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Mexico's Proposed Reform of Competition Law: A Critique from Europe

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I. INTRODUCTION

Legislative innovations in the competition law area may be based on good intentions but it is always a good idea to run a sanity check and refer back to fundamental principles of sound competition policy. On February 19, 2014, the Secretaría de Economía within the Federal Executive Branch proposed rather sweeping amendments to the Mexican Competition Act (the "Law Proposal"), which include a number of problematic elements. Most alarmingly, the Law Proposal refers to a newly introduced concept of "barriers to competition" and would make it a violation of competition law to create a "barrier to competition."

In our short article, we draw on our academic and professional expertise in the area of competition law, economics, and policy and on our experience as former enforcers. We also draw on experience from our participation in international forums of competition law enforcement agencies, such as the Competition Committee of the Organisation for Economic Cooperation and Development ("OECD"), the International Competition Network ("ICN"), and the United Nations Conference on Trade and Development ("UNCTAD").

We believe that merger control and standard antitrust rules give competition authorities a set of efficient and secure tools to guarantee the well-functioning of markets for which competition is the normal way to operate. The implementation of these policy interventions relies on a set of definitions, methods, and tools shared by most competition authorities around the world. This framework allows, on the one hand, for a full understanding by firms of the risks associated with anticompetitive behavior and, on the other hand, limits both the risks of "false negatives" and "false positives" by competition authorities. It also ensures that firms understand the level-playing field in which they operate and guarantees that their investments will not be confiscated.

A legal framework that would introduce a new and vague additional source of intervention by competition authorities would destroy this legal framework and lead to a high degree of uncertainty. In particular, the risk of divestiture of assets resulting from so-called "barriers to competition" would place a high burden on firms and would hamper their willingness to innovate and invest, leading finally to a less competitive economy.

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II. THE MEXICAN LEGISLATIVE PROPOSALS ON THE CONCEPT OF "BARRIERS TO COMPETITION"

We understand that a new Competition Bill is currently pending before the Mexican legislature. The proposed text includes a number of provisions that are rather familiar to competition law experts. In particular, there are provisions on anticompetitive agreements (Article 53 on "Absolute Monopolistic Practices"), unilateral conduct of dominant companies (Article 54 on "Relative Monopolistic Practices"), and merger control (Article 61 *et seq*. on "Concentrations").

However, the Law Proposal also includes a number of alarmingly novel provisions, concepts, and procedures, which seriously depart from mainstream competition law and economics and which go as far as being incompatible with the most fundamental notions of competition law enforcement. These provisions center on the introduction of a nebulous concept of "barriers to competition," which, as such, is not met in any other mainstream competition law enforcement system, to the best of our knowledge.

In particular, the following provisions of the Law Proposal are most relevant:

- Article 52 of the Law Proposal stipulates that "barriers that, according to this law, limit, damage or prevent free participation or economic competition in the production, processing, distribution or commercialization of goods or services are prohibited."
- According to Article 55, practices associated with such "barriers to competition" "shall be considered unlawful and be punished."
- According to Article 57 of the Law Proposal, "the Commission shall establish what is essential in order to prevent and eliminate any barriers to free participation and economic competition using the procedures set forth by this law."
- Article 94 of the Law Proposal appears to provide authority to determine whether "there are elements which determine the existence of barriers for free competition" and, if so, to order "corrective measures deemed necessary" for the purpose of "eliminating restrictions for the efficient operation of the market in question."
- According to the Law Proposal, "the measures may include the elimination of barriers to free competition, regulation of essential inputs or divestiture of assets, rights, partnership interests or shares of the Economic Agents in the proportion required to eliminate anti-competitive practices detected by the Commission. The measures concerning the existence of an Essential Input shall include mode of access to it, price or tariff controls, technical and quality conditions and time schedules."

