

The Value of Checks and Balances: “Non” Dominance in Restricted TV and Audio in Mexico



CPI COMPETITION POLICY
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By Francisco E. Castillo & Elisa V. Mariscal

One of the characteristics of a democratic country is the existence of checks and balances between its different branches of power. This peculiarity is useful, since the actions of the various arms of government are sometimes imperfect – due to institutional limitations, cognitive disagreements about the “state of the world”, or failures of political representation that affect the pursuit for the best possible results for the majority of citizens, among others. Thus, the government’s actions must be constructed among several institutions in order for each to compensate for the weaknesses in the others, while their redundancy allows for a decision to be maintained under joint control. Judicial review of administrative actions is a clear example of the above.

Framed against this background we find the approval by the legislative branch of a constitutional reform on the subject of economic competition and telecommunications, from which derived the Federal Telecommunications and Broadcasting Law (Ley Federal de Telecomunicaciones y Radiodifusión, LFTR), which granted authorities broad powers to limit excess of market power in the Restricted Television and Audio Services (Servicio de Televisión y Audio Restringido, STAR) markets. The reform created a technically independent organism, with budgetary autonomy and experience in the field of competition regulation which – far from imposing limitations – considered the risk of market power consolidation in the STAR market to be low. The resolution issued by the Plenary session of the Federal Telecommunications Institute in September 2015 found there were no elements that would determine the presence of an economic agent with substantial market power in the STAR sector. Here, we were presumably playing witness to a validation of Stigler and Peltzman: where there is conflict between different interests within the regulatory process, the interests of the producer tend to prevail over those of the consumer.¹²

This past Thursday, January 19th, 2017, we had a “taste” of what a mature democratic interaction may look like for Mexico. The First Circuit Collegiate Tribunal for Administrative Matters Specialized in Economic Competition, Broadcasting and Telecommunications (CERT), the first court created to specialize in technical and economic issues in Mexico, unanimously decided to strike down the IFT’s resolution, explicitly stating that the IFT’s resolution was illegal because it had been based on the use of data and evidence gathered outside the official timeframe for the investigation. Putting to one side the substance of the tribunal’s decision – with which the authors agree, and hope it will be respected by the IFT – the fact that, for the first time in the recent history of economic regulation in Mexico a judicial court has broken ranks with an autonomous regulator to strike down one of their resolutions is cause for general celebration.

¹ George J. Stigler, “The Theory of Economic Regulation”, *The Bell Journal of Economics and Management Science* 2, núm. 1 (1971): 3–21, doi:10.2307/3003160.

² Sam Peltzman, “Toward a More General Theory of Regulation”, *The Journal of Law & Economics* 19, núm. 2 (1976): 211–40.





This decision strengthens the impulse for doubling down on efforts to collaborate with the judicial branch in specialty subjects, as a way to expand their knowledge and allow their work of judicial control to go beyond the weak scrutiny given to administrative actions. Judicial review requires decisions that understand the deeper issues being discussed by specialized regulators. This control should impose rules, so that the discretion of administrative bodies is not spent on “novel” theories; or imposing new tests towards the end of an investigation without the affected parties having a say on the matter, weakening the Rule of Law. This decision sends a clear message to regulators regarding the importance of keeping an independent investigation department, capable of presenting and reviewing the evidence and arguments presented by all parties in an impartial manner. But above all, it exalts the technical and reasoned approach that must be taken when dealing with technical matters in sectors with a high level of specialization in their economic, regulatory and competition dimensions.

The importance of determining whether an agent possesses market power in the STAR sector

The regulatory paradigm that informed regulation in sectors involving network industries has changed in recent decades – mainly as a result of the privatization of former State-owned monopolies – incorporating elements that are relevant to competition policy³. Under this new perspective, regulation strategies are characterized by limiting *ex ante* type regulation in cases where:

- The development of infrastructure by smaller participants in the sector can be encouraged through price regulation, particularly on fees for access to the infrastructure used by the incumbent (investment ladder)⁴. And;
- There is a significant risk that the dominant company will abuse its power over the market.

