Time to Bid Farewell to the Failing Firm Defense? Some Thoughts in the Wake of Nynas/Shell and Olympic/Aegean

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Our last edition of the CPI Europe Column for 2013 is dedicated to the "failing firm defense." Kyriakos Fountoukakos and Lisa Geary (Herbert Smith Freehills) guide us through the recent developments in this area of EU merger control. The failing firm defense doctrine has been firmly in the spotlight in recent years, in view of the persistent difficult economic times in Europe with speculation that the Commission could increasingly accept failing firm defenses. This did not materialize until very recently when the Commission issued two consecutive clearance decisions (Nynas/Shell and Olympic/Aegean) in the short space of a few months. The Commission's statements in those cases and its overall decisional practice, however, suggest that there is no real relaxation in the Commission's approach and that the failing firm defense still applies rarely and narrowly and will only succeed in the presence of strong factual evidence. However, the authors argue that the approach in the two cases and the Commission's approach in past cases involving counterfactual analyses in situations similar to a failing firm scenario involving diminution of a business for reasons unrelated to the merger, show that the Commission can and will employ a broad counterfactual analysis of which a failing firm scenario is just one example. The authors argue that, in this light, the strictly applied failing firm test with its formalistic limitations may no longer serve a purpose and can indeed be seen as a concrete example of a wider counterfactual analysis. In this latter instance, the negative effects on competition and the causality link between them and the proposed merger will necessarily be considered and may well justify a clearance decision where the competitive conditions in the market absent the merger would not be more favorable. Strong evidence to prove the counterfactual will, however, always be essential. Companies should continue to be cautious before raising such issues before the Commission and should continue to expect that such failing firm style counterfactuals will continue to be accepted only exceptionally.

Introduction

Antitrust lawyers have been taken by surprise recently when the European Commission (the "**Commission**") accepted the so-called "failing firm defense" ("**FFD**") twice in short sequence to clear unconditionally transactions which will lead to monopoly or near-monopoly in the relevant markets.

In September 2013, the Commission cleared the proposed acquisition by Nynas of certain refinery assets of Shell Deutschland Oil GmbH[1] leaving the acquirer as the only EEA-based producer of the relevant products. In October 2013, the Commission applied the FFD in *Aegean/Olympic II*[2], after having previously rejected it and prohibited the deal.[3]

The Commission's approach to the FFD has been notoriously strict and the defense has been a real rarity. It has previously been invoked successfully only on a handful of occasions in more than two decades of EU merger control. So has the Commission gone soft in light of the current economic climate? And if so, why an article with the title "time to

[1] Case M.6360 *Nynas/Shell/Harburg Refinery*, Decision of 02 September 2013.
[2] Case M.6796 *Aegean/Olympic II*, Decision of 09 October 2013.
[3] The Commission had concluded in the prohibition decision that none of the three failing firm criteria were met.

bid farewell" to the FFD? Surely, the two consecutive successes of the FFD should make it more, not less, popular.

In this article we provide some background to the Commission's approach on the FFD and discuss briefly the recent cases (albeit acknowledging that there is a paucity of publicly available information – the decisions have not yet been published). We advocate that perhaps the time has come for the FFD to be put to rest as an independent and strictly delineated, exceptionally applied doctrine. The FFD is no more than one example of a counterfactual analysis. The Commission's recent approach does not in our view signify that the Commission has gone soft. Situations in which the FFD is satisfied are likely to remain the exception and hard evidence will need to be provided. However, more flexibility may be applied in looking at FFD-style scenarios in a more holistic way by focusing on the classic counterfactual question: what is likely to happen absent the merger and how does this compare with a scenario of allowing the merger? In other words, is it better to prohibit the deal and let the counterfactual materialize or clear the deal and perhaps preserve some efficiencies that the merger may bring about?

Background

The EU Merger Regulation ("**EUMR**") does not refer explicitly to a FFD at all. However, Article 2 of the EUMR makes clear that the Commission may only prohibit a transaction where it will result in a significant impediment to effective competition <u>and</u> there is a causal link between the transaction and that impact on competition. The Commission's assessment of the counterfactual provides it with a method of determining in each case whether such a causal link exists by comparing the competitive conditions that would result from the notified merger and those that would have existed without the merger.[4]

In most cases, the relevant counterfactual will be the competitive conditions prevailing at the time of the merger. Nevertheless, in certain circumstances the Commission may take into account reasonably predictable future changes to the market, such as the likely entry or exit of firms if the merger did not take place.[5] The FFD represents a particular application of this approach.

