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**DIRECTORATE FOR FINANCIAL AND ENTERPRISE AFFAIRS  
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More documentation related to this discussion can be found at: [oe.cd/cmkt](http://oe.cd/cmkt).

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## Competition for-the-market

### - Contribution from Peru<sup>1</sup> -

#### 1. Introduction

1. Indecopi, as the competition authority of Peru, makes recommendations and establishes criteria whose fulfillment seek to contribute to the promotion of competitive markets to achieve greater social welfare for the benefit of consumers, in compliance with its role as promoter of the development of a market economy and the performance of markets under the principle of free competition. Within this framework, Indecopi prepares and publishes various documents such as Market Studies (*advocacies*) and Normative Recommendations that become instruments that promote the culture of free competition. These documents contain an assessment of the existence of factors that weaken competition in each market, and, above all, they propose guidelines that would allow competition to be promoted in the market under analysis.

2. There are markets in which, due to their specific characteristics, it is efficient to promote the existence of a single firm in the market, as is the case of the natural monopoly, in which the State advocates the existence of competition "for the market", through previous bids or bids, whose winner of the process will become the sole supplier of the market, considering a certain geographical and temporal scope. This type of allocation mechanisms would allow the price fixed for the service to be competitive, reflecting its economic cost, or that its characteristics be of greater quality, among other positive effects for the economic agents. Competition "for the market" can be a good substitute for competition "in the market" (Lassere, 2014).<sup>2</sup>

3. In the specific case of competition for a market, Indecopi developed in 2016 an advocacy study on the market of tourist transport service to access the Inka City of Machupicchu. Moreover, it also processed a complaint for granting a firm the exclusive operation of vehicle technical inspection plants in Metropolitan Lima. As part of this document, a brief description of the regulatory framework under which Indecopi has competence to promote competition through market studies ("*advocacies*") will be provided, then we develop the two cases referred to, in which Indecopi analyzed whether there were factors limiting competition in each market, including the guidelines proposed to promote a greater degree of competition in such markets.

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<sup>1</sup> This document was prepared by the Department of Economic Studies of Indecopi and does not necessarily represent the opinion of the collegiate bodies that make up the different resolution bodies of Indecopi.

<sup>2</sup> LASSERE, B. (2014). Competition for the Market and Liberalization: The French Experience. Italian Antitrust Review. Vol 1, No 3 (2014). Available in: <<http://iar.agcm.it/article/download/11054/10248>>.

## 2. Legal Framework

4. In accordance with the provisions of article 14, paragraph 2, subsection e, of Legislative Decree No. 1034, "Law for the Repression of Anticompetitive Conduct", the Commission for the Defense of Free Competition of Indecopi (hereinafter, the Commission) is the area responsible for suggesting, exhorting or recommending the implementation of measures that restore or promote free competition to the entities of the Public Administration<sup>3</sup>. These measures include the elimination of barriers to entry or the application of economic regulation to a market where competition is not possible, among others.

5. These suggestions or recommendations are made through the publication of reports, studies, observatories and, in general, of advocacies that are carried out on different markets and in which their public and private agents in each market participate during its preparation. The Law for the Repression of Anticompetitive Conduct establishes that, after the recommendations of Indecopi have been submitted, the corresponding entities of the Public Administration must respond explaining their position in relation to the proposals made within a period of no more than 90 working days from their notification. The Commission then carries out follow-up work through formal written communications, with the objective of supervising the way in which its recommendations are being implemented.

6. In addition to the Commission for the Defense of Free Competition, Indecopi has a Commission for the Elimination of Bureaucratic Barriers, which carries out a legality and reasonableness analysis of prohibitions and demands which, despite not considering all anti-competitive conducts, their elimination helps for the promotion of competition. Specifically, this Commission may, within the framework of the analysis of the reasonableness of a complaint, assess the positive or negative impact of the barriers imposed on the economic agents of the market, as well as on the competitive dynamic in the market.