III. ANALYSIS OF THE PROPOSED PROVISIONS IN LIGHT OF BASIC COMPETITION LAW PRINCIPLES

Based on our review of the proposed legislation, we believe that the novel concept of "barriers to competition" could be used by the competition authority in two distinct but also interlinked ways:

First, it appears from Articles 52, 55, and 57 of the Law Proposal that a new kind of competition law violation is introduced, not recognized in competition regimes elsewhere, the erection of "barriers to competition." The text is not particularly clear as to whether this constitutes a self-standing third basic violation of competition law, apart from anticompetitive agreements (Article 53) and monopolization or abuse of market power (Article 54), or whether it is a specific practice that the law would consider as an example of an anticompetitive agreement (if pursued in an agreement put in effect by a number of firms) or of monopolization (if pursued unilaterally by a firm or firms holding market power).

However this concept functions, it would give rise to a competition law violation that would be unlawful and punishable by the authority through monetary sanctions and through the imposition of injunctive measures. In this sense, to the best of our knowledge, this would be a unique violation of competition law that is not present in other mainstream competition law systems. It is certainly not recognized in U.S. antitrust law or EU competition law, and we believe no similar provision exists in the national competition laws of the EU Member States or in the competition statutes of other major countries. This should not come as a surprise, since, as we explain below, there are valid legal, economic, and policy arguments against this flawed concept.

Second, it seems that Article 94 of the Law Proposal aspires to introduce into Mexican competition law a system of market investigation, where there has been no unlawful conduct by firms (in the form of anticompetitive agreement or monopolization). Yet, the authority would intervene to deal with what it perceives as "existence of barriers for free competition or of essential inputs which require to be regulated because they affect the process of free competition."

Such an enforcement mechanism is again unique. There are maybe a handful of jurisdictions, most notably the United Kingdom, Greece, and Israel, which include the market investigation mechanism in their competition law enforcement systems (which one of the authors of this paper is intimately familiar as a former Commissioner). Such market investigations, in other words, can be undertaken when there is a competition problem that is not caused by a competition law violation. The authority may intervene against a certain market structure or sometimes a "market failure" and this may, indeed, lead to regulatory measures. However, the Mexican proposals are different in nature from these models and are built around the nebulous concept of "barriers to competition," contrary to the above models.

The market investigation tool, as we know it from the above three jurisdictions, is a rather controversial way to intervene in a market and there are valid criticisms that can be launched against it, as we develop below. However, it is important to note that Article 94 of the Law Proposal is far more deserving of criticism, because it differs fundamentally even from the U.K., Greek, and Israeli systems and likely would lead to flawed outcomes that are detrimental to competition and consumer welfare.

A. "Barriers to Competition" as a Violation of Competition Law

In their current form, Articles 52, 55, and 57 of the Law Proposal appear to introduce a new kind of competition law violation, the erection of "barriers to competition." This is an unfortunate and flawed concept.

The very notion of "barriers to competition" is not a term or concept that is met in recognized competition theory, legislation, or case law elsewhere. It is a descriptive term that may have a very generic and imprecise meaning. Anticompetitive practices may result in creating "barriers to competition," but a "barrier to competition" by itself does not indicate there in fact exists any anticompetitive behavior. Besides, there are already means to fight barriers to entry when these barriers result either from unilateral monopolistic conduct or from collusive behavior. Mexican law currently in force, like other competition laws, has such means readily available. In addition, merger control allows competition authorities to assess the dangers of more concentrated market structures that can result from external growth. Indeed, in the context of merger control, competition authorities can impose structural remedies in order to correct the potential anticompetitive effects of a contemplated merger.

Various competition laws, following basic economic principles, refer to "barriers to entry," which is a different and precise concept. Entry barriers are factors that prevent or hinder companies from entering a specific market. They may result, for instance, from a particular market structure (for example, sunk cost industry, brand loyalty of consumers to existing products, the need for distribution systems, the costly establishment of a reputation) or the behavior of incumbent firms. Government policies can also be a source of entry barriers (such as through licensing requirements and other regulations).[2]

However, these factors are seen neutrally by competition laws. Their existence is only useful to define the product and geographic market or to assess market power or dominance on a properly defined market; the identification of entry barriers is not used to establish an infringement of competition rules. Indeed, the existence or erection of barriers to entry, as such, is not considered unlawful by the laws of other countries.

