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ANNUAL REPORT ON COMPETITION POLICY DEVELOPMENTS IN MEXICO

-- 2010 --

This report is submitted by Mexico to the Competition Committee FOR DISCUSSION at its forthcoming meeting to be held on 29-30 June 2011.

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Executive summary

- 1. This report presents the most recent developments in competition law and policy in Mexico, and summarizes the efforts to improve the transparency and predictability of the Mexican Federal Competition Commission's (CFC or the Commission) work, as well as some of its main advocacy and enforcement activities that were conducted in 2010.
- 2. During 2010, the CFC made important efforts to increase its transparency and predictability by facilitating access to its public information through a custom-made on-line search engine. In addition, the Commission developed several guidelines and reference papers to make explicit the methodologies it uses. With the same aim, it issued its Handbook of Procedures.
- 3. In April 2010 the President of Mexico, Felipe Calderon Hinojosa, submitted to Congress a bill to reform the competition legislation. The bill included important reforms such as the increasing of sanctions as high as 10 per cent of revenues and the possibility of criminal sanctions for firms that collude to fix prices; the simplification of merger review; the possibility of settling cases and conducting oral hearings; among others.
- 4. In 2010, the Commission issued several opinions to include competition considerations in the drafts of regulatory projects, legislative bills, regulatory framework and local regulations, among others.
- 5. It solved 519 issues. Mergers represented 30% of these issues, Investigations of monopolistic practices 5%, Concessions, bids, and permits 41%, Appeals for review 20%, Consultations and request 3%, and Declarations less than 1%.
- 6. Every year, the CFC works closely with the Judicial Branch in order to explain its resolutions and defend them when appeals are presented by firms before the tribunals. In 2010, the CFC maintained a good record in defending its decisions, winning 73% of the appeals that were presented.

1 Transparency and predictability

- 7. As the impact of competition policy in Mexico increases the demand to improve the transparency and predictability of the CFC's actions has also increased. For this reason, in 2010 the Commission launched several public consultations aimed at identifying areas in which the CFC's stakeholders believe it could improve.
- 8. As a result of the Commission's consultations, private practitioners, academic institutions and research centers, bar associations, non-governmental associations and the public in general expressed that the CFC should ease access and disclosure of its public information, as well as, issue guidelines.
- 9. In light of these suggestions, the CFC decided to focus its efforts in the two areas mentioned above.

1.1 Access and disclosure of public information

10. To increase transparency and to enhance the predictability and credibility of competition policy in Mexico, as well as, to respond to a longstanding demand by the Commission's stakeholders, the CFC developed a new on-line search engine.¹

Available at: http://www.cfc.gob.mx/index.php/RESOLUCIONES-Y-OPINIONES/buscador-de-resoluciones-y-opiniones-de-la-cfc.html.

- 11. Although, since 2007 the Commission has made an effort to digitalize all the information it has produced and make it available in the internet, the search tool on the CFC's website was far from user-friendly. To address this problem, the Commission decided to develop and implement a custom-made search engine which represents a substantial improvement in terms of usability, and therefore make all public documents issued by the CFC in its 17-year history readily available to specialists and the general public.
- 12. The new engine allows anyone interested in getting access to a particular decision or opinion by the CFC to search it by one (or a combination) of the following criteria: keyword, file number, name of economic agent involved, date, industry, type of procedure (i.e. investigation, merger, opinion, etc.), and type of anti-competitive conduct investigated.
- 13. At the end of 2010 the CFC organized a series of public events in which agency officials presented the new on-line search tool to the competition policy community in Mexico.

