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The Growing Acceptance of the Failing Firm Defence in UK Merger Control

Recent case law demonstrates a growing acceptance by the CMA of the defence, leading to merger clearance.

Overview

The failing firm defence—the principle that a firm would inevitably have exited the market in the absence of the transaction in question, historically a narrowly applied and rarely successful "defence" to an otherwise anticompetitive merger in the UK—has gained renewed prominence following recent CMA decisions in 2024–2025. The CMA's updated Merger Assessment Guidelines' (since 2021) two-limb exiting firm counterfactual may have prompted a more pragmatic and context-sensitive approach by the CMA. Recent cases demonstrate both the CMA's continued insistence on compelling evidence and a greater willingness to recognise inevitable exit based on that evidence. This marks a notable shift from the historically strict approach seen in earlier OFT and CMA practice at both Phase I and II. The UK's approach since 2021 differs from the European Commission's ("Commission") three-limb framework, but both regimes continue to anchor their analysis in demonstrable inevitability of exit and the absence of a less anti-competitive purchaser for the firm or its assets to the acquirer in question.

The Recent Application of the Defence

The last two years have produced several milestone cases that illustrate both the CMA's strict evidential bar and a more pragmatic, context-sensitive application of the test.

Failing firm arguments have typically been more successful in Phase II given greater time and ability for the CMA to interrogate financial information and to market test alternative bidder appetite and internal materials.

However, in 2024, the CMA cleared *Eurofins/Cellmark* at Phase I in only 11 days, accepting compelling evidence of Cellmark's deteriorating financial position, its importance to critical services (Cellmark was a supplier to UK police forces and government bodies), and the absence of viable alternative purchasers.

The trend in Phase I continued in 2025 with *Bidvest/Citron Hygiene*, where the CMA found Citron's continued exit from national and multi-regional supply inevitable and no realistic alternative purchaser, and with *Sportradar/IMG Arena*, where the CMA accepted a strategic-exit variant and found no less anti-competitive purchaser. In 2025, the CMA also cleared *Rundvirke Industrier AB / Calders & Grandidge (Boston) Limited* at Phase I, finding that absent the Merger, C&G's former owner Saint-Gobain would have closed the business, and there was no realistic prospect that C&G would have been sold to a less anti-competitive purchaser.

In September 2024, in *Tate & Lyle Sugars/Tereos*, the CMA initially rejected the failing firm argument at Phase I but accepted it at Phase II after deeper scrutiny, where it assessed additional documentary, financial and third-party evidence. At Phase I, the CMA's assessment found that the merger would have created a duopoly (the only other competitor being British Sugar) and found a realistic prospect of an SLC, rejecting the failing firm argument on the basis that Tereos' exit was not inevitable under limb 1. At Phase II, the CMA determined that, absent the merger, the most likely scenario was that Tereos would have closed the target and exited the UK B2C channel, leaving no competition between TLS and the target, and therefore, the conditions of the failing firm defence were met.

On 22 January this year, the CMA provisionally cleared at Phase II the completed acquisition in *Constellation Developments Limited / ABVR Holdings Limited*. The transaction, which concerns the used vehicle remarketing and retail sector, was found to satisfy limb 1 on the basis that Aston Barclay could not have continued as a going concern absent the merger, as it had no access to capital necessary for its restructuring. On the second limb, the CMA found that, although there were four alternative interested purchasers, the transaction would have resulted in weaker conditions of competition because they would not have been prepared to run the target as a national player compared to the pre-merger conditions. The clearance, though provisional for now, once again shows the regulator's increased willingness to consider and accept the defence.

These decisions indicate the defence is now being accepted more often. The period 2020-2023 saw only one acceptance (*Nijjar (Acton)/Medina*) at either Phase I or II. By contrast, 2024 saw acceptances of the failing firm defence in *Eurofins/Cellmark* and *T&L Sugars/Tereos*, and 2025 in *Rundvirke/Calders & Grandidge* and *Sportradar/IMG Arena*, as discussed above. 2026 may continue this upward trend as the CMA published its first failing firm (provisional) acceptance decision within the first month of the new year (in *Constellation Developments*, above).

While an element of successful application is, of course, macro-economic factors and the presence of a greater number or more persuasive examples of distressed businesses within the CMA's case mix, these greater success rates may also be explained by the CMA's two-limb framework, which was introduced by the revised 2021 Merger Assessment Guidelines. These reframed the defence as a two-limb "exiting firm" counterfactual focusing on: (i) whether the firm would exit (through failure or otherwise) absent the deal; and (ii) whether there is no less anti-competitive alternative purchaser. The CMA removed the old "third limb" whereby it considered whether the exit of a business would be a substantially less anti-competitive outcome than the merger, although arguably this is subsumed into the other limbs and overall competitive assessment.

Prior CMA Practice

The failing firm counterfactual has operated as a narrow and exceptional doctrine within UK merger control, applied successfully in only a small number of cases before 2024. Between 2003 and 2023, the OFT and subsequently the CMA accepted the defence in *First West Yorkshire/Black Prince Buses*, *Tesco/Kwik Save*, *CDMG Group/Ferryways*, *Homebase/Focus*, *HMV/Zavvi*, *East Coast Buses/First Scotland East*, *Sports Direct/JBB Sports*, *Aer Lingus/CityJet* and *Nijjar (Acton)/Medina*. The agencies consistently required parties to demonstrate that the target firm would inevitably exit the market absent the merger, that no substantially less anti-competitive alternative purchaser existed, and—under the earlier three-limb test—that the merger would not produce worse competitive outcomes than exit. In practice, most cases failed on the second limb of the test: it has been very difficult for merger parties to show that there is no buyer in the market for assets above liquidation value; particularly when the target was not subject to an auction process prior to sale. The OFT expressly required "sufficient compelling evidence" given the high stakes of accepting such a counterfactual, applying rigorous scrutiny to internal documents, third-party confirmations, auditor reports, and the circumstances of financial distress.

