CEDEC

Centro de Estudios de Derecho de la Competencia

"VERTICAL INTRA-BRAND COMPETITION"

The tension created by direct sales

Analysis under Colombian Competition Law

By:

Alfonso Miranda Londoño

Bogotá D.C., March 2013

Calle 72 No. 6-30, piso 12. **PBX (57-1)** 312-2900. **Fax. (57-1)** 310-4715.
Bogotá D.C., Colombia. amirandal62@mac.com

CONTENTS

VERTICAL INTRA-BRAND COMPETITION

The tension created by direct sales

By

Alfonso Miranda Londoño[1]

Summary

This document will discuss the potential antitrust and unfair trade issues that vertical intra-brand competition can create between the producer and its distribution channel, when the producer engages in direct sales. The document takes into consideration these issues under Colombian Competition Law.

The intra-brand competition between a manufacturer that engages in direct sales and its independent distribution channel creates a delicate situation in which the agents or distributors can easily feel that the producer is discriminating against them or that his conduct amounts to unfair trade.

From the perspective of the Colombian competition authority, the vertical relationship between the manufacturer and the distributors raises questions related to vertical agreements, abuse of dominance, unfair trade and merger review.

1. Competition Law in Colombia

Like most countries in Latin America, Colombia issued a first tear of antitrust legislation at the end of the fifties, under the political and academic influence of the U.S. and the European Union[2]. However, competition laws were not applied in this first era, mainly due to the economic protectionist model, which did not favor a competition environment.

[1] Alfonso Miranda Londoño is a lawyer from the Javeriana University Law School in Bogotá, Colombia. He specialized in Socioeconomic Sciences at the same University, in Banking Law at Los Andes University (also in Bogotá) and obtained his Masters Degree in Law (LL.M) from Cornell University (1987). Is the Director of the Law and Economics Department at the Javeriana University Law School, co-founder and Director of the Centre for Studies in Competition Law – CEDEC, and Professor of Competition Law at the Javeriana University. He is the partner that leads the Competition Law practice at *Esguerra Barrera Arriaga.* E-mail: amirandal62@mac.com

[2]

It must be recognized that even though Colombia had a Competition Law since 1959, because of the protectionist economic model widely applied in Latin America, these laws were not really effective until the nineties, post *Washington Consensus*, when Colombia included a principle of Free Competition in Article 333 of the 1991 Constitution[3], changed the economic model in order to open the markets to international trade and issued Decree 2153, 1992 (Decree 2153), which represents a modern approach to Competition Law.

Colombian Competition Laws refer to: **(i)** Antitrust or Competition Protection (as it is called in our legislation); **(ii)** Unfair Competition; **(iii)** Consumer Protection; and **(iv)** Metrology.

Rules on Competition Protection refer to Anticompetitive Agreements; Anticompetitive Acts; Abuse of Dominance and the breach of the Merger Control Regulations.

Also it has to be taken into account, that Competition Protection laws can be divided into the General Competition Protection Regime, applied to all sectors and economic activities not subject to special rules on competition; and the Particular or Special Competition Regimes, comprised of rules issued in special sectors, which characteristics and nature require a specific regulation[4].

Colombian Competition Laws contain a list of specifically prohibited conducts. When a company infringes any of the prohibitions described in Articles 47, 48 or 50 of Decree 2153, the authority will analyze the conduct in a way similar to the *Per Se Rule*[5]. In these cases the main defense for the accused company is to demonstrate that the company did not incur in the alleged conduct. Arguments related to pro competitive effects and other considerations might not be considered.

On the other hand, if the conduct does not fit within any of the specific prohibitions defined in the law, the SIC will investigate the alleged infraction under the general antitrust prohibition contained in Article 1 of Law 155 of 1959 together with article

---

[3] "*Article 333.- Economic activity and private initiative must not be impeded within the limits of the public good. No one may require permits or licenses to exercise economic activity except when authorized by law. Free economic competition is a right of every person, which entails responsibilities. The enterprise, as a basis of development, has a social function that implies obligations. The state will strengthen cooperative organizations and stimulate business development.*
The state, by means of the law, will prevent impediments to or restrictions of economic freedom and will curb or control any abuses caused by individuals or enterprises due to their dominant position in the national marketplace.
The law will limit the scope of economic freedom when the social interest, the environment, and the cultural patrimony of the nation require it."

