merging parties and of the competitors. In light of other competitive factors, it is not uncommon for MOFCOM to list the factors it has considered and then without providing further information regarding to the investigation to jump to the conclusion.

China, with its lack of explicit failing firm defense, does not have the ability to be pragmatic towards mergers that do not harm competitors and consumers. Mergers that can sustain the level of service and maintain the supply to customers and benefits customers without having any adverse impact on competition should have the opportunity to be cleared by MOFCOM. It should be emphasized that on the basis of the practice of international jurisdictions, if any adverse impact in the market results from the failure of the target, then a merger/acquisition of this target will not itself induce any harm and the merger/acquisition should be cleared provided it satisfies the failing firm defense.

One would hope that MOFCOM decides to incorporate the failing firm defense concept in its attempt to enhance its harmonization with the US and EU jurisdictions.

IX. SOME CONSIDERATIONS ON THE APPLICATION OF THE FAILING FIRM DEFENSE

The lack of an alternative purchaser must be established by good faith efforts to find another purchaser. The failing firm is required to

¹⁸² JERÓNIMO MAILLO, UNDERSTANDING CHINA'S COMPETITION LAW & POLICY: MERGER CONTROL AS A CASE STUDY (2011), available at <http://www.idee.ceu.es/Portals/0/Publicaciones/Understanding-Chinas-Competition-Law-&-Policy.pdf>.

have made a good faith effort to obtain *bona fide* offers from other firms that would keep the failing firm in the market while making a less serious threat to competition. However, the alternative purchaser may have much less to offer in the way of improving the efficiency of the acquired firm than the prospective competitor-purchaser. In addition, there is concern that the competitor's offer is higher because it includes a market power premium, a payment for anticipated gains in market power. There could be a market power premium, or an efficiency premium or both. The problem is that it is difficult to separate them. Overestimating the market power premium means underestimating the efficiency premium. The willingness of the acquirer to buy a company that is headed toward failure justifies giving its efficiency claims some additional credence.¹⁸³

From the above analysis we can draw a tentative conclusion that lack of alternative means of reorganization is a vital criterion for the success of the failing firm defense. However, there is substantial uncertainty surrounding the reorganization scenario. Reorganization and restructuring of companies can take multiple forms (e.g. scheme of arrangement, company voluntary scheme, etc.) and their success generally depends on creditors' and shareholders' approvals. Thus, a central problem in applying the reorganization criterion is that it may be impossible to make reliable predictions at the time of assessing the merger as regards the likelihood that alternative restructuring methods will be successful.

In the assessment of a merger in a failing industry, the competition authorities should also pay attention to the potential dynamic or innovative efficiencies. Dynamic or innovative efficiencies may make a particularly powerful contribution to competitive dynamics, R&D ('Research and Development'), and welfare but the problem is that they are not readily verifiable and quantifiable because they tend to focus on future products. Merger analysis should give efficiencies more weight if the profitability of a failing industry can be improved by the merger (e.g. by lowering fixed costs) even if the price effects are not immediate. Thus, there is a trade off between the viability of the failing firm and the positive impact that it may have on competition due to the existence of one additional competitor in the market and the further consolidation in the market (if a competitor merges with / acquires the failing firm) due to the merger, which may also result from the exit of the failing firm from the market.

¹⁸³ FTC, *supra* note 123. Statement of Edward Correia, Professor of Nw. Univ. on the Failing Company Defense. The Supreme Court interpretation of the alternative buyer condition was presented in the case of *Citizen Publishing Co. v. United States*.

The failing firm defense may be closely intertwined with other considerations such as social, public policy as well as employment issues. Competition authorities in assessing mergers involving failing firms should take into account such issues as they are likely to affect the outcome of the merger assessment. As regards economic and social benefits, there is an inherent difficulty in determining the extent of social costs/benefits in a failing firm context and how to account for them. The burden is borne in the form of higher prices and lost consumer surplus, while the relevant benefits concern the failing company's workers and shareholders and the community in which the failing company's assets are located. According to Correia (1995), competition authorities should also take social costs into account in adopting some general formulation of the failing company defense, rather than taking social costs into account in individual cases.¹⁸⁴ Such concerns may lead to a different interpretation of consumer welfare, thus entitling competition authorities to take social, public policy as well as employment issues into consideration in defining their consumer welfare objective of merger assessment.