We understand that the concept "barriers to competition" is not meant as "barriers to entry" by the Law Proposal; nevertheless, the use of the former term creates confusion because it resembles the latter term. Certainly, any theory which would make the existence or even erection of barriers to entry a violation of competition law would be fundamentally flawed and at variance with mainstream competition laws and basic economic principles. Barriers to entry cannot by themselves constitute an abuse of dominance or market power.

The apparent introduction of the concept of infringement based upon the existence of "barriers to competition" in Article 52, especially when combined with the other related provisions recited above, raises a related concern that efficient companies may be penalized for striving and succeeding in growing their market share through perfectly acceptable and desired conduct. More generally, a company's possession of a high market share is not unlawful in either the United States or the European Union or, indeed, in other competition law systems. Competition law encourages companies to grow their market shares through more efficient operations, investment, and innovation, and other pro-competitive behavior. Under EU competition law, other European competition laws, U.S. law and other leading economies' competition laws, a firm's dominant position is not, in itself, prohibited and cannot constitute a competition law violation. Instead, an abuse of dominance can only be established through evidence of exclusionary or exploitative conduct.

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[2] European Commission, Directorate-General for Competition, *Glossary of Terms Used in EU Competition Policy*, *Antitrust and Control of Concentrations*, Brussels, p. 17 (July 2002).

Thus, to punish a firm and force divestitures, the authorities must prove more: A company's status and its conduct are not unlawful if there is no finding that the company engaged in some kind of exclusionary, exploitative, or otherwise harmful conduct that is punishable under competition rules. A finding of high market shares, high concentration, barriers to entry, or, indeed, "barriers to competition" is not enough. High market shares as such do not even themselves indicate whether a firm has market power.[3]

A recent judgment of the Grand Chamber of the European Court of Justice makes some important general pronouncements on the role of dominance and on the intervention of competition law, which, we believe, deserve the attention of the Mexican law makers:

> It is settled case-law that **a finding that an undertaking has such a dominant position is not in itself a ground of criticism of the undertaking concerned** (Case 322/81 Nederlandsche Banden-Industrie-Michelin v Commission [1983] ECR 3461, paragraph 57, and Joined Cases C-395/96 P and C-396/96 P Compagnie maritime belge transports and Others v Commission [2000] ECR I-1365, paragraph 37). **It is in no way the purpose of Article [102] to prevent an undertaking from acquiring, on its own merits, the dominant position on a market** (see, inter alia, TeliaSonera Sverige, paragraph 24). **Nor does that provision seek to ensure that competitors less efficient than the undertaking with the dominant position should remain on the market.**
>
> Thus, **not every exclusionary effect is necessarily detrimental to competition** (see, by analogy, TeliaSonera Sverige, paragraph 43). **Competition on the merits may, by definition, lead to the departure from the market or the marginalisation of competitors that are less efficient and so less attractive to consumers from the point of view of, among other things, price, choice, quality or innovation.**
>
> According to equally settled case-law, a dominant undertaking has a special responsibility not to allow its behaviour to impair genuine, undistorted competition on the internal market (Case C-202/07 P France Telecom v Commission [2009] ECR I-2369, paragraph 105 and case-law cited). When the existence of a dominant position has its origins in a former legal monopoly, that fact has to be taken into account.
>
> In that regard, it is also to be borne in mind that Article [102] applies, in particular, to the conduct of a dominant undertaking that, **through recourse to methods different from those governing normal competition on the basis of the performance of commercial operators**, has the effect, **to the detriment of consumers**, of hindering the maintenance of the degree of competition existing in the market or the growth of that competition (see, to that effect, AKZO v Commission, paragraph 69; France Télécom v Commission, paragraphs 104 and 105; and Case C-280/08 P Deutsche Telekom v Commission [2010] ECR I-9555, paragraphs 174, 176 and 180 and case-law cited)."[4]

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[3] *See* Louis Kaplow, *Market Share Thresholds: On the Conflation of Empirical Assessments and Legal Policy Judgments*, Harvard John M. Olin Center for Law, Economics, and Business, Discussion Paper No. 692 pp. 9-10 (May 2011).

