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COMPETITION COMMITTEE****Barriers to Exit – Note by Colombia**

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This document reproduces a written contribution from Colombia submitted for Item 8 of the 132nd Competition Committee meeting on 3-4 December 2019.

More documents related to this discussion can be found at
<http://www.oecd.org/daf/competition/barriers-to-exit.htm>

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1. Theoretically, the existence of barriers to exit weakens the current mechanisms to relocate resources not optimally assigned, either to a different market or from one firm to another. In such sense, inefficiencies may appear as a result of keeping firms in the market who wish to exit but are unable to, due to the barriers they face to exit. These inefficiencies are generated because resources, both capital and labor, cannot be relocated efficiently, either within the same market (to more efficient agents, existing or new) or in other economic sectors, and agents' intentions to improve their market position or enter a new market would be affected.

2. In Colombia, the existence of barriers to exit hasn't been widely studied by this Superintendence because, in general, in the analyzed markets agents face these barriers equally, and therefore it doesn't imply a competition unbalance, hence they don't represent a main concern to this Competition Authority.

3. Nevertheless, since one of the most common ways for a firm to exit from a market is through mergers with their competitors or with firms that are vertically related to them, there have been some extreme cases in which the Superintendence of Industry and Commerce has been forced to restrict the exit of a competitor, due to the current competition structure in the market and the way the merger operation was presented. These restrictions were imposed in order to encourage the merging companies to propose mechanisms to limit or compensate the negative effects on competition shall the merger be completed in the terms in which it was presented.

4. These extreme cases occur when the merger operation significantly reduces competition. This happens when the exiting company, in order to reduce losses, opts to sell their assets of specific use to active competitors who already hold a strong position in the market. This way, clearing the merger, besides substantially improving the market position of a previously important agent, reduces the number of competitors and market contestability by impeding the entry of a new agent with the strength to counter the capacity of the dominant agent to affect the competition in the relevant market.

5. For these reasons, the decisions taken by the Superintendence of Industry and Commerce seeks to keep or even improve competition levels, either through the entry of new agents to the market or by reassigning the assets to existing agents that could counterweight the market leader, who intends to acquire them within the merger operation presented.

6. In the first scenario, the new agent could obtain through the purchase of assets a portion of the market very quickly, as well as the installed capacity necessary to compete in nearly the same conditions as the leaving company. On the other hand, in the second scenario where an incumbent agent different than the leader obtains the assets the leader agent wants, the competition capacity of this incumbent agent would be strengthened, allowing them to compete in better conditions with the current market leader.

1. Merger case of *Chlorine – Soda*

7. Recently this Superintendence analyzed the merger operation between **QUIMPAC DE COLOMBIA S.A. (QUIMPAC)** and **MEXICHEM DERIVADOS COLOMBIA**

S.A. (MEXICHEM), by which **QUIMPAC** intended to buy 100% of **MEXICHEM**'s shares.

8. In particular, **MEXICHEM**, arguing insufficient profitability levels, wanted to exit from the market by selling their assets to **QUIMPAC**, lead agent in the chlorine, caustic soda and ferric chloride markets, and the second most important agent in sodium hypochlorite, whom as a consequence of the intended operation would attain a dominant position in all the aforementioned markets, markets that already hold high concentration levels.

9. Furthermore, the Superintendence of Industry and Commerce determined that the involved markets have features that support the previously discovered concerns in regards of competition. Such features were mainly related to: (i) the specific use of production plants, which can only be used to produce chlorine and/or caustic soda derivatives; (ii) the existence of synergies in the production of goods in the chlorine-soda chain; (iii) the strong regulations in the chemical industry, specially due to the toxicity of products and derivatives; and (iv) the surplus production of chlorine and the deficit of caustic soda, which becomes an important factor because the only way to produce higher amounts of caustic soda is by producing more chlorine (simultaneous production).

10. Moreover, the Authority found that **MEXICHEM** is the main client of chlorine from **BRINSA S.A. (BRINSA)**. This allows **BRINSA** to produce caustic soda and sodium hypochlorite, and thus compete effectively with **QUIMPAC** in different markets.

11. Taking into account these features and the competition structure of the related markets, this Superintendence concluded that the intended operation would reinforce high concentration levels already existing in all analyzed markets, strengthening the position **QUIMPAC** holds over its competitors and generating closed market structures that may facilitate the coordination between the active agents in them. Additionally, it was found that there are strong barriers to entry in the relevant markets, namely a high initial investment, the existence of high sunk costs, long term for investment recovery, high idle capacity, unviability for imports (except for caustic soda) and legal and environmental barriers in both long and short term.