Furthermore, the policy towards mergers may have an impact on the employees of the merging firms. Allowing mergers can result in job losses, as may also be the case in prohibiting mergers. If a merger is not allowed and the failing firm exits the market, the lost jobs originate from plant closure. If an anticompetitive merger is allowed, jobs may be lost when the industry raises prices and reduces output. When the failing firm disappears from the market, the employment resources of this firm are likely to be devoted to the manufacture of a completely different product or provide totally different services, perhaps not as efficiently. However, the likelihood of job losses, inefficient use of labor force and the political / social ramifications that such issues may have should not determine the assessment of mergers under antitrust law. Issues relating to employment safety should be dealt with by employment policy and should not influence competition policy.

In addition to economic and social concerns, the relevant public policy considerations are related to the protection of private parties whose future depends on the existence of the failing firm as well as the welfare of the locality of the failing firm. The shareholders are unlikely to lose the investment and are likely to reap benefits in case the merger is profitable. The creditors will benefit as a result of retaining their rights against the debtor and are likely to be reimbursed for the credit they have provided to the firm.

¹⁸⁴ *Id.*

According to Posner¹⁸⁵ (1981), the failing firm defense is “one of the clearest examples in antitrust law of a desire to subordinate competition to other values”.¹⁸⁶ The social policy consideration regarding the merger works alongside the impact of the merger on competition. However, such policy considerations should never constitute the basis for merger assessment. Merger laws are very powerful tools to address a small number of issues and non-competition related policy considerations should never have a role to play.

Competition authorities (e.g. US, EU, UK) are unwilling to extend the failing firm defense/exception to firms which have not yet failed but are less efficient competitors. If a flailing firm defense/exception exists, parties to competition reducing (and thus likely profitable) mergers would have a strong tendency to claim that they are flailing even if their situation is not as severe as the one of a failing firm in order to invoke the defense and be treated more leniently than they should. In addition as the OECD report states, even if flailing firms could be reliably identified, competition authorities may take the view that the competition such firms provide, albeit weak, benefits consumers and should be allowed to continue as long as possible. A merger involving a flailing firm might foster a considerably better competitive environment than a similar merger involving a failing firm.¹⁸⁷ Similar arguments can be put forward for the unwillingness of competition authorities to accept declining industry arguments. However, what should be taken into consideration is that in declining industry situations, it is more likely that firms, which may be currently failing, may continue to be in an adverse situation and may not be viable at all in the near future.

An additional criterion for the acceptance of the failing firm defense is that there must be no other prospective purchaser.¹⁸⁸ Furthermore, this buyer must make a reasonable offer. A reasonable offer is defined as “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 offer.”¹⁸⁹ Thus, the alternative buyer only needs to offer

¹⁸⁵ Richard Posner was an assistant to the Federal Trade Commission, assistant to the solicitor general of the United States, in 1981 appointed as a judge of the U.S. Court of Appeals for the Seventh Circuit. He was the chief judge of the court from 1993 to 2000.

¹⁸⁶ Richard A. Posner, *Antitrust: Cases, Economic Notes and Other Materials* 472 (2nd ed. 1981).

¹⁸⁷ OECD, *FAILING FIRM DEFENSE* 21 (1996), *available at* <http://www.oecd.org/competition/mergers/1920253.pdf>.

¹⁸⁸ *Id.*

¹⁸⁹ OECD, *supra* note 136, at 33 n.39.

more than the liquidation value and be able to keep the assets operating in the markets, even though the alternative purchaser may have less to offer in the way of improving the efficiency of the failing firm than the prospective competitor purchaser. The competition authorities should consider whether the alternative purchaser has the capability to run the failing firm as a competitive, on-going business, including infusions of capital that will ensure the viability of the failing firm.¹⁹⁰ Furthermore, a non-market participant may simply seek a revenue stream rather than seek to operate as an effective competitor by making long-term investment plans.¹⁹¹ Many firms that purchase a distressed business may intend to ensure a revenue stream rather than to compete vigorously.