[4] Case C-209/10, *Post Danmark A/S v Konkurrencerådet*, Judgment of 27 March 2012, ¶¶ 21-24 (emphasis added).

As a general principle, competition laws and competition law enforcement should always strive to protect competition and consumer welfare, not individual competitors who do not deliver to consumers. Rivals may be less successful for other reasons, as well; for example, they may not invest in their companies or in innovation to the same extent, or they may simply be less efficient. Competition law should not encourage such firms. Legal rules and provisions that facilitate a redistribution of assets (such as in a divestiture order) or that force access to inputs developed by a dominant competitor are likely to encourage economic free-riding and discourage the very investment Mexican policy makers should want to foster.

Also, dominant companies should be free to compete aggressively as long as this competition is ultimately for the benefit of consumers.[5] So-called "competition on the merits" has beneficial effects for consumers and should therefore be promoted. Competition does not only allow consumers to obtain a broader supply and lower prices, it also leads to a selection of efficient firms by market mechanisms: this mechanism drives out of the market only those firms that are not efficient enough to sustain competition on the merits. Therefore, an inadequate intervention in this natural mechanism, like the divestiture of firms who gained market share due to their higher efficiency, would deprive consumers of the main and long-term benefits of competition.

This means that a company that competes successfully on the market may acquire a number of advantages vis-à-vis its competitors, such as a more efficient distribution network, a paramount brand, access to a technology that was developed with considerable effort and investment, and other assets or inputs that its competitors would desire or envy. However, it would be flawed if a law that prohibits "barriers to competition" (which is a very vague concept itself) gave the competition authority the power to order firms to divest assets or technology. This would give adverse incentives to firms to engage in a vigorous competition on the merits, since the benefits of a growing activity would be confiscated.

In addition, the simple threat of being subject to such a divesture makes investment more risky and should further discourage investment, competition on the merits, and innovation. It would ultimately be also a factor dissuading potential investors to enter the Mexican market.

These detrimental effects to consumer welfare, competition, and the economy were aptly described by Advocate General Jacobs, one of the most eminent Advocates General at the European Court of Justice, in his celebrated Opinion in *Bronner*:

> First, it is apparent that the **right to choose one's trading partners and freely to dispose of one's property** are generally recognised principles in the laws of the Member States, in some cases with constitutional status. Incursions on those rights require careful justification.
>
> Secondly, the justification in terms of competition policy for interfering with a dominant undertaking's freedom to contract often requires a careful balancing of conflicting considerations. In the long term **it is generally pro-competitive and in the interest of consumers to allow a company to retain for its own use facilities which it has developed for the purpose of its business. For example, if**

[5] *See, e.g.*, European Commission, Directorate-General for Competition, MEMO/08/761, Brussels, 3 December 2008.