12. Considering the conclusions reached, the Superintendence of Industry and Commerce invited the intervening companies to propose remedies that could mitigate the negative effects on competition in case of completing the merger operation. However, this Authority found the remedies proposal presented by **QUIMPAC** and **MEXICHEM** insufficient to mitigate the harmful effects identified, and therefore, chose to object the operation even though this decision prevented, for now, the exit of an agent that alleged not having sufficient profits on their investment.

2. Merger case of **EXXONMOBIL—TERPEL (2016-2018)**

13. Another case in which the Superintendence of Industry and Commerce had to make a decision that delayed the departure of an agent from the market was the merger operation between **EXXONMOBIL DE COLOMBIA S.A. (EXXONMOBIL)** and **ORGANIZACIÓN TERPEL S.A. (TERPEL)**.

14. In this case, **EXXONMOBIL** was interested in leaving the lubricants and liquid fuels markets, and **TERPEL**, the main agent in some coincidental markets showed interest

in purchasing their specific use assets. In particular, these two agents shared participation in the following markets:

1. Wholesale distribution of regular gasoline.
 2. Wholesale distribution of premium gasoline.
 3. Wholesale distribution of diesel.
 4. Retail distribution of regular gasoline.
 5. Retail distribution of premium gasoline.
 6. Retail distribution of diesel.
 7. Production and sale of lubricants for diesel engines.
 8. Production and sale of lubricants for motorcycles.
 9. Production and sale of lubricants for automotive transmission in general.
 10. Production and sale of lubricants for cars.
 11. Production and sale of greases in general.
 12. Production and sale of industrial lubricants.
15. The Superintendence of Industry and Commerce found that the intended operation would consolidate **TERPEL** as absolute leader in each wholesale liquid fuels market (regular and premium gasoline, and diesel), with market shares of more than 60% and with a considerable distance regarding their immediate competitor. Additionally, it would grant **TERPEL** a higher bargaining power against retail distributors due to the high connectivity between retail and wholesale distribution of liquid fuels along with the aggregated coverage of gas stations (GS) between **TERPEL** and **EXXONMOBIL**.
16. Moreover, the acquisition by **TERPEL** of the supply plants needed to exert wholesale distribution activities could impede or limit the development of other wholesale distributors, as well as the entry of new competitors, since with the intended operation, **TERPEL**'s storage capacity would represent more than 50% of the total national capacity.
17. In regard to the lubricants market, the intended operation would strengthen **TERPEL**'s market share, mainly in the industrial lubricants market, in which it would obtain more than 60%. Regarding the lubricants for motorcycles, cars and diesel engines markets, the Superintendence of Industry and Commerce determined that the operation would considerably enlarge the gap between **TERPEL** and its closest competitor. This would imply that every lubricants market (diesel engines, cars, motorcycles and industrial type) would become highly concentrated. Besides, the Superintendence discovered that there are recognized and consolidated brands nationwide for lubricants, and the GS sales channel is significantly important, especially in the car products markets.
18. Considering the conclusions reached, the Superintendence of Industry and Commerce convened the intervening companies to inform them about the possible anticompetitive effects of the intended operation, in order for them to propose remedies that mitigate the concerns found. In this sense, the companies proposed the transfer of the wholesale, industrial and retail commercialization of liquid fuels business to a third party in a term no longer than 36 months after the completion of the merger. Regarding the negative effects in the lubricants market, the intervening companies didn't propose any remedies that could isolate or eliminate possible restrictions to competition caused by the intended operation.

19. Under the above, the Superintendence of Industry and Commerce conditioned the merger operation between **TERPEL** and **EXXONMOBIL** to the compliance of a series of behavioral and structural remedies. These included the sale of the wholesale, industrial and retail commercialization of liquid fuels business to an independent third party, and the sale of some assets related to **TERPEL**'s lubricants market.

20. Thus, in order to comply with the imposed remedies, **TERPEL** and **EXXONMOBIL** had to search for a client for such assets, delaying **EXXONMOBIL**'s exit from the market.

3. Conclusion

21. As a conclusion, in Colombia, in some extreme merger cases where a very closed market competition structure and high barriers to entry have been identified, the decisions taken by the Competition Authority, within the framework of the ex-ante merger control, may delay or forbid the exit of an agent from the market, in order to avoid high concentration levels (that may constitute in high barriers to entry) and to maintain competition levels in the market.

22. However, the Superintendence of Industry and Commerce recognizes the importance of analyzing barriers to exit, in those cases in which their existence affects competition. As for example in markets related to the provision of public services, where there are high sunk costs.

References

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