This approach to regulation, gradually adopted by several countries – including our own – holds that regulatory mechanisms should be imposed *ex ante* only when three conditions are met:

- i) There are non-transitory barriers to entry;
- ii) There is an absence of a trend towards free competition, caused by said barriers;
- iii) Competition norms are insufficient to correct the consequences of a market failure caused by the presence of a dominant actor in the market.

This way, the modern regulatory regime relies on the implementation of the standard Competition triad:

- a) Definition of the relevant market;
- b) Identification of the dominant actor (economic agent with substantial market power, according to Mexican law), and;
- c) The formulation and implementation of appropriate regulatory remedies.

And so, the leading motivation for identifying an agent with substantial market power is to determine whether the market being analyzed faces any potential risks of uncompetitive behavior by the dominant company. Where this risk is significant, it is the duty of the sector regulator to impose appropriate measures.

³ Peter Alexiadis y Martin Cave, “Regulation and Competition Law in Telecommunications and Other Network Industries”, en *The Oxford Handbook of Regulation*, de Robert Baldwin, Martin Cave, y Martin Lodge (OUP Oxford, 2010).

⁴ The “Investment Ladder” is an approach proposed by Martin Cave, which has been widely embraced by telecommunications regulators in European markets. Martin Cave, “Encouraging infrastructure competition via the ladder of investment”, *Telecommunications Policy* 30, núm. 3–4 (abril de 2006): 223–37, doi:10.1016/j.telpol.2005.09.001..

The approach consists on giving companies that enter the sector successively, different levels of access to infrastructure while encouraging them to invest in network access infrastructure, which is increasingly less-replicable (ie. Going up each step of the investment ladder). The way this approach creates incentives for operators to invest is by establishing an access fee that increases gradually, or by eliminating the obligations for preferential access imposed on the incumbent after a pre-determined length of time.





Preponderance and Substantial Power in Telecommunications and Broadcasting in Mexico

Beginning in 2013, the regulatory framework in Mexico focused on easing the imposition of asymmetrical regulation in order to reduce the high levels of concentration in the broadcasting and telecommunications markets. Here, the legislature introduced the legal figure of preponderance, or Preponderant Economic Agent (Agente Económico Preponderante, AEP) as a Constitutionally defined concept applicable to service providers in two sectors: broadcasting and telecommunications. This was substantiated by their overwhelming participation in the national market (above 50%), whether measured by the number of users, subscribers, audience, network traffic or used capacity, as measured by the IFT.⁵

In effect, this allows the IFT to impose immediate regulatory measures to avoid free competition and free enterprise from being affected, thus protecting the end users. And so, the IFT determined that, in the Telecommunications sector, the economic group formed by América Móvil, Teléfonos de México and Teléfonos del Noroeste should be considered a preponderant economic agent, given its participation in the sector standing at more than 50%.⁶ Similarly, the IFT determined that Grupo Televisa (GTV) and a handful of its broadcasting subsidiaries could be classified as preponderant agents in the Broadcasting sector.⁷ As we can see, preponderance doesn't follow from specific criteria of competition policy, but merely from regulatory criteria.

The constitutional reform also gave the IFT the obligation to use its authority over competition in the telecommunications and broadcasting sectors to determine the existence of economic agents with substantial market power in the national Restricted Video and Audio services with public telecommunications networks and, if so, to impose any necessary measures.⁸ From a technical standpoint, this seemed to be a coherent decision, as economic convergence would eventually force restricted TV and Audio to become a competitive restraint on both sectors – telecommunications and broadcasting. In this way, the agency allowed a dynamic sector in the process of converging with two other regulated sectors to regulate itself, not by decree but through the effects of competitive dynamics between the operators in each market. This way, lifting or modifying measures imposed on these markets could be made more simple and flexible than it had been by the sectors that already had established preponderant agents.