1.2 Issuance of guidelines, guides and reference papers

- 14. Fostering competition culture among Mexican economic actors is a key objective of the Commission, just as well as providing transparent and predictable mechanisms for interacting with the authority. In this regard, the CFC acknowledges that key mechanisms, among others, to achieve the above are guidelines, reference papers, and documents in which the Commission makes explicit the methodologies it uses. For this reason, and responding to the specific requests identified through the public consultations, the CFC decided to develop the following documents to delineate, answer questions or doubts, and set parameters of the work it conducts:
 - Guidelines for opening an investigation;
 - Guidelines on confidentiality issues;
 - Guidelines for the leniency program;
 - Guidelines for trade associations;
 - Guidelines on procedural aspects of merger notification and review;
 - Guidelines on fine setting:
 - Reference paper on relevant market definition; and
 - Reference paper on the assessment of market power.
- 15. By the end of 2010, the CFC released two of the documents mentioned above: the Guidelines for trade associations and the Guidelines for the leniency program. The Commission will release in 2011 the draft Guidelines on procedural aspects of merger notification and review, the draft Guidelines on fine setting and the Reference papers on relevant market definition and the assessment of market power, the latter two developed for the CFC by Dr. Richard Schmalensee Professor of the MIT Sloan School of Management and Dr. David Evans Executive Director of the Jevons Institute for Competition Law and Economics, University College London.

1.2.1 Guideline for trade associations²

16. Trade associations are created with the aim, among other things, to represent, promote and defend the general interests of its members. However, in pursuit of these legitimate objectives they may

Available at http://www.cfc.gob.mx/images/stories/Documentos/guias/guiaparaasociaciones.pdf

conduct or facilitate anti-competitive practices that constitute violations to the Federal Law of Economic Competition (FLEC).

17. In many cases during its investigations, the CFC has found that these associations have conducted or facilitated anti-competitive practices mainly because of their lack of knowledge or understanding of the competition law. Therefore, the CFC developed a Guideline to solve the doubts that trade associations and its members may have about violations to the law and its sanctions. This document also provides recommendations that they can follow in order to avoid incurring in these practices and includes contact information they can use if they have committed a violation to the law or know about a competitor conducting anti-competitive practices.

1.2.2 Guideline for the Leniency Program³

- 18. The new Guideline for the leniency program issued by CFC is intended to be a useful tool to answer any doubt that might arise about the particular benefit granted in exchange of full cooperation on possible collusion cases. Although the Leniency program has been established on both the FLEC (since 2006) and its Bylaw (since 2007), there was a void in the step-by-step guidance to file leniency applications. For this reason, the Guide provides a detailed procedure to file a leniency request, which additionally explains the general downsides of getting involved in this variety of anti-competitive practices.
- 19. The Guideline was presented in December 6, 2010 and Thomas Barnett, former Assistant Attorney General for the Antitrust of the United States Department of Justice, was the keynote speaker in this event.

1.3 Other actions

20. Additionally, the Commission is working on a number of projects that will improve the transparency of its work:

1.3.1 Procedures' Handbook

21. This handbook is an internal consultation document that focuses in the activities of the CFC's areas. One of its main objectives is to define, validate and standardize the procedures, policies, mechanisms and measures for internal control and supervision of the Commission. This document will be presented to the plenary of the Commission for approval in early 2011.

1.3.2 Oral hearings

22. The bill to reform the FLEC submitted in 2010 to Congress by President Felipe Calderón Hinojosa includes the implementation of oral hearings. Their aim is to guarantee that the voice of the parties involved in the proceedings is heard by the Commissioners and CFC's officials directly involved in enforcement actions. In these hearings, individuals can make clarifications deemed relevant to the arguments, evidence, and allegations presented in written to the Commission and to the documents included in the case file. In this regard, the CFC has created an internal working group to examine the feasibility of oral hearings on the basis of the Commission's legal framework and, where appropriate, draft guidelines for their implementation.

