The Ecuadorian Agency Announces a Fast-Track Merger Proceeding

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On April 20, 2020, the Ecuadorian competition agency (*Superintendencia de Control del Poder de Mercado – SCPM*) published a Resolution[2] enacting Ecuador's first fast-track procedure for merger control. This is a welcome change that has been long requested by undertakings and practitioners. It should substantially shorten the long review periods[3] that even trivial transactions used to face and allow the agency to better prioritize its resources.

The Resolution includes a bit of everything. Besides creating the fast-track proceeding, it announces some exceptions for filings and merger reviews during the COVID-19 pandemic, and fleshes out the, until now, very abstract and confusing failing-firm defense. In this short note we will first address the more straightforward issues regarding filing during the COVID-19 emergency, and then reflect upon the most controversial aspects of the new failing-firm rules.

I. Merger Filings in Ecuador During the Pandemic

After initially suspending all new, pending and under-review merger filings,[4] the SCPM reversed its course. Several companies complained to the agency that they were finalizing negotiations of transactions that had to be notified, and that the suspension forced them to wait until the emergency was lifted just to begin the 5 to 6-month review period. It is reasonable to assume that some of them decided to close transactions without notifying and assume the risk of a possible gun-jumping investigation.

Consequently, the agency adopted a sensible solution. It reinstated merger procedures with some caveats and exceptions. First, the clock will start again for transactions that have been under review and where the agency has enough information to produce its report. Second, the 8-day rule is again in force. This rule requires all transactions to be notified within 8 calendar days of "conclusion."[5] In recent years, the agency has uniformly interpreted "conclusion" to mean the execution of the document from which the concentration arises, although there is some leeway to use a binding version of some preliminary document -such as a LOI or a MOU- if the parties wish to begin the procedure earlier.

Once notified, and until the health emergency is formally lifted by the Executive,[6] the agency can take three courses of action:

1. First, begin its regular review only when the agency has up-to-date information (corresponding to at least 2018 and 2019) allowing it to properly define the relevant market and the main competitive constraints without having to request information from any third party. This will most likely occur if the agency has recently reviewed other transactions in the same relevant market.

2. Second, begin its review if the transaction falls under any of the categories allowing it to benefit from the fast-track procedure. The categories are the following:

   2.1 **First landing.** If the firm acquiring control does not directly or indirectly conduct business in Ecuador. "Indirect" activity is defined as any sale or service rendered through any subsidiary of the economic group. Consequently, the sale of products through an independent distributor does not constitute indirect activity and thus may benefit from expedited review.

2.2 **Market share.** The parties' joint share in each of the relevant markets, both in horizontal and vertical mergers, must be less than 30 percent. This exception was created for economic groups with large sales that trigger the turnover threshold, but which have marginal activity in the affected relevant markets.

2.3 **Market concentration I.** Horizontal mergers where the affected relevant markets have a pre-merger HHI of 2000 points or less and the post-merger delta is less than 250 points.

2.4 **Market concentration II.** For vertical mergers where the affected relevant markets have a pre-merger HHI of 2000 points or less.

2.5 **Failing firms.** The agency incorporated a three-limbed test inspired by the EU Guidelines, with some variations that may have substantial consequences. The test comprises the following elements:

2.5.1 Undertakings that are unable to meet their financial obligations in the near future.

2.5.2 Potentially less restrictive alternatives. This limb imposes a high evidentiary threshold: proof that all efforts have been made to find the least restrictive alternative.

2.5.3 Absent the merger, the target company would exit the market.

3. If the merger does not meet any of these two exceptions, the notifying party must still submit all documents within 8 days of the conclusion of the agreement, but the review period will only begin once the emergency ends.

Finally, even though all transactions that fall within the exceptions will move forward, the agency has announced it will prioritize all cases related to the food industry and associated markets, pharma and medical supplies, cleaning and disinfectant products, and tourism and associated industries.

II. Failing Firm Defense in Ecuador

Finally, we want to briefly reflect on the new failing firm defense rules. Even though the Resolution seems to have adopted run-of-the-mill standards, the wording of some of the tests and the regulations may change more than meets the eye.

Prior to the enactment of the Resolution, Article 13(b) of the regulations was the only reference in the Ecuadorian system to the possibility of arguing a failing firm (the agency did not adopt any other or more orthodox standards through caselaw, either). The wording of the article was confusing, requiring the decision to be mandated by a public authority (without explaining which) in accordance with laws and regulations related to liquidation, bankruptcy, insolvency, suspension of payments, agreement with creditors or other similar procedures.

Now the Resolution has made clear that the competition agency is the public authority that must admit a failing firm defense. However, the second part of the article has not yet been clarified., Nonetheless, it seems the regulation requires the agency to analyze the first limb of the test (unable to meet their financial obligations in the near future) according to Ecuadorian law pertaining to bankruptcy and restructuring. Bankruptcy law is not well developed in

Ecuador, some of the requirements are too stringent, and there are different options for restructurating under different laws (for example, if an undertaking is covered by the recent entrepreneurship law).[7] Consequently, the regulations may have incorporated a body of law that leaves several open questions, and that may force the agency to take conservative positions in order to avoid any conflicting decisions with either judges or other administrative authorities in charge of bankruptcies and restructuring.

The second limb of the test is also problematic. The text of the Resolution requires proof that all *possible efforts* were made to sell the company or its assets to *the* least restrictive option. A literal interpretation will always require considering selling the company or its assets to a new entrant, which may too stringent.

The third limb does not adopt the counterfactual of the "assets" leaving the market, but rather of the whole company doing so. We don't see this as a substantial problem, as long as the agency does not interpret it to require proof of the "market share absorption" standard that, as the EU has shown, is too strict.[8]

However, all these possibilities are constrained by the requirement that the agency has decided to review all failing firm arguments within its fast-track process. This means that a decision will have to be made, on average, within two months of filing. This timeframe may prove too short to assess nuanced, difficult and very evidence-dependent cases such as filings by failing firms. Unfortunately, this procedural decision may rush a review that, in order to avoid type II errors (as the Ecuadorian system is designed to do),[9] will result in very few successful cases in an area of law that is already seldomly applied.

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[2] Superintendency of Market Power Control. Resolution No. SCPM-DS-2020-19 and No. SCPM-DS-2020-18. April 20, 2020.

[3] Before the fast-track procedure, the review period of a merger under Ecuadorian law ranged from 4 to 7 months on average.

[4] Superintendency of Market Power Control. Resolution No. SCPM-DS-2020-14. March 16, 2020.

[5] Filing must be done through the following email: recepcion.documentos@scpm.gob.ec.

[6] Executive order No. 1017. March 16, 2020.

[7]. Entrepreneurship and Innovation Organic Law. Official Record No. 151. February 28, 2020.

[8] Case IV/M308 *Kali und Salz/MdK/Treuhand*. OJ 1994 L186/30.

[9] As an example, even though the law does not allow the agency to consider possible conglomerate effects when assessing a transaction, there is still an obligation to file mergers where no horizontal or vertical overlaps or integrations are expected.