Current U.S. and EU policy towards failing firm defense may prefer systematically alternative purchasers that are unlikely to offer the same efficiencies that a competitor purchaser may offer. In addition, the defense may induce companies to be in a severe state of decline before they qualify for the defense. In the *Holland & Barrett/Julian Graves* merger, the OFT concluded that the merger would result in a substantial lessening of competition, as the OFT found evidence of other viable purchasers and rejected the failing firm defense arguments.¹⁹²

Thus, the requirement to make a good-faith effort to find an alternative purchaser safeguards against a loss in competition. However, as mentioned above, the merger with a non-incumbent firm who is likely to be a less anticompetitive alternative purchaser will not bring about any synergies. In addition, there is a concern that the incumbent's price offer is likely to be higher than the one of a non-incumbent. However, it cannot be determined whether this higher price is due to the resulting efficiencies which should be an argument in favor of the merger, or due to the expected increased market power of the incumbent which constitutes an argument against the acceptance of the failing firm defense. "[T]he willingness of the acquirer to buy a company that is headed toward failure justifies giving its efficiency claims some additional credence."¹⁹³ The U.S. Supreme Court interpretation of the alternative buyer condition was presented in the case of *Citizen Publishing Co. v. United States*.

Failing company claims indicate a trade-off between two scenarios that need to be considered, the company exiting the market and an

¹⁹⁰ Efficiencies, Failing Firms and the General Dynamics Defense: Hearing before the FTC (1995) (Testimony of Janet L. McDavid, Hogan & Hartson L.L.P.).

¹⁹¹ Valentine, *supra* note 7.

¹⁹² See *Holland & Barrett/Julian Graves Merger*, *supra* note 109.

¹⁹³ Correia, *supra* note 160, at 695.

anticompetitive concentration. The first scenario is of great importance if the costs of the concentration are balanced against the costs of blocking this concentration, where there is a probability that the failing firm will survive and remain competitive. If blocking the concentration implies that the failing firm's assets will exit the market and therefore the output of this firm will be lost, the allowance of the concentration seems to be the only sensible solution. The loss to stockholders, and the community where the business operates, would be less severe if the concentration was allowed rather than if the firm exited the market.

From an economic perspective, the capacity is a good predictor of likely output, and lost output is a good measure of the competitive harm. In the case of a concentration, it is very unlikely that the output will be reduced through the interdependence. More "output is reduced if the acquired firm's assets exit the market"; thus, the concentration is the preferred option.¹⁹⁴ However, it should be noted that the current market share of the failing firm may overstate its future competitive significance, as well as the anticompetitive effects of a concentration. What would be of importance is whether the concentrated entity can unilaterally or collectively affect prices and/or output.

The failing firm defense might also be applied when only a part of the company is failing. Refusal of such defense would force the parent company either to end a subsidiary or to keep it going at a loss. This requirement was widely discussed by the U.S. Supreme Court in the case of *International Shoe Co. v. FTC* and by the EU Commission in *Newscorp*.¹⁹⁵

Accepting the distressed industry arguments could help revitalize failing industries by lowering their overall costs and enabling them to compete more efficiently. In moderately concentrated industries exhibiting excess capacity, the ease of entry in combination with the increased threat of import competition would render any anticompetitive impact of the concentration unlikely. However, difficulty in the identification of a distressed industry and the distinction between

¹⁹⁴ A number of authors have estimated the loss in output from a firm exiting the market with the loss in output stemming from increased concentration. This literature points toward the conclusion that a certain loss in output by virtue of a firm's assets leaving the market will exceed the loss in output from a merger under any realistic set of assumptions. See John E. Kwoka, Jr. & Frederick R. Warren-Boulton, *Efficiencies, Failing Firms, and Alternatives to Merger: A Policy Synthesis*, 31 ANTITRUST BULL. 431, 445 (1986); Richard D. Friedman, *Untangling the Failing Company Doctrine*, 64 TEX. L. REV. 1375 (1986); Fred S. Mcchesney, *Defending the Failing-Firm Defense*, 65 NEB. L. REV. 1 (1986). See also Correia, *supra* note 160, at 688.