As noted by the Commission in its Horizontal Mergers Guidelines, "*[t]he Commission may decide that an otherwise problematic merger is nevertheless compatible with the common market if one of the merging parties is a failing firm. The basic requirement is that the deterioration of the competitive structure that follows the merger cannot be said to be caused by the merger. This will arise where the competitive structure of the market would deteriorate to at least the same extent in the absence of the merger*."[6] Therefore, in order for the FFD to be invoked successfully, a merger must be "*at least "neutral"*" as regards its

[4] Guidelines on the assessment of Horizontal Mergers, para 9.
[5] *Ibid.*
[6] Guidelines on the assessment of Horizontal Mergers, para 89.

effect on competitive conditions, compared to the scenario where the merger would not take place.[7]

The Commission considers that three cumulative criteria are "especially relevant"[8] for a FFD to be accepted: (i) the allegedly failing firm would in the near future be forced out of the market because of financial difficulties if not taken over by another undertaking; (ii) there is no less anti-competitive alternative purchaser than the notified concentration; and (iii) in the absence of a merger, the assets of the failing firm would inevitably exit the market.[9] The Commission has applied these criteria quite strictly in its previous practice with the conditions becoming a sort of dogma that must be met very clearly and precisely and with the burden of establishing the defense falling on the notifying parties.[10] As we show further below, the Commission has insisted, for example, that the firm's exit is due to "financial difficulties" (i.e. bankruptcy or near-bankruptcy style scenarios). It has been very suspicious of "failing division" defenses when the parent company is in a healthy financial state. It has applied the alternative purchaser condition extremely strictly requiring, for instance, proof of approaches to all possible purchasers and not just to one category of purchasers. It had also in earlier days applied the third criterion in a dogmatic manner by requiring that the counterfactual involve all the market share of the failing firm being accrued to the merging party rather than the assets simply disappearing (this has been relaxed in more recent years and we discuss this further below). Overall, the Commission itself acknowledges that it is "*generally difficult to establish that a firm is failing*"[11] in this sense.

However, the Commission's past approach has not always been entirely consistent. The Commission has cleared transactions that did not necessarily fall within the strictures of these specific criteria, where a counterfactual analysis disclosed that the merger scenario resulted in less harm to competition than other available alternatives.[12] It has also taken into account particular counterfactual scenarios in situations similar to a failing firm/division in cases involving, for example, closures of plants (rather than whole firms)[13] or exit of airline routes.[14] This emphasizes that the strict failing firm test represents one particular application of the general "causal link" test under Article 2 of the EUMR.

Three 'especially relevant' criteria to establish the failing firm defense

Allegedly failing firm would be forced out of the market in the near future

[7] OECD Competition Committee, Meeting of 21 October 2009, Roundtable on Failing Firm Defence, Note by the services of the European Commission, para 2.
[8] Guidelines on the assessment of Horizontal Mergers, para 90.
[9] *Ibid*.
[10] Guidelines on the assessment of Horizontal Mergers, para 91.
[11] OECD Competition Committee, Meeting of 21 October 2009, Roundtable on Failing Firm Defence, Note by the services of the European Commission, para 15.
[12] See, for example, Case COMP/M.2810 *Deloitte & Touche/Andersen (UK)*, Decision of 01 July 2002.
[13] See, for example, Case COMP/M.5283 *Sappi/M-Real*, Decision of 31 October 2008; Case COMP/M.5865 *Teva/Ratiopharm*, Decision of 03 August 2010.
[14] See, for example, Case COMP/M.5830 *Olympic/Aegean Airlines*, Decision of 26 January 2011. See further, Section B 1.2, Mergers chapter of the EU Competition Law Handbook 2014, Sweet & Maxwell, of which the authors are, respectively, editor and assistant editor.

Under this criterion, the notifying parties must demonstrate that the company would in any event exit the market as a result of financial difficulties. It is not necessary for the company to have entered into bankruptcy or similar proceedings in order for the test to be met, but such proceedings must be *likely* in the near future, absent the merger.[15] By way of example, in *BASF/Eurodiol/Pantochim,*[16] the Commission concluded that a clear-cut danger of bankruptcy had been made out as the target Belgian chemical companies were subject to a pre-bankruptcy regime under Belgian law and had been placed under Court administration. The Commission assesses financial distress on the basis of profitability, liquidity and solvency metrics in a company's balance sheet. The assessment of, and timescale for, likely exit are conducted on a case-by-case basis, looking at the specific characteristics of each market.