[4] In Colombia there are special regimes for the Financial and Insurance Sector, Telecommunications, Household Public Utilities, Electric Sector, Health Sector, and Transportation.
[5] Opinion Issued by the Superintendence of Industry and Commerce. File No. 58216, 2000.

46 of Decree 2153, 1992. The authority will analyze the conducts investigated under these provisions in way similar to the *Rule of Reason*. This system of analysis allows the authority to consider the nature, purpose and effect of the conduct, and to balance the anticompetitive and pro-competitive effects of the investigated conduct in the market[6].

In general it can be said that the authority will consider horizontal conduct of greater anticompetitive potential than vertical conduct, and there are some prohibitions that specifically refer to horizontal agreements, like the rule contained in Section 3 of Article 47 of Decree 2153, which creates a *per se* prohibition against horizontal market distribution agreements. This does not mean that vertical market distribution agreements are always legal, but the authority will study them using the *rule of reason.*

2. Analysis of the relationship between a producer that engages in direct sales, and its distribution channel

The situation of a producer that engages in direct sales and at the same time uses an independent distribution channel, raises interesting competition issues and concerns related to the vertical intra-brand competition that this situation creates between the producer and its distribution channel.[7]

The intra-brand competition between a manufacturer that engages in direct sales and its independent distribution channel creates a delicate situation in which the agents or distributors can easily feel that the producer is discriminating against them or that his conduct amounts to unfair trade.

From the perspective of the Colombian competition authority, the vertical relationship between the manufacturer and the distributors raises questions[8] related to unfair trade, vertical agreements, abuse of dominance and merger review.

---

[6] Resolution issued by the Superintendence of Industry and Commerce No. 14540/2002

[7] As The US Supreme Court affirmed in the GTE- Sylvania case, *"The market impact of vertical restrictions is complex because of their potential for a simultaneous reduction of intrabrand competition and stimulation of interbrand competition"*. (Continental T. V., Inc. v. GTE Sylvania Inc., 433 U.S. 36, 1977)

[8] In the Official Journal of the European Communities (2000/C 291/01), there are guidelines for the prevention of vertical restraints: *"103. The negative effects on the market that may result from vertical restraints which EC competition law aims at preventing are the following: (i) foreclosure of other suppliers or other buyers by raising barriers to entry; (ii) reduction of inter-brand competition between the companies operating on a market, including facilitation of collusion amongst suppliers or buyers; by collusion is meant both explicit collusion and tacit collusion (conscious parallel behavior); (iii) reduction of intra-brand competition between distributors of the same brand; (iv) the creation of obstacles to market integration, including, above all, limitations on the freedom of consumers to purchase goods or services in any Member State they may choose."*

2.1 Unfair competition

In a situation like the one described, the producer could use its position to acquire unfair competitive advantages not related to his efficiency, but to the relation with its distributors.

The Colombian Unfair Competition Law, Law 256, 1996 (Law 256) defines several kinds of unfair conducts that could be analyzed in a situation like the one described. [9]

2.1.1 Violation of the general prohibition

Article 7 of Law 256 contains the general prohibition against unfair trade conducts. All participants in the market must always respect the principle of good faith in commerce. It also forbids any act or event entered into with the purpose to compete or participate in the market, when such act is contrary to appropriate commercial practices, the principle of commercial good faith[10], honest practices in industrial and commercial matters; or when it is destined to affect the freedom of the consumer to choose or the competitive function of the market.

In a vertical relationship like the one described, a producer or manufacturer that sells its products through independent distributors and also has its own direct sales infrastructure, could easily design a strategy (conditions, discounts and other commercial measures) in order favor its own direct sales structure, in detriment of its distributors[11]. This kind of strategy may result in a violation of unfair trade and antitrust laws as described herein.