Available at http://www.cfc.gob.mx/images/stories/Documentos/guias/guiainmunidad2010.pdf

2 Changes to competition laws and policies, proposed or adopted

- 23. During the past years, the Mexican economy has been affected particularly by a combination of decreasing national competitiveness and low competition in several markets, especially those highly concentrated
- 24. To address this situation, in April 2010 the President of Mexico, Felipe Calderon Hinojosa, submitted to Congress a bill to reform the competition legislation currently in place. The bill was approved by the Chamber of Deputies and discussed in September 2010 by the Senate.
- 25. The bill includes the following elements:
 - Strengthening the competition policy by increasing sanctions as high as 10 per cent of revenues
 and the possibility of criminal sanctions for firms that collude to fix prices; allowing the CFC to
 undertake on-site searches, and avoid complex bureaucratic procedures that facilitate the hiding
 or destruction of evidence of an illegal conduct; and empowering the CFC to order the ceasing of
 acts or conducts that may seriously harm the process of competition and free market access.
 - Easing law enforcement by allowing the possibility for undertakings to settle cases and offer their views in oral hearings; it also considers notification exemptions for certain type of mergers that pose no material risk to competition from the obligation to notify.
 - Strengthening the institutional framework and operational capabilities of the CFC by considering in the law the possibility of reckoning substantial market power for more than one firm; formalizing in the FLEC the information requests for market studies and opinions; formalizing in the FLEC the issuing of guidelines by the CFC to grant concessions, acquisitions and public infrastructure; and by improving the information flow from the CFC to the society, in order to increase legal certainty s.

3 Advocacy activities

- 26. In 2010 the CFC continued its efforts to promote the principles of competition in the design and implementation of economic policies and regulation.
- 27. The Commission has the power to issue opinions on draft laws and secondary regulation initiatives, regulations, rules, agreements, circulars and other administrative acts, as well as, adjustments to programs and public policies, when they can have adverse effects to competition. In addition, the CFC may issue an opinion to promote the principles of competition on current regulatory framework such as laws, regulations, etc.
- 28. During this year, the Commission issued several opinions to include competition considerations in the drafts of regulatory projects, legislative initiatives, regulatory framework and local regulations. Relevant examples of this work are the Opinion on the draft guidelines for developing a model of costs in interconnection rates between concessionaires, the Opinion for the issuance of guidelines to prevent regulatory restrictions to the efficient functioning of production markets, marketing and distribution of dough and corn tortillas, and the Opinion on the schedules for taking off and landing in airports.

3.1 Opinion on the draft guidelines for developing a model of costs in interconnection rates between concessionaires

- 29. The concessionaires of public telecommunications networks are required, in terms of the Federal Telecommunications Act, to allow the interconnection of their networks with those of its competitors. The interconnection enables users who have contracted their services with different providers to communicate with each other, or that a user can access to telecommunications services provided by concessionaires other than the one that provides access to their network. Thus, interconnection is a key instrument for the existence of greater competition in telecommunications services, such as telephony.
- 30. To comply with this provision, concessionaires must voluntarily sign an interconnection agreement. Historically, however, the concessionaires have disagreed, particularly with respect to interconnection rates. This has harmful effects to competition, since a firm can set high interconnection rates in order to displace new or smaller competitors. In addition, operators can coordinate a rate increase in order to reduce competition between them in the final market.
- 31. In this context, in November 2010, the Ministry of Communications and Transport submitted to the Federal Regulatory Commission the draft resolution by which the Plenum from the Federal Telecommunications Commission issued guidelines for developing cost models of interconnection fees for the provision of services between concessionaires of public telecommunications networks. The draft sets out principles to be followed by the authority to determine interconnection fees applicable to the concessionaires in the event of a disagreement on tariffs.
- 32. In December 7, 2010, the CFC issued an opinion in which it noted that the principles proposed in the draft guidelines are similar to those used internationally and recognized as best practices in regulatory matters. As a result of its implementation, the draft would trigger a more efficient use of public telecommunications networks and prevent anticompetitive behavior. In addition, it would provide certainty to the concessionaries on the determination of interconnection rates and reduce costs associated with the negotiations in this area. For these reasons, the CFC recommended the expeditious implementation of the draft, in order to provide telecommunications services a competitive basis, for the benefit of consumers and businesses that require these services.