The Commission applies this criterion particularly strictly where a failing division, rather than a failing firm, is under consideration as the Commission is concerned that parent companies may engineer the balance sheet of an individual division to meet the test. Otherwise, the Commission reasons, "*every merger involving an allegedly unprofitable division could be justified under merger control law by the declaration that, without the merger, the division would cease trading.*"[17] In the Commission's previous decisional practice, this limb of the test appears to only have been met where it could be shown that the continued operation of the failing division would imperil the survival of the parent company.[18]

No less anti-competitive alternative purchaser

This limb of the test requires the notifying parties to establish that no less anti-competitive alternative purchaser exists, in essence, a counterfactual assessment of what the market structure would look like in the case of alternative acquirers.[19] In order to meet this criterion, the notifying parties must demonstrate that they have made all efforts to give alternative available investors the opportunity to enter into negotiations regarding the acquisition of the failing firm.[20] Where the Commission does not consider that the parties have made such efforts, the defense will not be available. In *JCI/FIAMM*, the notifying parties had made significant efforts to obtain alternative purchasers, but had limited their search to larger competitors. The Commission proceeded to contact additional (smaller)

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[15] OECD Competition Committee, Meeting of 21 October 2009, Roundtable on Failing Firm Defence, Note by the services of the European Commission, para 4.

[16] Case COMP/M.2314 BASF/Eurodiol/Pantochim, Decision of 11 July 2001, para 144.

[17] OECD Competition Committee, Meeting of 21 October 2009, Roundtable on Failing Firm Defence, Note by the services of the European Commission, para 14; Case COMP/M.2876 *Newscorp /Telepiù*, Decision of 02 April 2003, para 212.

[18] See, for example, Case COMP/M.4381 *JCI/FIAMM*, Decision of 10 May 2007, in which the notifying parties demonstrated successfully this ground (paras 712-721) but failed to establish that the relevant assets would inevitably exit the market. See also Case COMP/M.2876 *Newscorp/Telepiù*, Decision of 02 April 2003, para 214; Case COMP/M.5830 *Olympic/Aegean Airlines*, Decision of 26 January 2011, paras 2013 and 2017-2018.

[19] OECD Competition Committee, Meeting of 21 October 2009, Roundtable on Failing Firm Defence, Note by the services of the European Commission, para 5.

[20] *Ibid,* para 6.

potential purchasers to verify the parties' findings in order to confirm that the test had been met on this ground (although it was ultimately rejected on other grounds).[21]

Inevitable exit of assets

In the first case in which the Commission accepted the FFD, *Kali+Salz/MdK/Treuhand,*[22] the Commission expressed this limb of the test as a requirement that the entire market share of the target company would accrue to the acquirer in the event of withdrawal by the target company from the market. In later cases, this test has been changed to a less restrictive formulation: will the assets of the failing firm inevitably exit from the market?[23]
The rationale behind this limb of the test is that the two previous conditions do not address the possibility of a take-over by third parties of the various production assets of the failing firm in the course of bankruptcy proceedings. If these assets were to remain on the market, the effects on competition could be similar to, or more beneficial than, the take-over of the entire failed business by an alternative purchaser. The Commission therefore considers how investors would allocate the individual assets and the relative impact on competition of any potential short-term supply disruptions compared to the transfer of the business as a going concern. The Commission acknowledges that this part of the test is generally difficult to fulfil and has been applied "*rather strictly.*"[24]

Overall counterfactual analysis

The difficulty in establishing all three of the above criteria means that a successful invocation of the FFD is quite rare. However, as noted above, the FFD merely represents or should represent a particular application of the Commission's counterfactual analysis. Therefore, even if the "strict" failing firm test is not made out, a counterfactual analysis may lead to the conclusion that a diminution of competition on the relevant market is not a causal effect of the merger. For example, exit of the business may be due to issues other than strict bankruptcy style scenarios but it may be proven on the basis of cogent evidence nonetheless.