> **access to a production, purchasing or distribution facility were allowed too easily there would be no incentive for a competitor to develop competing facilities. Thus while competition was increased in the short term it would be reduced in the long term. Moreover, the incentive for a dominant undertaking to invest in efficient facilities would be reduced if its competitors were, upon request, able to share the benefits. Thus the mere fact that by retaining a facility for its own use a dominant undertaking retains an advantage over a competitor cannot justify requiring access to it.**
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> Thirdly, in assessing this issue it is important not to lose sight of the fact that the primary purpose of Article [102] is to prevent distortion of competition—and in particular to safeguard the interests of consumers—**rather than to protect the position of particular competitors.** It may therefore, for example, be **unsatisfactory**, in a case in which a competitor demands access to a raw material in order to be able to compete with the dominant undertaking on a downstream market in a final product, to focus solely on the latter's market power on the upstream market and conclude that its conduct in reserving to itself the downstream market is automatically an abuse. Such conduct will not have an adverse impact on consumers unless the dominant undertaking's final product is sufficiently insulated from competition to give it market power.[6]

In conclusion, with reference to Articles 52, 55, and 57 of the Law Proposal, for a company to be found liable in a manner consistent with competition theory, practice, and enforcement in modern market-based economies, there must be a predicate finding that the market power held was acquired through recognized exclusionary or exploitative conduct. A dominant market position or a concentrated market cannot, in themselves, amount to a violation of competition law based on the vague concept of "barriers to competition," and cannot lead to structural measures and price regulation. That would be bad law and would also be at variance with the most fundamental principles in effect in mainstream competition law systems globally. It would also harm both competition and consumers, apart from the specific companies concerned.

B. "Barriers To Competition" As a Trigger for a Market Investigation Leading to Behavioral and Structural Measures

The second way in which the Law Proposal employs the concept of "barriers to competition" is as a trigger for the conduct of a market investigation. This can potentially lead to the imposition of behavioral and structural measures on a number of market players, even though the companies concerned did not engage in any violation of the competition rules.

We understand that the Mexican Competition Act currently in force allows the conduct of market studies, which are issued as non-compulsory "opinions" by the chairman of the Commission.[7] Indeed, a number of market studies have been conducted and most of them concerned regulated sectors: technological convergence (2005), content provision in telecommunications (2006), competition in the provision of individual retirement accounts (2006), retail banking services (2007), competition in airport services (2007), and foreign trade (2008).

[6] Case C-7/97, *Oscar Bronner GmbH & Co. KG v Mediaprint Zeitungs- und Zeitschriftenverlag GmbH & Co. KG and Others*, [1998] ECR I-7791, Opinion of AG Jacobs, ¶¶ 56-58 (emphasis added).

[7] OECD Policy Roundtable, Market Studies, DAF/COMP(2008)34, p. 75.

Such market studies are in-depth opinions that elaborate on a particular industry's structure and its existing regulation and contain detailed analyses of competition conditions in specific goods or services in these regulated markets. They include a set of recommendations for the government or the legislature and observations on the industry's structure and behavior, but they do not and cannot lead to behavioral or structural measures that the competition authority can impose. In other words, such investigations are seen as a tool of competition **advocacy** (and potentially also legislative advocacy), and not as competition **enforcement**.[8]

Market studies that are disconnected from the imposition of behavioral or structural measures are a useful tool in the hands of competition authorities[9] A number of competition laws, including EU competition law, are familiar with this tool currently in force as a component of the existing Mexican Competition Act.[10]

However, the Law Proposal goes much further and introduces for the first time a very different model, that of **market investigations leading to the adoption of regulatory measures of a behavioral or structural nature**. This is not a model that finds favor with competition law systems internationally. We are familiar only with the U.K., Greek, and Israeli systems that have adopted this rather controversial model. We understand that the Law Proposal, indeed, purports to introduce the U.K. model into Mexican law.

The U.K. model of market investigation is aimed at assessing whether competition in a market is working effectively and where it is desirable to focus to answer this question, e.g. on the functioning of the market as a whole rather than on a single aspect of it, or the conduct of particular firms within it. A market investigation aims only to see if competition within the particular market under review is working well or can be improved and is not seeking to establish general rules and obligations for firms.[11]

A market investigation's overarching framework allows the investigation to tackle "adverse effects on competition" from any source. As well as being able to look into the conduct of firms, the competition authority can probe for other causes of possible "adverse effects on competition," such as structural aspects of the market (including barriers to entry and expansion) or the conduct of customers. Having established a competition problem, and identified its causes, the competition authority is then able to impose a wide range of legally enforceable remedies, including behavioral and structural measures, extending even to divestitures of assets, and make recommendations for remedial action by other public bodies.