3.2 Opinion for the issuance of guidelines to prevent regulatory restrictions to the efficient functioning of production markets, marketing and distribution of dough and corn tortillas

- 33. Corn tortillas are an integral part of food consumption in Mexican households. For half of the population, tortilla consumption represents more than 8 percent of their expenditure on food and, for the poorest, the purchase of this product absorbs up to 5 percent of their total income. Under this scenario, intense competition among suppliers of tortillas has an important social impact, because it allows consumers to choose among several options to purchase the product at the best possible price and quality.
- 34. However, in the course of its investigations and opinions, the CFC has found a constant repetition of regulatory barriers, particularly at the municipal level-that inhibit competition in the production and sale of tortillas and therefore cause artificially high prices in this type of food. Therefore, on March 11, 2010, the Plenum of the Commission issued a nonbinding opinion and presented the "Guidelines to prevent regulatory restrictions to the efficient functioning of production markets, marketing and distribution of dough and corn tortillas."
- 35. The CFC guidelines included four specific recommendations to avoid regulatory barriers to entry and prevent illegal price agreements between tortilla shops. These recommendations were based on the most common types of constraints identified in the studies by the Commission:

- Eliminate minimum distances and other restrictions on the number of participants.
- 36. Often local regulations prohibit the establishment of a new tortilla shops close to another, limiting the total number of tortilla shops in a locality or prohibit services like home delivery. Such provision reduces consumer choice and leaves them at the mercy of a small number of suppliers, which are able to charge artificially high prices.
 - Eliminate provisions that allow established businesses to comment on the entry of new players and on market prices.
- 37. Some local regulations allow the authority to consult with tortilla shop groups over the authorization to allow a new shop to enter the market. In other cases regulations require that tortilla shops agree on prices and schedules. This type of regulations hinders the new entrance of suppliers and promotes collusion between tortilla shops, which limits competition between suppliers and damages consumers.
 - Address request for market access based on transparent and public criterion that favor the entry
 of new participants.
- 38. Some local regulations do not clarify the requirements nor the time for new tortilla shops to obtain the authorization to operate. This has led to requests that probably under pressure from established tortilla shops have never been resolved or are hampered with additional paperwork. The effect of these practices is to limit artificially the number of tortilla shops and the choices of consumers.
 - Eliminate requirements for minimum quotas of local inputs.
- 39. There are municipal regulations requiring tortilla shops to use a certain proportion of inputs produced in the same locality (e.g., corn), which restricts the ability of the tortilla shops to obtain their raw materials in the best possible price and quality. These provisions raise the costs of the tortilla shops and increase food prices, thus harming consumers.
- 40. Application of these guidelines by the municipal authorities would help eliminate artificial barriers to entry for new tortilla shops and make it more difficult to illegal price agreements, thereby encouraging more competitive prices that benefit consumers, especially the poorest.

3.3 Opinion on the schedules for taking off and landing in airports

- 41. In August 2010, Nuevo Grupo Aeronáutico, S. A. de C. V. announced the indefinite suspension of its operation, situation that reduced the supply of air transportation services in Mexico. This affected the consumers in terms of higher prices and lower availability of routes and schedules.
- 42. In order to turn the situation around, on September 2, 2010, the Commission issued an opinion through which the Minister of Communications and Transports and the International Airport of Mexico City were recommended to assign, urgently and temporarily the schedules for taking off and landing (called slots) assigned to Mexicana in that airport.
- 43. However, the CFC pinpointed that it was fundamental that the reassigning be carried out taking into consideration measures that would favor competition, without creating exclusive advantages for any operator, with the objective to insure conditions for availability, price and quality for the consumers.

