

An Investigation on Barriers to Competition and Essential Supplies In Mexico's Federal Economic Competition Law

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The 2014 Reforms to Mexico's Federal Economic Competition Law (Ley Federal de Competencia Económica, LFCE) include a new procedure for investigating barriers to competition and essential supplies. This mechanism for market research is similar to those famously used by the United Kingdom's competition regulators.

This type of anti-competitive conduct is clearly distinct from the Monopolistic Practices analysis originally prescribed by the previous version of the law, and which is now included in Article 53, regarding Absolute Monopolistic Practices, as well as Articles 54 to 56, which discuss Relative Monopolistic Practices.

Specifically, Chapter IV of the second volume on Anticompetitive Conduct, entitled "On the Prohibition of Barriers to Free Association and Competition" contains a single article:

Article 57 IV. The Commission will provide what is needed to prevent and eliminate barriers to free association and economic competition, in the appropriate amount needed to eliminate anticompetitive effects through the procedures contained in this Law.

Article 57 doesn't mention any specific prohibition, but states only that the Commission will "provide what is needed" regarding barriers with "anticompetitive effects". This way the Law anticipates possible situations where structural, strategic or regulatory issues may cause problems for proper competition and free association.

Later, in chapter I of volume four, "Special Procedures", articles 94 and 95 refer to investigations used to determine Essential Supplies and Barriers to Competition. We must point out the introduction to Article 94:

Article 94. The Commission will begin investigation procedures, on its own or upon request by the Federal Executive itself or through a Secretariat, whenever there are elements that may suggest a lack of conditions needed for an effective competition within a market, and in order to determine the existence of barriers to competition, free association or essential supplies which could have anticompetitive effects.

The methodology and the damage criteria applied to these investigations in the UK are important points of reference for these procedures and for the application of remedies to these situations.

Following the logic of Britain's regulator, an investigation (and possible intervention) should be motivated centrally by the adverse effect on competition.

The introduction to Article 94 reflects this effect by establishing that investigations should take place "*when there are elements that may suggest a lack of conditions for effective competition within a market*". The lack of favorable conditions is easily distinguished from a procedure that tries to formally resolve effective competition issues, dealt with in Article 96.

There are two assumptions or types which determine the 'non-existence' of effective competition within a market. According to Art. 94: "*the existence of barriers to competition and free association or Essential Supplies that may have anticompetitive effects.*" The question here is what kind of obstacles can exist within a market – different from conducts that violate the basic tenets of free competition (absolute or *per se*), or displacement actions that require a Reasonableness test (relative) – which could justify the agency's intervention. From our point of view, COFECE's mandate is to watch over free association and competition, and to persecute and eliminate restrictions that hamper the efficient working of the Market (Article 2, LFCE).

If we only focus on barriers we may notice that, from an economic standpoint, the Law considers conducts that result from cooperative oligopolies (absolute monopolistic practices) and monopolies formed by dominant firms along with a slew of smaller competitors known as "Fringe firms" (relative monopolistic practices) as violations.

The law does not include sanctions for cases where the market efficiency is hampered by the presence of structural elements derived from different conditions of supply and demand or the predominant technology in the industry, such as economies of scale or network effects. Neither does it sanction the presence of strategic elements derived from non-cooperative oligopolies, such as when different agents find natural niches or where there are conscious parallelisms, nor when cooperative oligopolies engage in agreements that do not qualify as cartels, or cooperation between competitors that can be distinguished from cartel formation when reviewed under the scope of Rule of Reason. These situation, analyzed from a structural standpoint – with few participants – or an incentives standpoint – where there is strategic accommodation – are ideal starting points for market investigations or analyzing barriers to competition.

In cases involving Essential Supplies, it's clear that the Law has a very particular role in mind for the Federal Telecommunications Institute (Instituto Federal de Telecomunicaciones, IFT) – since COFECE is not, and should not become, a Sector regulator – and that the remedies prescribed will mostly involve their regulatory branch. We need only read Article 94 fraction VII, section c) to illustrate the point.

Art. 94 VII. “...

The Commission's resolution may include:

...

*c) A determination on the existence of Essential Supplies and guidelines to regulate, when needed, **the forms of access, prices or tariffs, technical and quality requirements, as well as a timetable for their application, or...***

The Law also establishes as a necessary condition for one or several agents with substantial market power to be accused of the negative conduct – in the case of relative monopolistic practices – or an agent that controls the Essential Supplies – in cases defined by Article 94 – in order to determine the existence of said conduct and apply the appropriate sanctions, whether regarded as an anticompetitive conduct or as harmful to effective market competition. This requirement does not apply to barriers to competition, as previously discussed.

Based on this description, although the procedures used to determine each element – barriers to competition or Essential Supplies – and the effects they cause (harming competition) are the same, the methodology and the logic of anticompetitive damages (harm theory) as well as the remedies proposed to alleviate these damages are not necessarily similar.¹

This is markedly different from what we find in Article 60, where supplies are anything (goods or services) that is controlled by one or more Economic Agents with substantial market share (which may be considered as aggregate market share) or who have been “determined to be Dominant by the Federal Telecommunications Institute [IFT]”.

One advantage of implementing this interpretation of barriers as regulation is that their analysis and determinations closely track economic theory. In other words the analysis of industries with ‘stranded costs’, economies of scale, network externalities, non-cooperative oligopolies and cooperative oligopolies distinct from those covered by the absolute

¹ We should point out that the 2014 reform included, among other things, the addition of 2 new conducts classified as Relative Monopolistic Practices – Fraction XII on the Negation of supplying an Essential Supply; and Fraction XIII on the tightening of margins at the final stage of production when it involves the End Consumer. This is why it was necessary to add an article that specifies how an Essential Supply should be identified (Article 60).

monopolistic practices classification, is relevant and appropriate for this kind of investigation.

If we consider barriers to competition as mostly comprising technological barriers or those imposed by demand, as well as implicit collusion conducts or non-cooperative, accommodating oligopolies, it stands to reason that the preferred remedies will not involve sanctions on a single act, but rather actions which address a host of principles and recommendations that may help lift these barriers or to change the rules that guide the market players' behavior. Whether these are orders to perform or to cease certain actions, behavioral guidelines (known as "soft laws") for the market under investigation –for example, the codes of conduct imposed by the United Kingdom's competition authority on the country's supermarkets– and finally, by drastically changing the rules of the market by modifying its structure.

We believe that the latter type of remedy is supported by Article 94, Fraction VII section b) in 2014's LFCE. It is not necessary for a lack of effective competition within a market to be determined as the result of an essential supply or that the only way to implement changes to the market is to act through regulation This would turn the Competition Authority into a Sector Regulator for every market it became involved with. As mentioned before, it would seem that this paragraph, along with fraction VII section c), was intended for the IFT, not for COFECE.