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[8] *Id*. p. 80.

[9] OECD Policy Roundtable, Market Studies, DAF/COMP(2008)34; ICN Advocacy Working Group, Market Studies Project Report, June 2009.

[10] Jurisdictions that recognize this tool include the European Union, the United States, Romania, South Africa, Italy, and Mexico. *See generally* Tamar Indig & Michal S. Gal, *New Powers-New Vulnerabilities? A Critical Analysis of Market Inquiries Performed by Competition Authorities*, COMPETITION LAW AS REGULATION (Di Porto & Drexl, eds. forthcoming, 2014), *available at* SSRN: http://ssrn.com/abstract=2333068. *See also* ICN Advocacy Working Group, Market Studies Project Report, June 2009.

[11] UK Competition Commission, CC3 (Revised) - Guidelines for Market Investigations: Their Role, Procedures, Assessment and Remedies, pp. 8-9 (April 2013).

The identification of anticompetitive features in a market investigation, or the imposition of remedies, does not mean that market participants have infringed the law.[12] Nevertheless, it certainly impinges on the economic freedoms of market participants, especially if they are the addressees of behavioral or structural measures. The Greek and Israeli systems are broadly modeled on the U.K. system.

There are a number of reasons why Mexico is well-advised to exercise caution before uncritically adopting this model. Certainly, some drawbacks of that system must be given proper consideration. Below we mention a number of such drawbacks:

1. A market investigation that leads to the imposition of regulatory measures of a behavioral or structural nature represents a rather extreme intervention in the core of economic freedom. Competition law, of course, may intervene to regulate conduct on the market. This is not objectionable when the company or companies concerned have acted through an anticompetitive agreement or by abusing their market power. On the other hand, when no such specific anticompetitive conduct has taken place, it is not obvious why a company should be subject to regulation and to measures restricting its freedom, merely because of the existence of a market structure that is considered simply undesirable. Such an intervention that, in the end, punishes a company for the status of the market on which it is present, departs from the general principle of imputation of antitrust liability that is applicable to competition law enforcement.

2. Even if there is an important public interest at stake, it is not clear why the existing orthodox legal standards and tools available to Mexico's competition authorities do not allow them to efficiently fight against anticompetitive conduct. On the one hand, merger control allows them to assess *ex ante* the risks of lessening of competition that an excessive increase of market power could create. On the other hand, the detection and punishment of anticompetitive practices allow competition authorities to restore *ex post* the competitive functioning of the market. They also give *ex ante* incentives to firms to behave in a pro-competitive way. The action of competition authorities in these two fields relies on a precise standard of proof, and intervention is based on the implementation of a set of approved methods and tests that guarantee legal certainty and a level-playing field on the market.

3. When the competition authorities are given the additional task positively to increase competition in a market, this increases uncertainty in the market. It is not clear which degree of intervention is warranted and which tools for achieving it are preferable. Thus, this represents a paradigm shift from the certainty (or from an acceptable degree of uncertainty) of the standard anticompetitive practices (agreements and abuse of market power) to the uncertainty of "increasing competition." This, in turn, might negatively affect firms' conduct, especially investment decisions.[13]

4. An argument that is used in favor of the market investigation tool is that it allows the competition authorities to deal with cases of "market failures." However, it is not certain that such "market failures" should always be remedied within the confines of competition law, particularly if the orthodox tools of competition law cannot remedy the absence of effective

[12] *Id*. p. 9.