¹⁹⁵ Commission Decision 4064/89, Case No COMP/M. 2876 - Newscorp / Telepiù, 2004 O.J. (L 110) 73 (EC).

a distressed industry and an industry experiencing a downturn may constitute putting crucial weight on the consideration of the distressed industry circumstances unlikely. In the distressed industry defense, there is a consensus that concentrations are strong candidates to achieve efficiencies.¹⁹⁶ Thus, efficiencies that may not be credible in booming industries may be applicable when the distressed industry defense is invoked.

X. CONCLUDING REMARKS

Firms in financially distressed conditions may face the prospect of illiquidity and may embark on a restructuring process in order to ensure their viability and profitability. Restructuring is the term for the act of converting a debt into another debt that is repayable at a later time.¹⁹⁷ In this process of restructuring, the companies may be involved in a concentration transaction of some kind. In such cases, the implications of competition legislation on the restructuring process may be severe. There may be instances where the negotiations leading to a restructuring plan may have been completed successfully and the proposed solution blocked by the antitrust authorities. A safe harbour for such cases is the concept of failing firm defense or failing division defense.

Each jurisdiction has its own formulated criteria that need to be satisfied in order for the failing firm defense to be acceptable. In general, the criteria that need to be satisfied include, *inter alia*, 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. Thus, the firm must be bankrupt, on the verge of bankruptcy or in imminent danger of financial collapse. In addition, there must be 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. Once these conditions are fulfilled the merger would not be considered to cause the deterioration of the competitive structure that follows the merger.

In particular, the US, EU and UK have devised criteria against which the failing firm defense can be assessed. In US, *inter alia*, the firm would not be able to reorganize successfully under Chapter 11 of the USBC and absent the acquisition, the assets of the failing firm

¹⁹⁶ FTC, *supra* note 144, at 21.

¹⁹⁷ See *Restructure*, OXFORD DICTIONARIES, <http://www.oxforddictionaries.com/definition/english/restructure?searchDictCode=all> (last visited Dec. 14, 2014).

would exit the relevant market.¹⁹⁸ In EU, *inter alia*, 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.¹⁹⁹ Furthermore, in the absence of a merger the assets of the failing firm would inevitably exit the market. Thus, for the failing firm to apply, a merger/acquisition and/or sale should be the only viable method of corporate restructuring.²⁰⁰ Otherwise, the failing firm defense cannot be applicable. In the UK, the competition authorities have followed a similarly strict approach towards the failing firm defense and have accepted the defense only in a few numbers of cases, and after the parties have clearly illustrated the absence of causality between the merger and the adverse impact in the market.

Hence, to qualify for the failing firm defense, the concentrating undertakings must show that one of the undertakings is a failing firm and that therefore the concentration itself does not bring about any anticompetitive effects. The logic in the defense is that the deterioration in the competitive structure of the market would have occurred even in the absence of the concentration through the exit of the failing firm.²⁰¹

Considering the concentration with the failing firm, the economic aspects of allowing and blocking this concentration, such as the loss of jobs, benefit to consumers and price maintenance, should also be borne in mind. Social costs must be taken into account in adopting some general formulation of the failing company defense, rather than taking social costs into account in individual cases.²⁰² MOFCOM should incorporate this rationale in its analysis.

Deciding when and how to apply the defense is difficult in part because the facts underlying the failing company claim may be closely intertwined with other claims, which are analytically distinct. For example, it may seem that current policy benefits alternative purchasers that are unlikely to offer the same efficiencies that a competitor purchaser may offer. In addition, the failing firm defense can be assumed to constitute an efficiency claim, since the concentrating company argues that it can ensure the viability and profitability of the failing company. As Correia argues, a failing company claim may also occur in the context of a declining industry where capacity

¹⁹⁸ Kokkoris, *supra* note 18, at 158-166.

¹⁹⁹ Kokkoris, *supra* note 101.

²⁰⁰ Ioannis Kokkoris., *Failing Firm Defense: A Success or Failure for Corporate Restructuring?* 4 INT'L CORP. RESCUE 149-156 (2007).