2.1.2 Deviation of Clientele

Article 8 of the UCL prohibits attracting clients from another company using conducts against honest commercial practices. In the case under study, a producer could easily use the information provided by its distributors in order to take away from them their clients using its own direct sales structure. It is important therefore that the parties

[9] In January 24th, 2013, the Superior Tribunal of Bogotá (Bogota's Court of Appeals) issued a decision stating that the decision of a producer to distribute its own products does not go against the principle of good faith. This means that direct distribution should not be considered as an unfair trade act in itself; but it certainly creates conditions that can lead to unfair competition and should be regarded carefully.

[10] According to Resolution 17710/2005, commercial good faith is defined as all the: *"practices adjusted to principles of honesty, trust, loyalty and sincerity that should be followed by merchants in all their acts"*

[11] See Monsanto Co. v. Spray-Rite Svc. Corp., 465 U.S. 752 (1984)

are in agreement as to which information that the distributors must present to the producer is confidential or strategic information which could even be a commercial or industrial secret, case in which it would be forbidden for the producer, under article 16 of Law 256, to divulge such commercial secrets and also to take commercial profit from them.

2.1.3 Induction to contractual default

Under Article 17 of Law 256 it is considered unfair competition to induce workers, clients or other obliged parties to default in their obligations. This prohibition must be considered together with the one included in article 9 of Law 256, against promoting or causing the disorganization of a company. In the case under study the producer has enough information from its distributors and could try to produce any of the mentioned effects[12].

2.1.4 Violation of Laws and Regulations

Under article 18 of Law 256 it is considered that a company engages in unfair competition when it effectively obtains in the market a significant competitive advantage over its competitors by violating a law or regulation. In the case at hand the manufacturer may be accused by the distributor of obtaining a significant advantage through the violation of antitrust laws as will be seen in the following chapter.

2.1.5 Unfair Exclusivity Clauses

Finally, under article 19 of Law 256, it is considered as unfair competition to enter into exclusive dealing clauses in supply contracts, with the purpose or effect of impeding access of the competitors to the market or monopolizing distribution channels. In this case the accusation may not come from the distributor himself who would be a part of the conduct, but from a third party, for example another company who wants to be distributor in the same zone an is excluded from participating in the network.[13]

---

[12] In order to determine whether the conduct falls in this category, there are some elements that should be put into consideration. These are a.)Existence of a contractual relationship between the parties b.) agent's knowledge of the contract termination c.) aimed at the expansion of and industrial sector or the elimination of a competitor and d) the usage of confusion, fraud and/or deceit in order to accomplish it (Case 3129/2012, Superintendence of Industry and Commerce)

[13] The per se rule, only applies to exclusive dealing clauses when their main purpose is to restrict competition. Accessory clauses designed to secure the performance of a distinct principal obligation, should be analyzed under the rule of reason (Resolution 46325/2010 Superintendence of industry and Commerce)

2.2 Anti competitive practices

Conducts such as the ones described above, undertaken by a producer, may not only lead to unfair competition litigation or investigations under Law 256, but may also be sufficient cause for the Superintendence of Industry and Commerce – SIC, to launch administrative investigations for the violation of competition laws.

2.2.1 Violation of the General Prohibition

The described conducts can be investigated in the first place as a violation of the general prohibition against all anti competitive practices contained article 1 of Law 155, in combination with Article 46 of Decree 2153. Such investigations will be conducted by the SIC under the *Rule of Reason* analysis.

2.2.2 Vertical Imposition of Prices

Pursuant to Article 47(1) of Decree 2153, the manufacturer and the distributor could be investigated for vertical price fixing. As in many other jurisdictions, in Colombia, horizontal price fixing agreements represent the most basic infraction to Competition Laws. In that regard, Article 47(1) of Decree 2153 defines as *per se* illegal, all agreements entered into with the purpose or effect of fixing prices directly or indirectly. The law does not distinguish between minimum and maximum prices or between horizontal and vertical price fixing agreements, and it is considered that both kinds are expressly prohibited and therefore *per se* illegal[14].

For that reason, the manufacturer cannot impose or enter into an agreement with its distributors in order to fix the prices at which the distributors will sell the product to the retailers or to the final consumers[15].

It is also important that the distributors or the retailers do not enter into agreements to fix prices on their own, because those horizontal agreements are also regarded as *per se illegal* as said before.