[13] Indig & Gal, *supra* note 10.

competition in a specific market. The source of the problem may not lie in competition itself, but rather in other factors, such as regulation, network effects, customer inertia, or imperfect information flows between market participants. A good example is often the case of regulated markets or of oligopolistic markets that were recently liberalized. In most cases, the answer to the problem of "market failures" lies in regulation itself and not competition. For example, in the only final market investigation conducted in Greece by the Hellenic Competition Commission, it transpired that the real problem lay in State regulatory measures that were restricting competition.

5. The introduction of a full-fledged market investigation system entails a dramatic departure from the basic philosophy of competition law, as it breaks some of the traditional lines between *ex post* and *ex ante* regulation and broadens the competition authorities' powers significantly to include "market engineering."[14] Indeed, it is not guaranteed that competition authorities can recreate conditions of free competition as if they were the product of a "laboratory."

6. Competition authorities themselves sometimes are reluctant to be given such regulatory powers by legislation and may consider the market investigation tool a "poisonous chalice." This is because it may result in diluting the resources designated to traditional tasks, leading to inferior performance and inferior deterrence. For example, the indicative timescale of the U.K. Competition Commission for the carrying out and finalization of a market investigation is 18 to 24 months. To that timescale, one must add the proceeding before the Office of Fair Trading ("OFT"), which makes the decision to "refer" the case to the Competition Commission. In short, this is a terribly time- and resource-consuming exercise. In the United Kingdom, it consumes the resources of two well-endowed and sophisticated authorities. It is not clear how smaller competition authorities could cope with it, bearing in mind that they have to prioritize their other antitrust cases. In Greece, the Hellenic Competition Commission has not been eager to open this proceeding, precisely for lack of resources. In sum, the market investigation tool may be described as a "luxury tool" that has to be handled with care.

7. The introduction of the market investigation tool, particularly when the law gives the Executive the initiative for its deployment, creates a certain politicization of competition law enforcement and may ultimately harm the competition authority's independence. This, of course, depends on the circumstances of each country. It may also provide an excuse to governments that fail to proceed with desirable structural reform, because they can pretend that it is the role of the competition authority to proceed to structural reform via the market investigation tool. This is an idea that we consider extremely dangerous.

As a result, while we certainly consider interesting the U.K. experiences with the market investigation tool, particularly with regard to existing or former State monopolies, we caution against its uncritical introduction into other economies that do not share the same economic, political, and institutional features. Mexico should proceed with caution even if it is satisfied that its institutions share a substantial degree of empirical expertise attained from "normal" competition enforcement.

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[14] *Id.*

C. The Flawed Test of "Barriers to Competition" in Mexico's Proposed Market Investigation System

In any event, even if Mexico is firmly resolved to introduce into its Competition Act a system of market investigation leading to the imposition of behavioral or structural measures, we consider imperative that the current text of the Law Proposal which refers to the totally nebulous concept of "barriers to competition" be revisited. Article 94 of the Law Proposal provides that "[t]he Commission shall initiate ex officio or by request of the Federal Executive Branch, on its own motion or through the Secretary General's Office, the proceeding of market investigation to determine the existence of barriers to competition or of essential inputs."

This text is at variance with the test used in the other known systems that include such a market investigation tool. For example, U.K. law refers generally to any "feature, or combination of features, of a market in the United Kingdom for goods or services" that "prevents, restricts or distorts competition," and, more specifically, to "the structure of the market concerned or any aspect of that structure" and to the conduct of the market participants and their customers.[15]

Greek competition law, for its part, gives powers to the Hellenic Competition Commission to conduct market investigations in sectors of the Greek economy where "there are no conditions of effective competition" and where it considers that its existing enforcement powers "do not suffice for the creation of conditions of effective competition."[16]

Finally, in Israel, the law in force empowers the competition authority to actively change market conditions in markets characterized by a high degree of oligopolistic coordination.