²⁰¹ ANGUS MACCULLOCH & BARRY RODGER, COMPETITION LAW AND POLICY IN THE EC AND UK 221 (3rd ed. 2004).

²⁰² Correia, *supra* note 156, at 699-700.

is certain to exit the market. If that is the case, a concentration may be justified both on efficiency grounds as well as on failing firm defense grounds, which must be analyzed separately.²⁰³

As an effective institution to offer incentive to the economic modernization and further growth, the “law” undertakes the responsibility of rewarding and protecting whoever assumes business risk, i.e. venture. Competition law, in particular, should be legislated and enforced solely toward the enhancement of consumer welfare by the protection of effective competition among competitors, to avoid the business entities perusing their profit targets at the sacrifice of customers. Admittedly, there are other factors, such as employees, overall industry strategy, national interests, and the like, in a wide society should be under the shed of the “law” against the overly selfish activity of enterprises. However, this protection should be exercised by other public policies, other than competition law. “The goal of competition policy is to contribute to overall welfare and economic growth by promoting market conditions in which the nature, quality, and price of goods and services are determined by competitive market forces.”²⁰⁴ “Competition is the commercial interaction between actual and potential suppliers and their customers,”²⁰⁵ effective competition itself would be sufficient to deliver the best reasonably available value to customers and consumers.

Moreover, the effective and successful enforcement of competition law in the US and the EU is highly reliant on the fact that “independent high courts have played a significant role in supporting litigation against government-based anticompetitive restraints”²⁰⁶. In contrast, MOFCOM, as one ministry below the Council, makes the enforcement of AML unlikely to be capable of exercising the power solely according to the economic and “free market” considerations. Thus, this may be a prerequisite deficiency for China’s antitrust enforcement.

From the perspective of substantive competitive analysis, MOFCOM has struggled to lead itself to the track of economic analysis, however, from several latest decisions, it still did not identify the competitive effects by considering all relevant aspects or it did

²⁰³ *Id.*

²⁰⁴ OECD, OECD GUIDELINES FOR MULTINATIONAL ENTERPRISES para. 97, at 58 (2011), available at <http://www.oecd.org/daf/inv/mne/48004323.pdf>.

²⁰⁵ ALISTAIR LINDSAY & ALISON BERRIDGE, THE EU MERGER REGULATION: SUBSTANTIVE ISSUES art. 2-013, at 47 (4th ed. 2012).

²⁰⁶ In the US, local protectionism is dealt by the Dormant Commerce Clause and the federal antitrust laws. The European Court of Justice (ECJ) deals with anticompetitive government restraints. See Mehra, *supra* note 1, at 5.

not take such evidence as necessary to constitute sound arguments of theory of harm.

There are significant concerns that MOFCOM's enforcement is driven by political influence or MOFCOM takes into account the industrial policy in merger control.²⁰⁷ However, reconsidering the anti-trust policy history in the US, the Chinese agency seems to repeat several mistakes made by the counterparty in the US. After all, "US antitrust policy has evolved from a system of regulation based on political, social, and ideological considerations to one premised on modern economic principles."²⁰⁸ Given the relatively short enforcement period and the accompanying limited experience and superficial understanding of competition policy by MOFCOM, it has the potential to enhance its merger enforcement in the future.

There have been several improvements, such as increasingly detailed analysis of the decisions, publication of the decisions in merger cases that got unconditional approval. MOFCOM should continue to enhance this approval. One main way for that would be the explicit introduction of failing firm defense as such clauses exist in a variety of major jurisdictions and has proved to be beneficial for the harmonization of international competition enforcement.

To conclude, if MOFCOM wants to establish a positive high-profile, it should always bear in mind that competition law and enforcement are focused on protection of competition and consumers.

²⁰⁷ Cary & Ewing, *supra* note 179, at 20.

²⁰⁸ Thomas R. Howell, Alan Wm. Wolff, Rachel Howe & Diane Oh, *China's New Anti-Monopoly Law: A Perspective from the United States*, 18 PAC. RIM L. & POL'Y J. 53, 54 (2009), available at <http://digital.law.washington.edu/dspace-law/bitstream/handle/1773.1/519/18PacRimLPolyJ53.pdf?sequence=1>.