- 44. Specifically, the Commission recommended:
 - Not to restraint the authorization of routes, in other words, to authorize promptly the operation of any route to any airline that requests so and meets the regulations in security matters.
 - Not to associate (just in exceptional cases clearly justified) the assignment of a slot to a specific route.
 - To impose limits to the accumulation of slots by schedule, to avoid an excessive concentration of this fundamental input.
- 45. Along the same lines, the Commission recommended that once the situation caused by the Grupo Mexicana be overcome, a permanent procedure of slot assignments capable of insuring the competition in crowded airports needs to be drafted, in order to promote the efficient work of the aeronautics industry in Mexico
- 46. Currently, the assignments of slots are made according to what is stated in the Regulation of Airport's Law. Therefore, in late 2010 a working team made up of representatives from the Federal Competition Commission, the Minister of Economy, the Minister of Communications and Transports, the International Airport of Mexico City and Services for Navigation in the Mexican Air Space was created, in order to design an amendment to the Regulation of Airport's Law that would make more efficient the procedure to assign slots.
- 47. This working team came up with a proposal to amend the Regulation, which, at the closing of this report, is being analyzed by the Sub minister of Transportation.

4. Enforcement of competition law

- 48. To enforce effectively the FLEC the CFC has several procedures grouped into six areas: monopolistic practices; mergers; opinions; consultations; requests for reconsideration and appeals, and declarations on effective competition conditions.
- 49. In the next subsections the Commission's work in the areas of monopolistic practices, mergers, opinions and appeals will be summarized.

4.1 Action against monopolistic practices

50. Monopolistic practices are those that, because of their object or effect, damage or prevent the process of competition and free market access in the production, processing, distribution and marketing of goods and services. The FLEC considers two types of monopolistic practices: relative and absolute.

4.1.1 Summary of a relevant case

Mexican Social Security Institute public procurement process of medicines and drugs⁴

In May 2006, the CFC requested information from the Mexican Social Security Institute (IMSS) on their public procurement activities to purchase drugs and medicines. With the information from IMSS the Commission found several patterns that displayed similar positions between providers and high prices in some drugs, which seem to indicate possible collusion. Therefore, in August 2006 the Commission launched an official investigation.

⁴ Files IO-003-2006, RA-019-2010, RA-028-2010 and others related.

The Commission's investigation focused on public tenders conducted from 2003 to 2006 for the purchase of two products: insulin and electrolyte solutions. With the information gathered in the investigation it was found that, indeed, several companies coordinated their positions to raise the prices of these products acquired by the Institute to the detriment of its beneficiaries and public finances.

In January 28, 2010 the Plenum of the Commission fined the six pharmaceutical companies that conducted bid rigging, as well as eight individuals acting for and on behalf of their employers to carry out absolute monopolistic practices. The sanctions imposed amounted to an aggregate of 12.6 million US dollars.

In addition, the analysis conducted by CFC using the information provided by the Institute identified that its procurement rules and policies atomized its bidding process throughout the Mexican territory, facilitating market sharing and bid rigging, aside from preventing them from identifying collusive behavior. The CFC's recommendations to the IMSS focused on consolidating its requirements and procedures. These recommendations were aggressively implemented and derived from this action, from 2006 to 2010, IMSS has saved over 2.9 billion US dollars in the purchase of medicines, equivalent to the annual budget of the Commission for the next 218 years.

4.2 Mergers

51. Merger control is the key preventive tool of the Commission to protect competition and free access to markets. The CFC has the exclusive powers to assess mergers, acquisitions, or any other act by which corporations concentrate in Mexico.

4.2.1 Summary of a relevant case

• Novartis/ Nestle/ Alcon Laboratories⁵

In March 17, 2010 the CFC was notified an international operation by which Novartis AG (Novartis) acquired the shares of Alcon Inc. (Alcon), owned by Nestlé. As a result, Novartis controlled indirectly Alcon Laboratories, Inc.

Novartis is a Swiss company that develops, produces, distributes and markets pharmaceuticals, vaccines, generic pharmaceuticals, health products, and contact lens care products. Alcon is a Swiss company that develops, manufactures and markets ophthalmic pharmaceuticals, ophthalmic surgical equipment and supplies for the care of contact lenses and other products related to eye care. In Mexico, Novartis and Alcon overlapped in various pharmaceuticals.