There are limited instances where the CMA has accepted that the prevailing pre-merger competitive conditions were not sustainable, which in turn influenced the outcome on remedies and clearance. In *Müller/Dairy Crest*, the CMA assessed the transaction against a counterfactual in which the target's operations would contract to a single site (Severnside) absent the deal. The CMA did not consider continuation of the status quo to be realistic: it concluded that the target's remaining assets would inevitably exit for strategic reasons and that there would be no purchaser that was materially less anti-competitive. By contrast, in *Medtronic/Animas*, while the CMA accepted that Johnson & Johnson had widely marketed the Animas business without success and had decided to exit, it could not rule out the existence of less anti-competitive purchasers for certain assets (notably customer and patient records and limited ancillary assets) transferred under the deal. Nevertheless, the CMA accepted at Phase I that these limited transfers did not give rise to a substantial lessening of competition. In *Eurocar Parts/Andrew Page*, the CMA concluded at Phase II that 49 depots for which there was no alternative purchaser and therefore for which the counterfactual was closure did not give rise to an SLC and so were not part of the remedy package (while the depots for which there was an alternative purchaser and gave rise to an SLC were).

Illustrative cases demonstrate the rigour applied by the CMA: in *First West Yorkshire/Black Prince Buses* the OFT required proof of the owner's retirement, financial unsustainability, and unconditional sale of the depot, plus evidence that the business had been marketed to over 60 operators without alternative interest. In *HMV/Zavvi*, clearance turned on landlord rejections of competing bids, leaving HMV as the only viable purchaser for several overlap stores. As outlined above, an observable shift occurred with the CMA's 2021 Merger Assessment Guidelines, which consolidated the framework into a two-limb test by folding the third-limb analysis into the broader competitive assessment. *Nijjar (Acton)/Medina* marked the first successful application of this revised approach.

The CMA also rejected several claims where parties could not meet the stringent evidentiary tests, including *Whitby Seafoods/Kilhorne Bay*. There, the CMA found that the first limb-that exit was inevitable or that its current shareholders would have not been able to continue managing the business in the short to medium term, absent the merger-had not been established, noting that Kilhorne Bay remained profitable with increasing revenues. The case illustrates how difficult it is to satisfy the CMA's requirement for "compelling evidence" of inevitability at Phase I. The merger was referred to Phase II, but the parties abandoned the transaction, stating that the resources required to engage in a Phase II investigation were out of all proportion to any potential benefit from the deal. Similarly in *Poundland Group plc/99p Stores*, the CMA found that while the target business had operational difficulties, there was no reason to believe that it was structurally unsound and could not be fixed. These rejections underscore the doctrine's historically narrow scope and the high bar for meeting the conditions of the test.

Comparing the UK's approach to that of the EU

The CMA treats failing firm claims within its counterfactual framework for the SLC test. In setting the counterfactual, it looks to a realistic, foreseeable non-merger future and, in an exiting firm scenario, asks whether the target would imminently exit and whether there is a credible, less anti-competitive alternative purchaser. If those conditions are met, the counterfactual is exit or sale to that alternative buyer; the comparative question (*i.e.,* whether the merger worsens competition against that baseline is then addressed in the substantive competition analysis). Even where the strict conditions for an exiting firm counterfactual are not met, evidenced financial weakness can still inform the competitive assessment. A credible alternative buyer can also anchor the counterfactual, even if its offer falls below the seller's preferred price, provided it exceeds liquidation value.

Under the Horizontal Merger Guidelines (HMG), the Commission applies three cumulative conditions: (i) the firm must be about to exit the market without the deal, (ii) there must be no less anti-competitive buyer available, and (iii) competition would be no worse because the firm's assets would otherwise leave the market anyway.

This causality-based framework appears stricter than the CMA's two-limb approach. Since the Guidelines came into force in 2004, only two failing firm defences have been accepted—*Aegean/Olympic (II)* and *Nynas/Shell/Harburg* (with the latter being cleared on the basis of a combination of the failing firm defence and merger efficiencies). Notably, both cases involved only a division of the seller, rather than the entire firm, suggesting the Commission may be more willing to accept the defence in such circumstances.

The requirement in the HMG that the failing firm's assets would "inevitably" exit the market and the Commission's strict interpretation set a very high threshold, making clearance under the failing firm defence extremely difficult in practice. However, this may be about to change. In May 2025, the Commission launched a public consultation on the review of the HMG. The updated guidelines could signal a shift in the assessment of the failing firm defence in the EU in the near future.

Key Takeaways

- **CMA's pragmatic shift**: The CMA is applying a more context-sensitive, two-limb "exiting firm" counterfactual—focusing on inevitable exit and absence of a less anti-competitive buyer—while still demanding compelling evidence. Recent cases demonstrate that what was previously considered a near-insurmountable bar to meet, has now been achievable in more (of course, fact-dependent) cases.

- **CMA will still apply rigour to its fact-based assessment**: Parties must be able to demonstrate to a high evidentiary standard that the target would inevitably have exited the market absent the merger (via financial failure or as a result of e.g., a strategic shift), and that no alternative, less anti-competitive purchaser of the firm or its assets than the acquirer was found.

- **UK–EU divergence endures**: The UK's two-limb approach contrasts with the Commission's stricter three-limb, causality-based framework, which fixes a closure/asset-exit counterfactual and ties timing to real-world sale processes.

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This memorandum is not intended to provide legal advice, and no legal or business decision should be based on its content. Questions concerning issues addressed in this memorandum should be directed to:

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