In the *Andersen* cases,[25] the Commission did not refer at all to the FFD but applied a thorough counterfactual assessment to conclude that the proposed transactions did not result in an impediment to competition. These cases concerned the acquisition by other members of the then "Big Five" audit firms of assets of Arthur Andersen following its rapid disintegration in the aftermath of the Enron scandal. The Commission had previously found that the auditing and accounting market for large firms was susceptible to collective

[21] Case COMP/M.4381 *JCI/FIAMM*, Decision of 10 May 2007, para 734.
[22] Case IV/M.308 *Kali+Salz/MdK/Treuhand*, Decision of 14 December 1993.
[23] Case COMP/M.2314 *BASF/Eurodiol/Pantochim*, Decision of 11 July 2001, paras 149-151. See also, judgment of the Court of Justice on the appeal against the *Kali+Salz* decision, Joined Cases C-68/94 and C-30/95, *France and Others v Commission*, judgment of 31 March 1998.
[24] OECD Competition Committee, Meeting of 21 October 2009, Roundtable on Failing Firm Defence, Note by the services of the European Commission, para 7. See, for example, Case COMP/M.4381 *JCI/FIAMM*, Decision of 10 May 2007, paras 746-751; Case COMP/M.6447 *IAG/bmi*, Decision of 30 March 2012, paras 616-621.
[25] Case COMP/M.2810 *Deloitte & Touche/ Andersen UK*, Decision of 01 July 2002; Case COMP/M.2816 *Ernst & Young France/ Andersen France*, Decision of 05 September 2002.

dominance but concluded on the basis of its counterfactual analysis that no causal link could be found between the proposed transactions and a possible situation of collective dominance.[26] In this regard, the Commission noted that a reduction from five to four global accounting networks was inevitable and that the proposed merger was not more harmful for competition than other possible scenarios (such as the take-over of the Andersen assets by one of the other remaining Big Four audit and accounting firms, or the dispersal of Andersen's shares between the remaining firms).

The Commission has also conducted a broad counterfactual analysis in a number of failing division cases. For example, in *KLM/Martinair*,[27] even though the FFD was not strictly made out, the Commission's assessment of the relevant counterfactual took account of Martinair's financial difficulties, ageing assets, its significant investment requirements and difficulties in obtaining such investment to ultimately conclude that the merger-specific effects of the proposed concentration in respect of the parties' passenger air transport activities were likely to be limited.[28] Similarly, and more recently, in *IAG/bmi*,[29] upon concluding that none of the three strict criteria of the FFD were fulfilled, the Commission proceeded to assess the transaction on the basis of an "overall causality criterion," i.e. "*whether the likely outcome(s) of the counterfactual would produce a deterioration of the competitive structure in the market to a similar degree compared to the merger.*" The Commission found that this was not the likely outcome, given that, in the event of bmi's exit, the reallocation of its slots would have actually improved competition on the market.[30] It therefore insisted on expressing concerns and only approved the deal on the basis of remedies.

More broadly, outside the strict confines of a FFD, there are many cases where the Commission has looked at counterfactual scenarios involving diminution of a business (e.g. plant closures or exit from specific airline routes). A detailed analysis is beyond the scope of this paper. Just by way of example, in *Sappi/M-real*[31] the Commission took into account closures of paper mills (which were planned before and independently of the transaction) when assessing the combined market shares of the parties as a result of the transaction. In *Teva/Ratiopharm*,[32] the target had closed production facilities 6 months prior to notification. The Commission satisfied itself that manufacturing was unlikely to resume (either by the target or third parties) even if there was a price increase. The Commission therefore concluded that the relevant counterfactual was the decision to exit the markets for products made at the facility - and no overlap arose in respect of those products.

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[26] *Ibid*.
[27] Case COMP/M.5141 *KLM/Martinair*, Decision of 17 December 2008.
[28] *Ibid*, para 175.
[29] Case COMP/M.6447 *IAG/bmi*, Decision of 30 March 2012.
[30] See also Case COMP/M.2876 *Newscorp/Telepiù,* Decision of 02 April 2003, in which the Commission concluded that the first two of the three failing firm criteria were not made out and did not take a final position on the third. However, the Commission considered that the risk of exit, if it were to materialise "*would be a factor to take into account when assessing the…merger*". The Commission ultimately concluded on the basis of a counterfactual analysis that a conditional approval of the transaction would be more beneficial to consumers than a disruption caused by a potential closure of a particular platform (para 221).
[31] Case COMP/M.5283 *Sappi/M-real*, Decision of 31 October 2008.
[32] Case COMP/M.5865 *Teva/Ratiopharm*, Decision of 03 August 2010.

