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**DIRECTORATE FOR FINANCIAL AND ENTERPRISE AFFAIRS  
COMPETITION COMMITTEE**

### **Working Party No. 3 on Co-operation and Enforcement**

#### **AGENCY DECISION-MAKING IN MERGER CASES: FROM A PROHIBITION DECISION TO A CONDITIONAL CLEARANCE**

-- Note by Colombia --

**28-29 November 2016**

*This document reproduces a written contribution from Colombia submitted for Item 4 of the 124th meeting of the OECD Working Party No. 3 on Co-operation and Enforcement on 28-29 November 2016.*

*More documents related to this discussion can be found at [www.oecd.org/daf/competition/agency-decision-making-in-merger-cases.htm](http://www.oecd.org/daf/competition/agency-decision-making-in-merger-cases.htm)*

Please contact Ms. Despina Pachnou if you have any questions regarding this document [phone number: +33 1 45 24 95 25 -- E-mail address: [despina.pachnou@oecd.org](mailto:despina.pachnou@oecd.org)].

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-- COLOMBIA --

1. From an economic perspective, merger control is supposed to prevent undue competition restrictions that can derive from certain transactions. In that sense, competition authorities should focus primarily on the detection of such restrictive potential effects. However, an efficiency approach can reveal the potential benefits of the transaction, which if it were to be blocked society might never harness.
2. Competition authorities are experts in identifying potential anti-competitive and pro-competitive effects that could result from a merger. But when it comes to estimate the magnitude of those effects, authorities usually face numerous challenges (especially young agencies), particularly because no specific methodology has proven to be failsafe.
3. Without having reliable and affordable tools to estimate the extent of the identified pro-competitive and anti-competitive potential effects of a transaction, it is highly difficult for a competition authority to balance those effects, in order to identify the real (net) potential result over competition.
4. As competition authorities constantly face statutory time constraints, among other resource restrictions, the challenge is to minimize what in statistics is called a type one error (or alpha error), which in merger control occurs when an authority grants clearance to a transaction that should have been blocked, or conditioned. In contrast, a type two error (or beta error) occurs when a transaction that could have been authorized, is blocked or conditioned.
5. As a type one error is much more harmful for competition than type two error, it is desirable to minimize the occurrence of those mistaken authorizations. This could be achieved if competition authorities focus on the anti-competitive effects, rather than offsetting these with the pro-competitive ones, as any transaction that has to be blocked or conditioned after conducting the latter analysis, will certainly be blocked or conditioned under the former, as no potential benefits would have been taken into account.
6. It is not about ruling out the possibility that competition authorities conduct efficiencies analyses, however due to time and other resources constraints, and in order to minimize the possibility of harming competition, those analyses should be reserved for exceptional cases, and the burden of proof should always rely on the merging parties, rather than on the competition authorities.
7. In this sense, the Colombian merger control regime includes an exceptional possibility of a conditional clearance, for transactions that have the potential to harm competition, provided they: (i) bring along pro-competitive effects that outweigh the harm; and, (ii) such benefits cannot be reached through other means. In any case, the merging parties must demonstrate to the SIC that the two conditions are met.
8. Colombian competition law also requires that in such cases where the clearance is granted after an efficiency analysis; the authorization should be accompanied by a set of remedies that ensures the resulting efficiencies will be transferred to, or at least shared with consumers, so the benefits will not be taken over by the merged firm.

## 1. Mergers that have been prohibited in the last five years by the SIC

9. The Superintendence of Industry and Commerce (SIC) has blocked two mergers in the last five years, one in 2015 and the other one in 2016.

10. In the first proposed transaction, Terpel, a specialized firm in fuel distribution for different types of transportation (boats, aircrafts, cars, etc.), was going to acquire a retail aircraft fuel distributor (Aviacom), located in three Colombian airports where Terpel had presence exclusively as a wholesale distributor (vertical merger).

11. Terpel is also a retail distributor in a large number of airports in Colombia, including the ones that concentrate most of the national air traffic (horizontal effects), and has 75%-85% of the wholesale market. Furthermore, Terpel is the current retail distributor of most of the fuel consumed by the largest airlines in Colombia (who represent more than 70% of the national demand and more than 80% in the three airports included in the transaction).