The Commission found that the merger would have a negative effect on competition in the market for multiple-action anti-allergy ophthalmic products. More specifically, the Commission concluded that, with the acquisition of Alcon, Novartis could reach a significant market share and no competitors with the ability to counter a likely price increase or reduction in supply for this product were identified.

To address the concerns of the Commission in this market, the companies proposed to the CFC to divest one of their products. In August 18, 2010 the transaction was authorized, subject to conditions of divestiture.

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⁵ File CNT-017-2010.

4.3 Judiciary

- 52. To ensure compliance with its resolutions, the Commission devotes significant resources to defend its actions and administrative decisions before the judiciary.
- 53. In 2010, the judiciary confirmed in 73% of the cases that the Commission met the requirements of motivation and complied with the legal framework involved in its proceedings and resolutions.

4.3.1 Summary of a relevant case

• Effectivale case⁶

In December 2007, the CFC issued a final decision to sanction Efectivale S.A. de C.V. (Efectivale) and other firms that sell food stamps for committing an absolute monopolistic practice, by which they agreed to raise the fees charged to the establishments that accept food stamps.

Following this decision, Efectivale promoted an appeal on the grounds that the CFC's decision was improperly grounded and motivated because, from their point of view, the arguments previously submitted to pursue its request for reconsideration were not properly analyzed. However, on February 20, 2009, a District Court denied the appeal and, said the Commission decision was properly founded and reasoned.

Efectivale presented an appeal against the Court's decision. However, in February 2010, a College Tribunal denied the appeal from Efectivale and confirmed in its terms the resolution of the CFC.

5. Resources of competition authorities

5.1 Resources overall (current number and change over the previous year)

- 54. The Commission does not have complete budgetary autonomy; the Ministry of the Economy negotiates its own budget, and that of the CFC, with the Finance Ministry, and with Congress.
- 55. In 2010, the CFC's budget was \$ 155.4million pesos (approximately US\$12.3 million).

Annual Budget of the CFC in 2010						
		Change over previous year				
Approved budget in local currency	\$155.4 million pesos	-\$16.4 million Mexican pesos				
Approved budget in USD	\$12.3 million USD*					

^{*} Average exchange rate in 2010 was 12.63 Mexican pesos per dollar

56. The Commission had 183 staff in 2010, out of which 121 were non-administrative staff and exclusively worked on competition enforcement. There were 48 lawyers, 40 economists and 33 who have other background (such as social sciences, mathematics, engineering, and business administration.

Number of employees (person-years) as of 2010						
		Change over previous year				
Economists	40	+5				
Lawyers	48	+17				
Other professionals	33	-2				
Support staff	62	-6				
All staff combined	183	+14				

⁶ File DE-022-2005, y RA-027-2007 and other related documents.

ANNEX 1

FEDERAL COMPETITION COMMISSION

Files concluded in 2010

rnes Concluded in 2010	
	2010
TOTAL	519
MERGERS	158
Authorized	85
Conditioned	3
Not Authorized	0
Admissible Concentration Notices	67
Withdrawn	3
MONOPOLISTIC PRACTICES AND OTHER RESTRICTIONS TO COMPETITION	26
Complaints	24
Sanctioned	2
Closed	4
Dismissed	18
Own Initiative Inquiries	2
Sanctioned	2
Closed	0
CONCESSIONS, BIDS, AND PERMITS	211
Favorable Opinion	169
Favorable Opinion Under Restrictions	11
Non Favorable Opinion	0
Dismissed	31
CONSULTATIONS AND REQUESTS	18
DECLARATIONS	1
APPEALS FOR REVIEW	105
Merger	3
Monopolistic Practices	100
Concessions, Bids and Permts	0
Consultations and Requests	0
Declarations	1
Other	1
Decisions	
Confirmed	45
Modified	42
Revoked	3
Dismissed	15