In several airline cases the Commission has also looked at counterfactuals involving changes in alliances or exit from routes.[33] In the original *Olympic/Aegean Airlines* case,[34] the Commission concluded that Olympic would have exited a number of routes, independently of the merger, and took this into account in its analysis by removing the routes in question from any concerns expressed (concerns remained in respect of other routes which led to prohibition of the deal as explained further below).

Response to the economic crisis

The Commission has on a number of occasions rejected any suggestion that it should adopt a more lenient failing firm test as a result of the economic crisis.

The Commission's view is that the test is designed to identify the limited circumstances where a firm's assets would exit the market but for the proposed merger and that it continues to serve this purpose. Senior Commission officials have emphasized that they consider that existing rules provide sufficient flexibility to enable the Commission to respond quickly to scenarios as they arise.[35] By way of example, the Commission considers that a lack of available capital in a market does not justify a relaxation of the failing firm requirements but can certainly be taken into account by the Commission in its factual assessment. It reasons that difficulties in raising capital may result in fewer viable buyers on the market, thereby facilitating the fulfillment by the notifying parties of the "no less anticompetitive solution" criterion.[36]

Recent cases

There has been speculation following the Commission's recent decisions in *Aegean/Olympic Airlines II* and *Nynas/Shell/Harburg Refinery*, which we discuss in greater detail below,[37] as to whether the Commission has finally relaxed its approach. This is not evident as it could be argued that the cases in question were just specific examples where the strict criteria of the FFD were clearly met. On the other hand, they could be seen as at

[33] See, for example, Case COMP/M.5747 *Iberia/British Airways*, Decision of 14 July 2010*;* Case COMP/M.5403 *Lufthansa/bmi*, Decision of 14 May 2009; Case COMP/M.5440 *Lufthansa/ Austrian Airlines*, Decision of 28 August 2009.

[34] Case COMP/M.5830 *Olympic/Aegean Airlines*, Decision of 26 January 2011.

[35] As noted by former Competition Commissioner, Neelie Kroes, "*the Commission is continuing to apply the existing rules, taking full account of the economic environment. Our rules provide the necessary flexibility to deal with decisions that require fast treatment, such as transactions which are part of rescue operations, in order to enable immediate implementation of these transactions. On substance, the EU merger control rules allow the Commission to take into account rapidly evolving market conditions and, where applicable, the failing firm defence*." SPEECH/09/385 "Competition law in an economic crisis", Opening address at 13th Annual Competition Conference of the International Bar Association. See also, comments by Philip Lowe in May 2009: "*In terms of our substantive assessment of the competition impact of a merger in crisis conditions, again we see no need to adjust our existing rules. The EC Merger Regulation already allows the Commission to take into account rapidly evolving market conditions in its competition assessment…Where applicable, we can also take into account a failing firm defence. We would of course examine any such defence very carefully – and it would have to meet strict conditions*", 14 May 2009 "*Keeping markets working effectively: Europe's challenge in recessionary times*".

[36] OECD Competition Committee, Meeting of 21 October 2009, Roundtable on Failing Firm Defence, Note by the services of the European Commission, para 19.

[37] We note that little information is publicly available. A more detailed analysis must therefore be undertaken to reach more definitive conclusions as to the Commission's approach once the decisions in those cases are published.

least an opening towards a more flexible counterfactual analysis outside the strict dogmatic conditions of the FFD.

Aegean/Olympic Airlines II

In its decision in *Olympic/Aegean Airlines I* in 2011 the Commission had rejected categorically the possibility that the failing firm or failing division defenses were applicable, as none of the three criteria were satisfied.[38] The Commission had however looked at counterfactual scenarios involving a number of individual routes and was able to conclude that both parties would remain competitive on those routes.[39] The Commission therefore found that the merger led to monopoly on several routes, that the proposed remedies were not sufficient and hence prohibited the merger.

However, by October 2013 as a result of the on-going Greek economic crisis and a significant deterioration of Olympic Air's financial situation, the Commission was in a position to approve the transaction. The Commission made clear that its decision to approve the transaction is attributable solely to the FFD. As noted by Commissioner Almunia in the press conference announcing the decision, "*had Olympic been able to continue operations outside of the Aegean group, the decision would have been a prohibition*" due to the overlaps between the parties on five routes.