However, despite the LFTR having established an obligation for rigorous analysis of competition; despite the Preliminary Finding by the IFT's independent Investigating Authority (AI), which found that GTV held substantial market power in 2,124 relevant markets for the delivery of STAR services;⁹ and that the Competition Unit – after assessing all the evidence presented by the affected parties, mainly GTV – proposed to the Plenary session of the IFT to declare the existence of substantial market power holders in the relevant markets by the economic group led by Televisa;¹⁰ and that the IFT's Plenary kept within the Resolution the AI's arguments with virtually no modification, the final decision came as a surprise. In little over a page

⁵ Eighth Transitory Article of the "Decree by which are reformed and added several dispositions to articles 6, 7, 27, 28, 73, 78, 94 and 105 of the Political Constitution of the United States of Mexico, on the subject of telecommunications", published in the Official Federal Gazette on the 11 of June, 2013.

⁶ Resolution by which the Plenary session of the Federal Telecommunications Institute determines the economic interest group formed by América Móvil, Teléfonos de México and Teléfonos del Noroeste to be Preponderant Economic Agent in the telecommunications sector. Available at <http://www.ift.org.mx/industria/politica-regulatoria/preponderancia-telecom/resolucion-pleno-ift-determina-grupo-1>.

⁷ Resolution by which the Plenary session of the Federal Telecommunications Institute determines the economic interest group formed Grupo Televisa to be Preponderant Economic Agent in the broadcasting sector. <http://www.ift.org.mx/industria/politica-regulatoria/preponderancia-radiodifusion/resolucion-ift-determina-grupos-interes>.

⁸ Transitory Article 39 of the Federal Telecommunications and Broadcasting Law

⁹ Public version of the preliminary finding issued in file AI/DC-001-2014. Available at: Versión pública del dictamen preliminar emitido en el expediente AI/DC-001-2014. Disponible en: <http://www.ift.org.mx/unidad-de-competencia-economica/version-publica-del-dictamen-preliminar-emitido-en-el-expediente-aidc-001-2014>.

¹⁰ Stenographic version (public version) of the XXXIII Extraordinary Plenary Session, 30 September 2015. Available at: http://www.ift.org.mx/sites/default/files/conocenos/pleno/sesiones/extraordinaria/xxiii-sesion-extraordinaria-del-pleno-30-de-septiembre-de-2015/versionpublicaestenografica33ext300915_1.pdf. Pg 14





arguments were presented that ran against the entire trove of information suggesting a Preliminary Decision in the opposite direction – based on data that exceeded and did not match with the time period under investigation by the AI – and the IFT Plenary found that it could not determine the existence of an economic agent with substantial market power in the STAR sector markets.

Specifically, the IFT declared that “the companies that currently form a part of GTV enjoy the largest aggregate participation in this service”, only to reel back with the suggestion that “their leading competitors have grown and increased their own share of the market.” The figures presented in the document show that the market share of companies “currently” part of GTV fell from 64.1% to 62.2% in the period between September 2013 and March 2015. A supposed 2 percent rise in the market share afforded to players on the margins of the market was sufficient, in the regulator’s opinion, to determine that the largest player does not hold substantial market power. This despite the AI’s ample evidence, pointing towards GTV’s substantial market power in 2,124 relevant markets, since the group:

- 1) Enjoys the largest share of each of these markets;
- 2) Controls which content is relevant for its rival’s commercial offer to include;
- 3) Has a competitive advantage over its rivals in accessing third party content, as it enjoys a wide base of subscribers in most of the relevant markets;
- 4) Unlike its competitors, it has two technological platforms (cable and satellite) for delivery of STAR services, allowing it to provide broader service, reach a larger percentage of consumers with varying price flexibility and market preferences, as well as weakening a market that, should it not form a part of the economic group, could represent an important competitive restriction;
- 5) There are significant barriers to entry in the relevant markets; and
- 6) There are few competitors in these markets exerting insufficient competitive pressure on GTV. The above is reflected by the large profit margins and high average earnings per user, which are not only greater to all other STAR providers in the market, but have also shown a tendency to increase in recent years.