---

[14] Although this is the current Superintendence position, it has been argued that in such case there is not really a price fixing case, mainly because competition laws are designed to prevent such conduct between two products (conversely, in the instant case there is only one product). See Zuleta, Alberto. *"Colombian Regulations on Resale Price Maintenance"*. Competition Law Review No. 7. Volume 7. Bogotá. Pontificia Universidad Javeriana, Law School, Jan-Dec 2011. (Document in Spanish)

[15] In contrast, The US Supreme Court affirmed on the Leegin Creative Leather Products, Inc. v. PSKS, Inc. *et al* Case (2007): *"Notwithstanding the risks of unlawful conduct, it cannot be stated with any degree of confidence that resale price maintenance "always or almost always tend[s] to restrict competition and decrease output."* (…) "*Vertical agreements establishing minimum resale prices can have either pro-competitive or anticompetitive effects, depending upon the circumstances in which they are formed."* In the U.S., these conducts are, thus, analyzed under the *rule of reason*.

2.2.3 Discrimination Agreements

The standard for discrimination in Colombian competition law is drawn from article 13 of the Political Constitution, which guarantees equality under the law. The Colombian Constitutional Court has construed this principle under the Aristotelian concept of distributive justice *"equality for the equals".* Reference to discrimination is found in the list of agreements and conducts of abuse of dominance.

The manufacturer and its distributors have to be careful not to enter into an agreement to discriminate third parties in violation of Article 47(2) of Decree 2153, which specifically prohibits and considers *per se illegal* to enter into agreements with the purpose or effect of establishing conditions of sale or commercialization that are discriminatory to third parties.

As will be seen in this document, apart from this form of discrimination, by agreement against for example, some of the clients of the retailer, it is also possible to enter into discrimination as a form of abuse of dominance.

2.2.4 Vertical Market Distribution

Pursuant to article 47(3) of Decree 2153, it is considered *per se* illegal to enter into horizontal market distribution agreements. Vertical market distribution agreements are not explicitly prohibited by the law, which does not mean that they are always legal. Any such agreements will have to be analyzed using the *Rule of Reason*[16], under the general prohibition contained in Article 1 of Law 155 in combination with Article 46 of Decree 2153, in a way similar to the *Rule of Reason* analysis used by the U.S. Supreme Court in the case of *Continental TV. Vs. GTE Sylvania*[17].

In 1999, the SIC began an investigation against the three soft drinks manufacturers in Colombia: Postobon, Panamco (Coca-Cola) and Bavaria *(Case 19644/2000 – Soft Drinks)*. The SIC accused the producers and their distributors of horizontal and vertical price fixing agreements in violation of Article 47(1) of Decree 2153, and of

---

[16] As a matter of fact, Courts around the world consider the nature, purpose and effects of the conduct, not only in regard to intrabrand competition, but also in regard to interbrand competition. Such is the case of *Monroe Topple & Associates Pty Ltd v The Institute of Chartered Accountants* (06 August 2001), where the Federal Court of Australia affirmed: *"The course of action which ICAA has followed may have had the effect of eliminating or restricting "intrabrand competition", but it may have promoted "interbrand competition".".* In this case, the Court's concern for interbrand competition was more important than the concern for intrabrand competiion.

[17] In this particular case, The US Supreme Court considered that, if there are no vertical restraints, the retail services that enhance interbrand competition might be underprovided. This is because discounting retailers can free ride on retailers who furnish services and then capture some of the increased demand that those services generate.

horizontal and vertical market allocation in violation of Article 47(3) also of Decree 2153.

The investigated companies explained that they had not entered into horizontal or vertical price fixing. They argued that the manufacturers unilaterally imposed to the distributors the price at which they had to sell the product to the retailers. In regard to the market allocation, the manufacturers argued that they did not have a horizontal agreement but that they awarded territories to their distributors in order to reduce costs and increase efficiency in their distribution channel, therefore increasing inter-brand competition in the market. The companies were able to convince the authority that there were no *per se* violations and that under the *Rule of Reason,* their conduct to unilaterally impose prices to their distributors and award territories for logistic purposes had pro-competitive effects and fostered inter-brand competition. The SIC accepted the guarantees offered by the companies and terminated the investigation without sanctions. The SIC accepted the unilateral RPM imposed to the distributors and the vertical market allocation for logistic purposes.