The decision also appears to represent a rare example of the strict failing firm criteria being satisfied in the case of a failing division. In the Commission's 2011 decision, the substantial financial strength of Olympic Air's sole shareholder, Marfin, played a significant role in the disapplication of the failing firm/division defense. However, by 2013 the situation had altered sufficiently to enable the Commission to conclude that, with or without the merger, Olympic Air would be forced to exit the market in the near future. As the Commission noted, Olympic Air had never been profitable and the prospect of profitability in the foreseeable future was "*extremely unlikely*" under any business plan. Moreover, it appears that the financial position of Marfin had deteriorated since 2011, most recently as a result of an unsuccessful bond offering in summer 2013. The Commission therefore accepted written confirmation by Marfin that they were not prepared to provide further financial support to Olympic Air. In light of the on-going Greek financial crisis, it was unlikely that alternative sources of capital would have been readily available, particularly for a perpetually unprofitable organization such as Olympic Air. As a result, the Commission concluded that Olympic would have been shut down by Marfin if not acquired by Aegean.

Further, in the 2011 Decision, the Commission concluded that Marfin had significant incentives to avoid a bankruptcy of Olympic Air, as a result of the considerable exit costs and the likely negative effect on Marfin's credit ratings and ability to raise funds in the

[38] The Commission noted that the notifying parties had not explicitly argued a FFD, but had "put forward arguments analysing the defence criteria." Case COMP/M.5830 *Olympic/Aegean Airlines*, Decision of 26 January 2011, para 1988.

[39] See also Case COMP/M.5440 *Lufthansa/Austrian Airlines*, Decision of 28 August 2009, in which the Commission also conducted a counterfactual analysis in respect of specific routes.

equity markets.[40] However, in light of the significant deterioration of the airline sector in Greece[41] since that decision was adopted, and in Marfin's own financial position, it is likely that the Commission was this time in a position to discount such incentives.
Unlike in 2011, the second and third limbs of the FFD test appeared to have also been met relatively easily. Here, the Commission's market investigation confirmed that no other credible purchaser was interested in acquiring Olympic Air and, at the press conference announcing the clearance decision, Commissioner Almunia noted that one identified potential market entrant was now the subject of an in-depth State aid investigation.[42] Further, there had been no expression of credible interest in the acquisition of Olympic's "*very few assets*" including its brand, which was owned by the Greek State.

The Commission therefore concluded that "*there is no doubt that the "failing firm defense" scenario can apply and should apply in this case.*"[43]

In the light of the above, rather than representing a relaxation of the requirements for the FFD, this decision may simply demonstrate that in this particular instance there was ample evidence – given the significant decline in Olympic Air's financial position over the course of a three year period, which was largely attributable to the Greek economic crisis – that the FFD criteria had been met.

Nynas/Shell/Harburg Refinery Assets

In September 2013, the Commission cleared unconditionally the proposed acquisition by Nynas of the Harburg refinery assets of Shell Deutschland Oil.[44] The result of the transaction was that Nynas would remain the only producer of napthenic base and process oils in the EEA and would face substantial competition only from a US-based importer. However, after an in-depth investigation, the Commission concluded that the transaction would not raise competition concerns as, absent the transaction, the Harburg plant would simply have closed.

Shell Deutschland succeeded in demonstrating to the Commission that it was economically unsustainable for it to continue to operate the Harburg refinery in its current structure. During its in-depth investigation, the Commission concluded that there were no alternative buyers for the refinery assets. Therefore, the most likely alternative scenario to the transaction was the closure of the refinery, i.e. exit of the assets from the market.
One unusual feature of the case is that, unlike other 'failing division' cases, including *Aegean/Olympic II* (which can be seen as a more traditional FFD scenario), the parent company was not experiencing financial issues and it was not suggested that its financial health would have been impacted by the difficulties faced by the refinery assets. In this respect, one could postulate that the case involves a more lenient application of the failing

[40] See Case COMP/M.5830 *Olympic/Aegean Airlines*, Decision of 26 January 2011, paras 2034-2039.
[41] See SPEECH/13/800, Statement on Aegean/Olympic Air merger, 9 October 2013.
[42] See Case SA.35888 (2013/C) - Rescue aid for Cyprus Airways (Public) Ltd.
[43] SPEECH/13/800, Statement on Aegean/Olympic Air merger, 9 October 2013.
[44] Press release IP/13/804 Mergers: Commission approves acquisition of Shell's Harburg refinery assets by Nynas AB of Sweden, 02 September 2013.

