A Highway Heist and a Scot-free let go

written by Rhea Susan Verghese | April 28, 2020

Failing Firm Defence as Tool in the Landscape of Mergers

The first question that routes into understanding would be, what is a failing firm and a defence in connection to the same. This means a commercial failure of the target firm as a consequential bearing of a prohibited merger, and the prohibition being used as a defence. When a particular firm is fiscally weak or has decided to depart from the market, merger control proceedings would involve the acquisition of such a firm or maybe the assets of the entity. Now, when an acquisition among very few competitors occurs, there is a leeway of substantial lessening in competition in the germane marketplaces. In situations of the like, merging parties use the failing firm defence ("FFD") as a scot-free let go for easy merger clearance on a preferential first-hand basis. As much as merger parties pull in multiple ways of a free escape, the process as a whole would have to suit the elements of an FFD in the eyes of the competition authority.

The elements of consideration would be; if irrespective, the failing firm would leave/exit the market premise if the merger had not taken place or would the loss of the firm have a lessening impact of competition in the pertinent markets or apart from the merger, is there no lesser competitive alternate?

Do not Dismiss the Elements

The first condition requires the notifying parties to prove their financial difficulties with respect to the conditioning perspective of them being a failing firm. Also, the competition authority is not going to take into consideration a plain showcase of the company's accounts. The demand for high-level evidence will be the requirement failing which the analysis of the same will not lead to suiting of the first condition.

The parties will have to show their internal documentation which was to be made use of prior to the specific merger, show the alternate strategies adopted by them towards the merger consideration as the last resort, for e.g. the minutes of the respective board meetings or investor presentations. This can put the notifying parties into a dilemma as they will want to paint a positive picture of failure to attract potential buyers while the competition authority will want to scrutinize their every move.

The deliberation of the second condition will mean and require the warning parties to prove that such acquisition shall not create anti-competitiveness or lessening of competition in the pertinent markets in comparison to the natural digression of customers to opposing firms which is a natural phenomenon in such cases. Analytically, the likely behaviour of the supposed failing firms' customer base will be the criterion of assessment.

If in conclusion, it shows that customers of the existing market can do with buying from smaller markets as against the ones of the merging parties or can wholly buy from alternate firms in equilibrium or higher shares, then such loss will speak otherwise. In such cases where the acquisition shows a less anti-competitive effect, then the requisite merger is a likely scenario in all probabilities.

The third and final condition requires that the merging warning parties show that there are no substitute purchasers and even if there are, the outcome of the same will lead to anti-competitive effects in the germane marketplaces. The operations of an alternate purchaser might not necessarily be in the same market of the existing firm, yet if such a purchaser being the neighbour party of such firm shows interest in the purchase and knows the works of the firm, then such purchaser is deemed to be a credible alternate purchaser.

As for the latter half of the statement, the stake in market share will be the standard norm of assessment. Higher market share than the capital purchaser will simply mean, no likeliness of an anti-competitive effect in the pertinent market. All for all, an FFD with reference to a credible alternative purchaser in the picture is difficult to prove given that the intentions of such purchasers will act for the existing firm as a fear of the unknown.

Has India witnessed the failing firm apocalypse and used it as a defence?

30 million tons of steel was pushed under the bankrupt carpet of India which involved the two steel giants of the nations i.e. Tata Steel and Bhushan Steel.[1] A breach in the form of an acquisition came to light which required the prior approval of the Competition Commission of India ("CCI") before the approval of the resolution plan go-ahead given by the committee of creditors in the Insolvency and Bankruptcy Code ("IBC"). It is the CCI that decides on the combination perspective under Section 5 of the Competition Act.

As much as CCI stands as an important decision-maker, it respects the timelines governed by IBC and any combination arising out of the same allows the resolution applicant to achieve the 'Green-Channel' approval from CCI as well. The green channel approval is meant to help in speedy trial of combination cases arising out of the IBC. The main role of the CCI is to make sure that the proposed combination is not likely to have an appreciable adverse effect on the competition in India. This was well observed in the present case as well.

A Parallel Conclusion?

For a firm to be able to rely on this defense as a corporate rescue, the route to recovery in such a case should showcase absolute impossibility and a cent percent probability of failure in spite of having tried all alternatives. The firm has to show up like being bankrupt with no rescue to recuperating without a helping hand. India pretty much has a fine merger regulation mechanism on board, and following the conditions will pave the way to transparent and speedier means in trial.

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[1] Combination Registration No. C-2018/03/562

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