As seen in section 2.1.5, exclusivity clauses between a manufacturer and its distributors can also be investigated as an unfair trade practice under Article 19 of Law 256. According to this article it is considered as unfair competition to enter into exclusive dealing clauses in supply contracts, with the purpose or effect of impeding access of the competitors to the market or monopolizing distribution channels.

2.2.5 Other restrictive Agreements Specifically prohibited by the law

There are however, other restrictive agreements that are specifically prohibited and are considered as *per se* illegal even if they are entered into between a manufacturer and a distributor:

- Agreements entered into with the purpose or effect of assigning production or supply quotas are considered *per se* illegal under Article 47 (4) of Decree 2153.

- Agreements entered into with the purpose or effects of limiting technical developments are considered *per se* illegal under Article 47 (6) of Decree 2153.

- Agreements with the purpose or effect of subordinating the supply of a product to the acceptance of additional obligations that did not naturally belong to the objet of the transaction are considered *per se* illegal under Article 47 (7) of Decree 2153.

- Agreements entered into with the purpose or effect of abstaining to manufacture a product or provide a service or to affect the levels of production, are considered *per se* illegal under Article 47 (8) of Decree 2153.

- Bid rigging agreements in violation of Article 47(9) of Decree 2153.

2.2.6 Anticompetitive acts against the distributor

There has been intense debate in Colombia regarding the legality of unilateral RPM, for Article 9 of Law 155 explicitly allowed manufacturers to set final resale prices to the consumers, case in which the manufacturers, their distributors and independent retailers had an obligation to apply those prices. Also, the former Consumer Protection Statute, Decree 3466, 1982 (Decree 3466) explicitly allowed manufacturers and wholesalers to set resale prices.

Even though article 9 of Law 155 has not been expressly abolished, the SIC, backed by the Council of State, has interpreted that it was tacitly abrogated by the expedition of the 1991 Constitution. On the other hand, Decree 3466 was entirely replaced by the new Consumer Protection Statute, Law 1480, 2011 (Law 1480) and the new law does not refer to RPM.

Finally, Article 48(2) of Decree 2153 prohibits influencing another company to increase its prices or abstain to lower them, and Article 48(3) of Decree 2153 prohibits the conduct of *Unilateral Refusal to Deal* as retaliation to a company's price policies.

In 1999 the SIC decided an investigation (*Case 27263/1999 and 13514/2000, Compañía Colombiana de Medidores Tavira*) against a wholesaler of water measurement equipment. Medidores Tavira was sanctioned by the SIC, for influencing its distributors by forcing them to increase their prices or to withdraw their intentions to reduce their prices. The decision was challenged before the administrative jurisdiction and the Council of State upheld the SIC's decision.

In 2001 the SIC decided an investigation (*Case 8231/2001 and 20229/2001, Casa Luker*) against a Chocolate company. Casa Luker was sanctioned by the SIC, for influencing Makro, one of its distributors, requesting them to maintain the prices of their products, even though the products had been sold by Luker with a 7% discount. Luker was fined by the SIC. The decision was challenged before the administrative jurisdiction and the Council of State upheld the SIC's decision

As can be seen, it is *per se illegal* for the manufacturer and its distributors to enter into vertical agreements to set prices and unilateral RPM is no longer considered as authorized. As a matter of fact, SIC considers that in each level of the production chain there should be an independent decision in regard to prices. Furthermore, it is expressly forbidden to influence a company to increase prices or to abstain from lowering them and the conduct of *Unilateral Refusal to Deal* is also illegal when applied as retaliation to a company's price policies. As a result, it is considered unsafe to enter into unilateral RPM and companies are advised to go as far as suggesting retail prices. For instance, in Colombia, many laboratories advertise in the package of the medicaments a *Maximum Suggested Retail Price,* which is accepted as legal by the SIC.