As seen from these examples, none of the existing full-fledged market investigation systems relies on the notion of "barriers to competition" and none singles out "essential inputs." Indeed, the relevant text of the Law Proposal suffers from a number of flaws:

1. As explained above, the concept of "barriers to competition" is confusing and not customary in competition law and economics.[17]

2. The linkage of "barriers to competition" with the existence of so-called "essential inputs" is equally confusing and dangerous. If by "essential inputs" the text refers to the doctrine of "essential facilities," then this raises serious concerns. Competition laws exceptionally consider a dominant company's refusal to grant access to "essential facilities" as an abuse of market power if there is an exclusionary incentive to restrict competition on a downstream market. But in order to do so, competition authorities carefully examine to what extent the facility should indeed be considered as essential. This is a crucial step since otherwise, forcing access would deprive the owner of his property right and therefore, of any incentives to invest in the production of the input.

Outside the area of market power and of exclusionary abuses, there can be no application of the doctrine of "essential facilities." Particularly in the area of market investigations, if that

[15] UK Enterprise Act 2002, s. 131 *et seq*. *See also* recent amendments by Enterprise and Regulatory Reform Act 2013, s. 33 *et seq*.

[16] Article 11(1) of the Greek Competition Act.

[17] *Supra*.

doctrine were to be put in effect, it would amount to a serious blow to competition on the merits and to consumer welfare.

3. Introducing a new and vague concept of "barriers to competition," especially in combination with the reference to "essential inputs" would certainly send a clear signal to firms to be reluctant to engage in investments in the absence of a clear legal context regarding their assets. That would be in particular detrimental to innovation.

4. A policy mandating divestitures for companies that attain specific market-share thresholds, or have invested in what may be considered as "essential inputs," may also have perverse consequences on their incentives to invest and innovate over the longer term. For instance, a firm may refrain from making significant investments for fear of triggering mandatory divestitures if these investments may lead to substantial growth in the firm's share. Likewise, it may refrain from investing in and developing an innovative technology for fear of that technology being considered an "essential input."

5. The proposed price regulation provisions, which are linked with the mandating of access to "essential inputs," are problematic and would bring the authority into the shaky ground of a cross-sector regulator, when it has no such expertise. The proposed legislation also begs the question of "what is the correct price" of access, especially in the case where there has been no prior access. Moreover, competition authorities are not well equipped to define what the access price of an "essential input" should be. Usually, they only define principles these prices should obey, like that according to which prices should be "cost oriented," but are unable to compute the adequate **level** of prices that should prevail for the access to a facility.

6. The envisioned change in the legislation carries thus the risks of "false positives;" that is, the likelihood that pro-competitive behavior will be punished. This in turn would lead to perverse incentives to firms. In order to adequately invest in R&D, new projects, and production tools—which are all ingredients of competition on the merits—firms need to be secured in the legal environment in which they operate. Legal certainty regarding the assessment of anticompetitive behavior is a crucial part of this environment and competition authorities should only base their interventions on methods and concepts that leave limited scope for vague interpretations.

IV. CONCLUSIONS

Our analysis of the Law Proposal leads us to the following conclusions:

- The introduction of a *sui generis* violation of competition law centered around the notion of "barriers to competition" (per the proposed Articles 52, 55, and 57) is flawed and runs counter to the most fundamental principles of competition law and economics. It would create an intolerable degree of legal uncertainty for enterprises and would be detrimental to competition, consumer welfare, and to the Mexican economy as a whole.
- The adoption of a system of market investigation leading potentially to behavioral and/or structural measures should be viewed with caution because of a number of drawbacks. A more developed cost-benefit analysis is called for, building on past experiences in those few systems that have adopted this model. In addition, the applicable test for regulatory

intervention should be clearly structured around a consumer welfare standard and not around nebulous concepts.

- In any event, the introduction of market investigations to deal specifically with "barriers to competition" and perceived problems associated with "essential inputs" is flawed and at variance with the other few existing models, which the Law Proposal in effect purports to follow. It should be avoided because it creates a severe risk that pro-competitive behavior will be blocked, thus harming the public interest that competition law aspires to protect in the first place.