12. The combination of this advantageous position and portfolio effects, would in the short run result in most airlines switching their demand in the three airports, from Aviacom's competitors to Terpel. Even though at the moment of filing Aviacom was between second and fourth place amongst its competitors, none of them were vertically integrated, nor could they effectively compete with Terpel, as they had no presence in other airports, and this would have consolidated Terpel as a monopolist retailer.

13. Terpel proposed remedies that were not accepted by the SIC, as they were limited to behavioral ones regarding non-discriminatory treatment of its retail competitors, as their wholesale distributor, and this was not enough to eliminate or even mitigate the potential harm of the transaction.

14. The second prohibited transaction was also filed by Terpel and it involved the supply of aviation fuel in Colombia's second largest airport. It was an application to become the exclusive operator of the airport's fuel distribution network, an essential facility that allows the delivery of fuel sold by different retail distributors, to the various aircraft. If approved, Terpel, as the dominant retailer in this airport (greater than 90% market share and high entry barriers), would achieve a significant competitive advantage, given it would control an essential facility that every other retailer has to use in order to distribute their product. This, in the short run, would exclude other minor distributors, who mainly supply to private owners and small airlines, from the market.

15. As in the first case, Terpel proposed behavioral remedies regarding non-discriminatory treatment to its retail competitors, which could not eliminate nor alleviate the competition concerns.

## 2. Some mergers that have been cleared subject to remedies by the SIC in the last three years

16. Some important mergers that the SIC has recently cleared subject to remedies are in the supermarket sector and in the beverage sector (non-alcoholic drinks).

17. One of them was a merger between the largest supermarket chain in Colombia (Exito), and a medium-size chain located in the South-West. Applying the isochrone technique to define all geographic markets involved in the transaction, the SIC ranked them with an index<sup>1</sup>, according to the combined effect on concentration levels due to the magnitude of the change and the final level of concentration.

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<sup>1</sup> The index formula was:  $index = \sqrt[2]{HHI_{final} * (HHI_{final} - HHI_{initial})}$

18. Considering that there are substantial entry barriers in this market, the SIC determined an objective “tolerance” threshold<sup>2</sup>, to select all the isochrones where the simulation yielded high increases or high final levels of concentration, and where the parties would have to make divestitures in order to achieve a “tolerable” effect on the market.

19. Another important conditioned merger was the one between Pepsi and Postobon, regarding the production, distribution and commercialization rights of *Gatorade* in Colombia. In this case the SIC concluded there were no significant concentration effects in the market, as there were at least two segments of isotonic drinks (“premium” and “regular”) and, for its price and target, *Gatorade* was the only product that belonged to the premium category.

20. Nevertheless, due to some potential vertical effects arising from Postobon’s commercialization of important production factors for isotonic drinks (such as sugar), the SIC imposed a set of behavioral remedies regarding non-discriminatory treatment to other isotonic drinks producers. The SIC also required the design and implementation of a compliance program, by the acquiring firm (Postobon).

### **3. ‘Best practice’ regarding prohibitions and remedies imposed by the SIC**

21. Colombian competition law (Law 1340/2009) establishes that a merger should be blocked if it “tends to produce an undue restriction of competition”, which could happen, in general, whenever it affects “competition freedom, consumer welfare or market efficiency”. However, competition law also provides that an objectionable transaction can be cleared by imposing remedies that are “suitable to ensure effective preservation of competition”.

22. For vertical mergers the analysis is usually less restrictive, as this kind of transactions do not rise concentration levels, usually bring notable efficiencies as they eliminate transaction and intermediation costs between different links of a value chain, and rarely have the potential to harm competition.

23. In the case of horizontal mergers, there seems to be relative consensus around the fact that most of them, besides presenting some efficiencies that can be derived from economies of scale, tend to increase market concentration, and therefore, reduce competition. Still, most of these transactions get clearance from competition authorities, and this occurs because most agencies “tolerate” small or non-significant changes in concentration levels, especially when there are no other alarms such as dominance, entry barriers, low market contestability, etc.

24. On this topic, in Colombia, when parties propose remedies in horizontal mergers, these should eliminate or mitigate the anti-competitive concerns, to the level that they are “tolerable” by the competition authority.