## 3. Concession assessment

7. Since 2014, Indecopi prepares and shares reports, market studies (*advocacies*), in which it issues recommendations regarding the most relevant measures to promote or introduce competition in different sectors, either competition in the market or competition for the market. Specifically, Indecopi has issued nine documents analyzing the conditions of competition in specific markets and has given recommendations<sup>4</sup>. This work complements to the resolution of complaints about anti-competitive behavior. The following two cases study the functioning of specific markets and give some recommendations to promote competition. The first case explains the competition advocacy about the tourist transport service market to access to the Inka City of Machupicchu, and the second one is related to the complaint about the concession granted

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<sup>3</sup> The term "entities of the Public Administration" is to be understood in a broad sense and includes: i) the entities that make up the Executive Branch such as the Office of the President of the Council of Ministers and the Ministries; ii) the Congress of the Republic; iii) the Judicial Branch; and iv) regional and local governments.

<sup>4</sup> In general, Indecopi has carried out a total of 7 advocacies or market studies, 1 recommendation document and 1 technical opinion of a specific case. These 9 issued documents can be found in the following link (in section "Advocacies"): <<https://www.indecopi.gob.pe/en/clc-publicaciones>>.

to a single firm to operate exclusively the vehicle technical inspection plants in Metropolitan Lima.

### 3.1. Tourist passenger transport service on the route Aguas Calientes – Puente Ruinas – Inka City of Machupicchu’s case<sup>5</sup>

8. Peru's main tourist attraction worldwide is the Inka City of Machupicchu, located in the city of Cusco, and visited in 2018 by 1.23 million foreign tourists, representing 27.92% of the total foreign tourists who visited Peru in that year<sup>6</sup>. To access Machupicchu, tourists can go from the town of Aguas Calientes: (i) paying a tourist passenger transport service, or (ii) hiking through a path for approximately 2 hours. However, in practice only a minority part of tourists chooses the second option due to the physical wear and tear and time involved in carrying it out, so in fact the tourist transport service has no substitute nearby.

9. From the analysis concluded by the Commission in its competition advocacy, it was identified that since 1995<sup>7</sup> - the year in which the first concession contract granted by the District Municipality of Machupicchu was signed - until today, a single firm, whose name is Consettur<sup>8</sup>, operates in this tourist transport market, from Aguas Calientes to Machupicchu. The Commission found that the first concession granted was for a period of 2 years but then several contracts were signed along the time<sup>9</sup> that extended the concession until March 2011. Therefore, the Commission concluded that when this advocacy was drafted, all contracts signed were expired and it was appropriate to convene a new tender for the service.

10. It should be noted that Indecopi does not have the power to grant or declare the conclusion of the concession held by Consettur to provide tourist transport service on the route from Aguas Calientes to the Inka City of Machupicchu; however, the Commission does have the power to suggest how to improve the competitive pressure in this market, taking into account the characteristics of the route.

11. The Commission identified two specific characteristics of the tourist transport market in Machupicchu which lessen the entrance of rivals on that market. On the one hand, the provision of the service would generate "negative externalities", especially to the environment, that are not assumed by Consettur (or internalized such as erosion and pollution); therefore, the price of the service, which does not reflect all costs incurred, generates an inefficient result in the market. On the other hand, the restriction of space is another limitation for the provision of the service, because the service is performed on a

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<sup>5</sup>The advocacy study is available at the following link: <<http://repositorio.indecopi.gob.pe/bitstream/handle/11724/5700/Abogacia%20transporte%20turistico%20Machupicchu.pdf?sequence=1&isAllowed=y>>

<sup>6</sup>Mincetur (2018). Available in: <[https://www.mincetur.gob.pe/centro\\_de\\_Informacion/datos\\_turismo.htm](https://www.mincetur.gob.pe/centro_de_Informacion/datos_turismo.htm)>.

<sup>7</sup>In 1995, the public bidding process for the tourist transport service on the route Aguas Calientes - Puente Ruinas – Inka City of Machupicchu was carried out by the District Municipality of Machupicchu.

<sup>8</sup>Tourist Transport Services Consortium Machupicchu – Consettur Machupicchu S.A.C.