This analysis shows that the manufacturer should not attempt to agree or impose the prices at which the distributors will sell their products to the retailers or the final consumers; and should never attempt to retaliate against the distributors because of their pricing policies, which should be independent.

2.2.7 Abuse of Dominance of the Manufacturer Against the Distributor

According to Article 45(5) of Decree 2153, 1992 a company enjoys a dominant position when it has the possibility of affecting directly or indirectly the conditions of the market. In order to establish if a company has a dominant position, the SIC will first define the relevant market in its product, geographic and temporal dimensions, using conventional economic tools such as the SSNIP test. Once the relevant market is defined, the SIC will analyze the concentration in the market with the help of concentration indexes such as the HHI, NEE, CR4 and others. The authority will proceed to analyze the barriers to entry and the contestability of the market in order to establish if the accused company enjoys a dominant position.

Article 50(2) prohibits vertical discrimination (exploitative abuses), that is, the application of differential conditions to equivalent transactions in a way in which providers or consumers are put in disadvantageous position as compared with other providers or consumers of similar conditions. Article 50(4) prohibits horizontal discrimination (anti-competitive abuses), that is, the imposition of different purchase conditions to different consumers when done with the purpose of diminishing or eliminating competition.

A distributor may feel that the manufacturer is discriminating against him if the direct sales structure put in place by the manufacturer can offer better price, discount and other conditions to the final consumers in a way that impedes him from competing.

Finally, a distributor may be subject to a *Tying* imposition by a manufacturer with a dominant position. It is considered as an abuse of dominance to subordinate the supply of a product to the acceptance of additional obligations that did not naturally belong to the objet of the transaction, in violation of Article 50(3) of Decree 2153. A distributor may feel that the manufacturer imposes obligations not related to the distribution relationship in order to make him less competitive thus favoring its own direct sales.[18]

[18] So far, in Colombia there has not been a deep discussion on the matter, however, due to the high influence of American antitrust on Colombia we believe that the Jerrold and Jefferson Parish holdings can be of use before the Supertintendence. (See *Jerrold Electronics Corp. V. United States*, 365 U.S. 567 (1961) and *Jefferson Parish Hospital Dist. No. 2 V. Hyde*, 466 U.S. 2, 9 (1984).)

2.3 The Cement Case

As has been explained in some detail, the situation of a producer that engages in direct sales and at the same time uses an independent distribution channel, raises interesting competition issues and concerns related to the vertical intra-brand competition that this situation creates between the producer and its distribution channel.

In 2011 Holcim terminated its relationship with Colcementos, one of its distributors in Medellín (Department of Antioquia), based in the default of Colcementos in the payment of its invoices. Colcementos accused Holcim of abuse of dominance and unfair trade *(Abuse of Dominance Case 56821/2011, 7287/2012. Unfair Competition Case 56823/2011, 7285/2012 – Colcementos v. Holcim)*

The SIC acquitted Holcim in both cases at the level of the preliminary investigation: the one related to abuse of dominance and the one related to unfair competition. In the abuse of dominance case, the SIC concluded that with only 6% of market participation, Holcim's conduct was not significant and had no capacity to affect competition. The SIC took into consideration that Colcementos continued in the market selling other brands of cement.

In the unfair competition case, the SIC stated that the conflict between the parties, more than a conflict of unfair competition was a contractual conflict and if the distributor wished for damages pursuant to the alleged affectation, it should file a contractual liability action. In both cases, the competition authority decided to close the investigation considering that the facts did not constitute a penalized practice.

The SIC stated that considering the cement market is characterized by producer companies having great influence in the markets close to their production plants, given the high costs of transporting their product, it was not economically viable for a company to undertake harmful actions against their distributors considering their distributors could easily market other brands of products.

Regarding the claim of unfair competition, the competition authority stated that Colombian competition law protects rivalry between market agents, that it is normal for an act of competition to lead to client deviation and the subsequent damages for the other competitors, but this may not be penalized. What is prohibited is unfair competition.

If the action undertaken is unfair but it may not be considered to be a competition act, the conduct may not be prohibited by the competition laws, but through other rules such as rules on contractual or tort civil liability.