25. Regarding SIC’s analysis, in 2013 the authority issued the “Merger Control Guidelines” (updated once), which contain the main criteria that the SIC considers to evaluate potential vertical/horizontal and unilateral/coordinated effects. This document includes an explanation of the principal alerts that can lead to block a merger or to its conditional clearance, such as high concentration levels, dominance from the merging parties, high entry barriers, buyers power and supply substitutability, among others. The guidelines also contains the list of most commonly used quantitative and qualitative tools in merger analysis.

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<sup>2</sup> The tolerance threshold corresponds to a hypothetical market in which the highest possible HHI after de transaction is 2.500 (below high concentration levels), and less than 20% of increase (index = 1.113). If the transaction yielded a higher index in an isochrone, it was up for divestitures, unless there was a dominant firm, third to the parties.

26. As well, the Merger Control Guidelines indicate the minimum requirements of a remedy proposal from the parties, and, according to the kind of harm, the general SIC considerations regarding the effectiveness of structural and behavioral remedies. For example, in horizontal mergers, the second ones are considered to be less effective to eliminate or mitigate competition concerns.

#### **4. Challenges in remedies design faced by the SIC**

27. In general, it has been particularly challenging for the SIC, designing behavioral remedies, as their effectiveness is difficult to verify. Nevertheless, due to procedure dispositions in competition law, it is easier and less time-consuming to impose penalties to a merged firm that has failed its commitments, than to initiate an antitrust investigation against that firm for antitrust conducts. For that reason, the SIC continues to impose such remedies, regarding non-discriminatory or non-exclusionary treatment that could eventually be sanctioned through an antitrust investigation, but that, in case of occurrence, can be corrected in a shorter period.

28. For reference, a remedy fail can be sanctioned in less than a year, in comparison to an antitrust investigation, that can take more than two years (the legal deadline to handle an investigation is five years).

29. Regarding structural remedies, one of the main challenges that competition authorities face in small economies, such as Colombia, is that a large number of firms have a virtual presence in local markets, as their main assets (if not all) and headquarters are located in other countries.

30. In such cases, if a merger has the potentiality to harm competition, usually no effective local divestitures can be ordered to eliminate or mitigate competition concerns. Alternatively, it is desirable that the parties establish carve outs to ensure the business independence in national markets, but it is usually highly challenging for the authority to verify them.

31. There is also an important challenge that the SIC faces, when a proposed merger involves large foreign companies for which Colombian business is not a significant proportion of their global income, but jointly represent substantial harm for local competition. In such cases, the agency has to consider a tradeoff between blocking the transaction or imposing strict remedies, and facing the fact that due to that decision the parties could just retire from the local market, losing them as effective competitors. Then, the remaining question is ¿what is preferable, a lax clearance of a potential harmful merger, or the withdrawal of the local market by the merged firm.

#### **5. Testing the SIC's approach in courts**

32. Colombian competition law includes the possibility for the parties to seek for a court review, regarding a SIC merger decision. Nevertheless, because of the deadline that the parties usually establish to close the transaction, this option is not commonly exercised, as a court review can take several months, and even years to resolve.

#### **6. Third parties/public opinion**

33. Colombian competition law establishes a 10 day period (labor days), starting with the publication of the notification in the SIC website, to receive comments and relevant information from third parties/public in general, regarding the proposed transaction. This information, if relevant, is included in the SIC analysis.

34. During the same period, any market agent who demonstrates legitimate interest in the outcome of the SIC's decision, can apply to be formally recognized as a third party to the merger. When that condition is granted by the SIC, given the solicitant meets the required legal conditions, it can intervene in any stage of the analysis, including remedies design.

35. Besides the open 10-period, the SIC usually sends information requirements to the principal stakeholders (usually competitors and clients), regarding their opinion about the potential effects of the transaction (among other specific quantitative and qualitative information). Other sector authorities (regulators, ministries, etc.), if any, are also required to cast their opinion regarding the transaction and, when necessary, regarding remedy design.

## **7. Minimizing the risk of ineffective implementation of remedies**

36. Colombian competition law explicitly gives priority to structural remedies in cases of potential undue competition restrictions, as they are thought to be more effective in preserving competition than behavioral ones.

37. In any case, competition law requires the authority to monitor and supervise compliance with imposed remedies, through a time period that is explicitly established in the final decision.