Problems with the IFT’s decision regarding Substantial Market Power in the STAR market

Two main concerns arise from this action by the IFT’s Plenary. The first, correctly identified by the Tribunal, is that the evidence used to determine the IFT’s decision was introduced illegally, as it corresponds to a period not covered by the AI’s investigation. The AI’s preliminary findings contain evidence that covers the period between January 2009 and August 2014 – a period that was considered by the Tribunal as “representative and corresponding to the legal mandate imposed by the legislature to the IFT”¹¹, which lies in contrast with the evidence used by the Plenary to reach their decision. This evidence refers to the period between September 2014 and March 2015, which not only doesn’t correspond to the period under investigation, but fails to meet the legislative mandate (Transitory article 39 of the LFTR) to issue a declaration on substantial market power.

The second concern stems from the fact that the evidence used is not only illegal in nature, but that it is also built on incomplete data (cherry picking) or – even more serious – a deliberate intention of presenting information with the aim of persuading the audience to accept a position, when the evidence being left to one side points to a different conclusion. In this case, there are at least four reasons for concern regarding the seriousness of the decision to include or exclude certain information:

- 1) The “erosion of GTV’s market share” is observed over such a short period of time that it is impossible to make scientifically valid assertions regarding this observation. The reduced time frame (six

¹¹ Resolution of the Appeal under Review 141/2016 by the First Circuit Collegiate Tribunal for Administrative Matters Specialized in Economic Competition, Broadcasting and Telecommunications. Available at: http://sise.cjf.gob.mx/SVP/word1.aspx?arch=1304/13040000198342170004004.docx_0&sec=Marco_Antonio_Perez_Meza&svp=1. paragraphs 156 and 159.

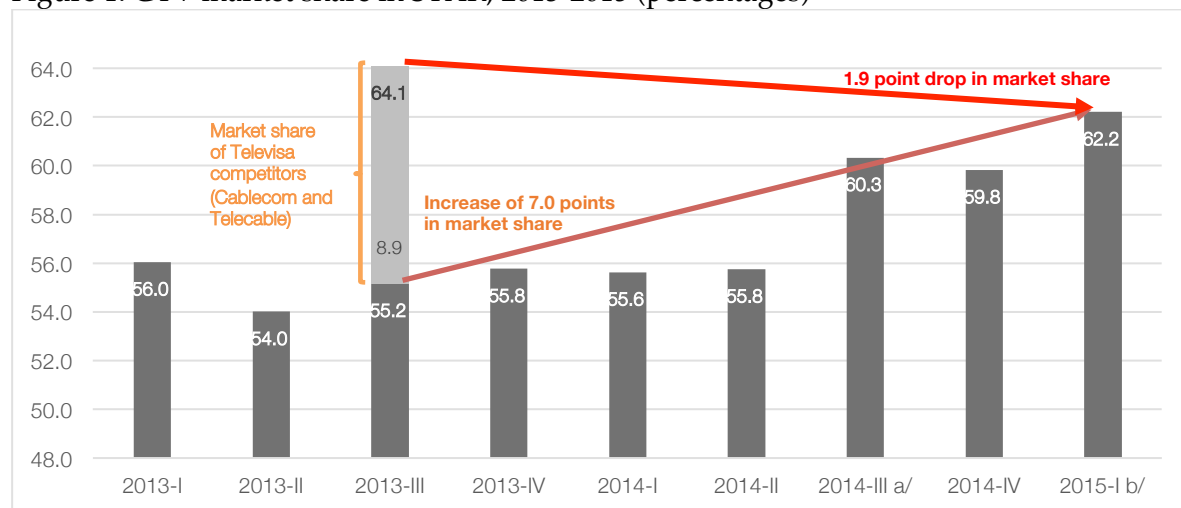




months) used by the Plenary to make its decision is in stark contrast to the period analyzed by the preliminary findings (five years). The suggestion that the increase in market share by GTV's competitors over such a short period of time is evidence of a lack of substantial market power cannot be supported by economic theory.