On the other hand, during the preliminary investigation it was not demonstrated that the cement manufacturer had deviated a relevant number of clients from the distributor and whether the small number that was deviated was caused by an act of unfair competition.

In the opinion of the SIC, for a person's conduct to be penalized and considered to be unfair competition or restrictive of competition, it must reveal:

> "**a. Excluding effect:** The act restricts free participation of persons in the market, with a possible excluding effect, or restricts access to new competitors.
>
> **b. Exploitation effect:** The act significantly increases or consolidates the participation of whoever engages in the same, reaching a position from which it may maximize its profits regardless of its competitors, which constitutes an exploitation placement of its supply, thus obtaining an illegal benefit.
>
> **c. Affect the competitive operation of the market:** If the act promotes carrying out acts of unfair competition or restricts competition, or breaks the correct dynamic of the market and thus distort the economic behavior of competitors, affecting consumers."

2.4 Economic Integration – Merger

Under Colombian Competition Law the relationship between a manufacturer and its distributor can become so intense that it obliterates the business initiative and independence of the distributor in such a way that it can amount to an economic integration that may be subject to merger control under Colombian laws.

If the distribution contract puts the distributor under the control of the manufacturer it may help to disqualify accusations of anticompetitive practices and unfair trade between the manufacturer and the distributor; but it may also create a risk related to compliance with the merger control regulations. Failure to comply with these regulations can lead to investigations and heavy fines.[19]

2.4.1 Definition of Economic Concentration

According to SIC's doctrine, business transaction amounts to an economic integration whenever it allows two (2) or more companies, which previously participated independently in the same market (horizontal effect) or in the same value chain (vertical effect), to act as a single operator on a permanent basis, under the direction of a single management body.[20]

[19] In Colombia control and supervision of vertical mergers is more intensive that the one in the US.
[20] Opinion issued by the Superintendence of Industry and Commerce. File No. 00001365.

2.4.2 Duty to Inform or Notify Mergers

Merger control legislation in Colombia is set forth mainly in Law 155 as modified by Lw1340 and in the regulations from the SIC. Law 1340 substantially changed the characteristics and procedure for merger control.

Article 4 of Law 155, modified by Article 9 of Law 1340, establishes that *"... the companies that are in the same economic activity or participate in the same* value *chain"*, must inform the SIC the proposed operation, *"... that they intend to undertake in order to merge, consolidate acquire control or enter into an economic integration,"* as long as they fulfill the following requirements:

1) That the companies, individually or jointly have an operational income, in the fiscal year prior to the projected operation, worldwide, above the amount established in minimal monthly legal salaries, by the Superintendence of industry and Commerce.[21]

2) That the companies, individually or jointly, by the end of the fiscal year prior to the projected operation owned total assets worldwide, in excess of the amount established in minimal monthly legal salaries, by the Superintendence of Industry and Commerce.[22]

According to article 9 of Law 1340, it is possible to **notify** the merger transactions when the described economic thresholds are meet, but do not have an individual or joint participation in the relevant market of 20% or more. **Notification** is a short form procedure with no waiting period. The transaction is effectively immediately.

If any of the above economic thresholds are met, and the participation in the relevant market is superior to the 20%, Article 10 of Law 1340 of 2009 provides that the interested companies must **inform** the SIC by submitting pre – evaluation request of the proposed operation. **Information** is a long form procedure with a waiting period. The transaction can only be made effective after receiving clearance from the competition authority.

Finally, when the transaction is held between companies that belong to the same economic group, it does not have to comply with the merger control regulations.

---

[21] At present, one hundred thousand (100,000) minimal monthly legal wages, as enacted by SIC's Resolution.
[22] At present, one hundred thousand (100,000) minimal monthly legal wages, as enacted by SIC's Resolution.

As can be seen, the relationship between a manufacturer and a distributor, depending on the level of intervention agreed of the business of the distributor by the manufacturer, can be construed as an economic integration, subject to merger review. This can become a form of protection from antitrust or unfair competition investigations and lawsuits, but also creates a risk if the companies fail to **notify** or **inform** the transaction to the SIC, depending on the characteristics of the transaction.