division test. However, the Commission's decision appears to have been influenced by submissions by Shell Deutschland during the in-depth investigation that the refinery assets were economically unsustainable in their current set-up and that the acquiring company had proposed a different business model for the assets, which required significant investment. This approach may therefore be similar to that taken in *KLM/Martinair* where a broader counterfactual analysis disclosed the extent of investment that would have been required for Martinair to be a viable competitor on the market, thus enabling the Commission to conclude that the transaction would have limited effects on competition. The decision may also have been informed by the practical impact that closure of the refinery assets would have for EEA consumers. The Commission concluded that exit of the assets would have reduced EEA production capacity for napthenic base and process oils below EEA demand levels, resulting in higher prices for consumers. The Commission also identified some merger-specific efficiencies, which it considered were likely to be passed on to consumers.[45]

Conclusion

A number of observations can be made on the basis of these recent cases.

First, despite the sequence in a short space of time, it is not clear that these cases represent a radical departure or relaxation in the Commission's approach to FFD situations. As in the past, it is highly unlikely that the Commission will be in a position to accept a FFD absent an in-depth investigation or compelling evidence. It will be generally quite difficult to provide the Commission with the necessary reassurances about the financial situation of the target (and its parents) and the availability and viability of alternative purchasers in the comparatively short period of a Phase I review.

Second, the cases do, however, demonstrate that the FFD can succeed if clear evidence is available to demonstrate to the Commission that the three criteria are met. In light of the current economic climate, a significant deterioration in the financial situation of a company, demonstrated with clear factual evidence, may even suffice to overturn a previous rejection of the FFD. The Aegean/Olympic case is a good illustration of this point. Third, despite the success in those situations which might hint at a possible more open approach, the Commission is likely to continue to apply the FFD in a strict fashion and only in exceptional cases will all of the criteria be made out. In this regard, it is clear that the Commission's decision in *Aegean/Olympic II* was informed by the specific circumstances affecting the company and its parent, and the Greek economy. In *Nynas/Shell/Harburg Refinery*, while the Commission's broader counterfactual analysis certainly appears to have played a role, the Commission still concluded that exit of the assets from the market was the most likely alternative scenario to the notified transaction. As such, these decisions do not suggest a significant departure by the Commission from its previous practice.

Nevertheless, perhaps the two cases could be seen as a wider acknowledgment that the FFD is simply a specific example of counterfactual analysis and there is no "magic" involved

[45] *Ibid*.

in the three criteria specified in paragraph 90 of the Horizontal Merger Guidelines. Even where the three strict FFD criteria are not met, it is still open to the Commission to conclude that a diminution in competition will not be caused by the notified transaction. In particular when it comes to the first criterion (exit due to financial difficulties) a more open approach could be applied by the Commission to allow greater scope for counterfactual scenarios involving diminution in the competitive force of a business such as closures of divisions, plants or specific lines of business. Cases such as *Sappi/M-Real, IAG/bmi,* and *Teva/Ratiopharm* show that the Commission can and does take such considerations into account. Olympic, and in particular Nynas, can perhaps be seen as part of this wider counterfactual approach.

Such a broader approach to the counterfactual would be closer to the one employed by the UK competition authorities where the FFD or FFD-style scenarios appear to have been more successful than at EU level.[46]

If this broader approach were to become the norm, it would indeed be time to bid farewell to the FFD at least in its distinct, dogmatic form. The FFD would simply become one example of a specific counterfactual of diminishing competitive constraint absent the merger. Very clear and convincing evidence will still however be required as in any counterfactual scenario. We do not therefore expect any great flood of FFD-style defenses to be successful in the years to come.

[46] See, for example, *Stena AB and DFDS A/S merger inquiry*, Decision of the Competition Commission on 29 June 2011. There the Commission found that the decision to close a route was linked to the transaction. Nevertheless, it analysed whether, on the basis of the available evidence the route would have remained open on the counterfactual. The Competition Commission concluded that the least costly option was to close the route and that exit would have occurred in any event, absent the transaction. In light of this, and the potential cost of re-entry, it was concluded that the exit of the route represented the appropriate counterfactual. See also *Sector Treasury Services and Butlers merger inquiry*, Decision of the Competition Commission on 31 August 2011.