- 2) The drop in market share is far too small (2 percentage points) to infer a loss of market power, or the existence of conditions for effective competition in local markets, which weakens the Plenary's conclusions.
- 3) The localized geographical dimension used to determine relevant markets is extensively justified by the AI's Preliminary Findings. The trends in market share taken into account by the Plenary are at a national level. To consider aggregate trends at a national level ignores the reality of local markets, especially those where no real restrictions to competition exist.
- 4) Finally, the Plenary took into consideration the market share of an economic agent that did not exist during the time period reviewed by the Plenary (September 2013). GTV's historical market share, considered in the Plenary's conclusions for their resolution, included within GTV's interest group the companies Cablecom and Telecable, although neither of these companies were a part of the group at the time.¹² A correct reading is that, in the period considered by the IFT's Plenary Session, GTV's market share in fact increased by 7.0 percentage points. This is consistent with a valid analysis of economic competition.

Figure 1. GTV market share in STAR, 2013-2015 (percentages)



a/ Acquisition of Cablecom (august 2014).

b/ Acquisition of Telecable (january 2015).

Source: Own elaboration with data of the Quarterly Reports of the IFT, 1er. Quarter 2013 to 1st. Quarter 2015 and Televisa Annual Reports 2013, 2014, and Televisa Quarterly Reports 2013, 2014 and 2015.¹³

Judicial Checks and Balances: Appeals against the IFT's resolution

¹² Cablecom joined in August 2014, Telecable joined in January 2015.

¹³ Reports available at the following links: <http://i2.esmas.com/documents/2014/05/09/3242/descripcion-del-negocio.pdf>, <http://i2.esmas.com/documents/2013/10/24/3122/reporte-tercer-trimestre-2013.pdf>, <http://i2.esmas.com/documents/2013/07/08/3056/reporte-segundo-trimestre-2013.pdf>, <http://i2.esmas.com/documents/2013/04/25/2957/reporte-primer-trimestre-2011.pdf>, <http://i2.esmas.com/documents/2014/04/28/3224/reporte-primer-trimestre-2014.pdf>, <http://i2.esmas.com/documents/2014/07/07/3262/reporte-segundo-trimestre-2014.pdf>, <http://i2.esmas.com/documents/2014/11/28/3388/reporte-tercer-trimestre-2014.pdf>, <http://i2.esmas.com/documents/2015/05/04/3491/descripcion-del-negocio-2014.pdf>, <http://i2.esmas.com/documents/2015/04/23/3470/1ertrimestre2015.pdf>, Consulted October 2015





It is against this background that three different actors appealed before the Judicial branch, including Televisora del Valle de México (Proyecto40). This broadcaster appealed over the effects of the resolution on the Gratuity of Repeat Broadcasting of Open Television Content through Pay TV Systems Rule. According to the recent constitutional reform, broadcasters identified as having substantial market power would lose the right to transmit content created by other agents - including broadcasters of open-access television - without paying for this broadcast.

The First Specialized Court found that the plaintiffs had no legal or judicial standing on the matter, thus overruling the appeals. However, Proyecto40 then went before the First Circuit Collegiate Tribunal, which disagreed with the lower court, finding Proyecto40 to have legitimate interests to support an appeal on the IFT's resolution. Their decision establishes a real, differentiated and qualified negative effect on the company's judicial character. The tribunal then determined that the evidence used by the IFT's Plenary in making its decision had been illegal, granting the appeal to Proyecto40 and effectively striking down the IFT's resolution. Of course, the conclusion to this case will take some time. For the time being, the IFT has yet to issue a new resolution, which must respect the due processes established by the Judicial branch.

Often times it's subjects, such as the violation of human rights – deprivation of liberty, censorship, criminal abuse of authority or domestic violence – which capture our imagination and cause us to reevaluate the system of freedoms and individual rights we live in. In our case, a “small” and highly technical case in a minor and often overlooked sector, reminds us that Mexico is still on a decades-long journey towards becoming a country of Laws. Even though this doesn't always happen with the speed we would wish or in the manner we may have dreamed, the Tribunal's decision represents a great and decisive stride towards this country of laws, facts and reason which we have worked decades to build.