3. PROCEDURE

Pursuant to Article 6 of Law 1340, the SIC has been granted exclusive powers to conduct administrative investigations for the Infraction of the Competition Protection and Unfair Competition Laws. It must be remembered that Competition Protection includes the rules on merger control.

In an administrative investigation, by definition, the authority can act pursuant to an accusation filed by any person, or officiously.

As said before, the SIC can declare the violation of competition laws, order the investigated companies to cease in their illegal conduct, and impose fines both to the companies and the natural persons involved.

One of the improvements of Law 1340 was the notorious increase in the capacity of the SIC to impose fines. Under Decree 2153 the maximum fine could go up to 2000 minimum monthly wages (around USD $500.000) to the companies and 300 minimum monthly wages (around USD $70.000) for the natural persons involved; whereas now, under law 1340 the SIC can impose the companies up to 100.000 minimum monthly wages (around USD $30’000.000) or up to 150% of the profits obtained with the anti competitive conduct, and up to 2000 minimum monthly wages (around USD $500.000) to the natural persons involved. There is an important addition in regard to the express prohibition to the investigated companies to pay for the fines imposed to the natural persons.

It must be noted that the SIC can impose fines for anti competitive conduct, but also for the obstruction of investigations; infringement of the merger control regulations; failure to comply with orders; failure to comply with obligations acquired pursuant to guarantees accepted for the anticipated termination of investigations or the conditions accepted for the approval of a merger transaction. There are also circumstances that allow the authority to impose harder or softer sanctions depending on different factors.

4. CONCLUSIONS AND PRECAUTIONS

The analysis in this document shows that the relationship between a manufacturer and its distributors can become tense and full of gray zones when the manufacturer engages in direct sales. Some of the precautions that a manufacturer may take in order to mitigate the risks associated to vertical intra-brand competition, are the following:

4.1 In general terms, the manufacturer should give its direct sales area and its distributors an equal and non-discrimination treatment in order to reduce the probability that the distributors feel that the manufacturer is biased to favor its direct sales area and give it a competitive advantage that will be perceived as an anti competitive practice or unfair competition.

4.2 In this sense, the manufacturer should grant its distributors access to the same information, types of discounts and commercial treatment it gives to its own direct sales area. Such employees must have access to information of the same level and quality than that available to distributors and no strategic and detailed information of the operation of the distributors should be provided to them in order to avoid risks of unfair competition and competition restrictive practices.

4.3 If the manufacturer's employees in charge of direct sales have access to sensitive and strategic information that independent distributors must provide to the manufacturer in order for the latter to monitor their activity, such information on prices, units sold, clients, promotional activities, discounts, etc., may be used by the direct sales area to obtain a competitive advantage before dealers or behaviors that could be construed as restrictive or unfair by dealers and by the authority.

4.4 For that reason the manufacturer must if possible, separate the direct sales persons from the information related to the distribution network. If this is not possible, it should instruct its employees in charge of the directs sales area not to use for commercial purposes sensible information provided by the distributors in their normal reports.

4.5 The manufacturer should design a series of measures to protect free and loyal competition tending to guarantee to independent dealers or agents that the company will not grant anti-competitive advantages to the internal direct sales area.

4.6 These measures shall tend to guarantee independence in decision-making and information management among persons who handle direct sales and those who handle relations with dealers or agents. For this we recommend **(i)** dealing with different persons; and **(ii)** that those persons sign a "Chinese Wall"-style confidentiality agreement in order to guarantee that sensitive, strategic and competitive information remains independent.

5. TABLE OF AUTHORITIES

5.1 Statutes

- Political Constitution, Article 333
- Law 155, 1959
- Decree 3466, 1982
- Decree 2153, 1992
- Law 256, 1996
- Law 1340, 2009
- Law 1480, 2011

5.2 Cases

- *Case 19644/2000 – Soft Drinks*
- *Continental TV. Vs. GTE Sylvania*
- *Case 27263/1999 and 13514/2000, Compañía Colombiana de Medidores Tavira*
- *Case 8231/2001 and 20229/2001, Casa Luker*
- *Abuse of Dominance Case 56821/2011, 7287/2012. Unfair Competition Case 56823/2011, 7285/2012 – Colcementos v. Holcim*