<sup>9</sup>It is reported that there was a major controversy over a 30-year contract that was signed up together with the initial 2-year contract, however, the Superior Court of Justice of Lima and the Supreme Court of Justice of the Republic, established this 30-year concession contract was false and invalid.

very narrow unpaved road, which varies between 5 and 10 meters depending on the sector, which does not allow several vehicles to travel at the same time. In 2011, Sernanp<sup>10</sup>, the public entity that oversees the protection of natural areas in Peru, established a cap on the number of vehicles that may enter the Machupicchu Sanctuary Conservation Unit<sup>11</sup>.

12. The Commission indicated that even in cases where it is not possible to develop competition in the market, this is not an element that ends up discouraging other firms from wanting to compete for this market, as indicated by Demsetz (1968)<sup>12</sup>. Rather, firms interested in providing the service may participate in a bidding process, which grants the license to the firm offering the service at the lowest price, and this price is expected to be close to that of competition, eliminating or reducing the monopoly operator's ability to exercise market power.

13. The Commission noted that within the framework of Demsetz's proposal, it is necessary to consider certain inconveniences when signing the concession contract. For example, the winning bidder may be encouraged to provide a low-quality service in the medium term and thus increase its profit margins, affecting consumers. Similarly, in cases where firms offer more than one service or have differentiated prices in the market, this mechanism will present difficulties in choosing the firm that wins the concession. A third disadvantage may occur if one of the parties benefited by the contract ends up getting involved in the design of the bidding contest and establishing conditions that seek the best result for itself.

### *3.1.1. Policy recommendations*

14. In that sense, considering that the concession contract signed between Consettur and the Municipal District of Machupicchu would be expired, and that the best mechanism to promote competition in the tourist passenger transport market in Machupicchu pointed to "competition for the market", the Commission concluded that the service must be re-tendered, for which it must first establish clear specifications that define the parameters of the service and transparent rules for the selection procedure.

15. In line with the above, the Commission suggested the following as competition variables that the authority may establish at the time of designing the bidding contest: (i) the price to be charged to end users, (ii) the payment of a monthly fee to the municipality, and (iii) the participation of local firms, leaving it to the municipal authority to decide which competition factors are most appropriate, taking into consideration the promotion of free competition.

16. Also, it was recommended that the design of the bid take into consideration elements that promote transparency during the competitive process, so that none of the participating firms can be composed of officials or firms related to the municipality.

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<sup>10</sup> National System of Natural Areas Protected by the State.

<sup>11</sup> According to the resolution of the Historic Sanctuary of Machupicchu N° 001-2011-SERNANP-SHM of January 6, 2011, a total of 24 vehicles was established as maximum limit.

<sup>12</sup> For a "Demsetz Competition" to be feasible, two requirements must be fulfilled: (i) inputs must be available to all bidders in the market, with competitively determined prices; and (ii) the cost of collusion between rival bidders must be high.

17. Finally, the Commission considered it important to point out that an eventual tender for the tourist transport service in Machupicchu should seek to achieve the widest possible diffusion, in order to attract enough investors to compete for the concession of the service, thus fostering competition for the market.

### 3.2. Vehicle technical revisions service in Metropolitan Lima's case

18. In Peru, every vehicle that circulates in the national system of land transport must approve since 2003, and periodically, vehicle technical revisions. The purpose of this requirement is to ensure that motor vehicles circulating in Peruvian territory comply with the appropriate technical requirements and characteristics in order to protect the life and health of drivers, pedestrians and other transport users<sup>13</sup>.

19. In order to comply with this requirement, the Metropolitan Municipality of Lima (hereinafter, the Municipality) issued a bidding process in 2004 to grant in concession the execution of the infrastructure of the technical revision plants and the operation of the vehicle technical revision service for Metropolitan Lima, under the premise that the most efficient option for citizens, companies and agents in general was to cede the exclusivity of the operation to a single bidder, that is, to establish ex ante competition for the market.

20. The winning consortium was formed by the firms Lidercon S.L. (hereinafter, Lidercon) and Icesur S.A. However, the latter company retired from the concession, which delayed the opening and operation of one of the technical revision plants, and was the reason why the Municipality decided to rescind its contract in 2007. In view of this, Lidercon decided to take the case to arbitration in order to preserve the exclusivity<sup>14</sup>.

21. In this context, other operators expressed interest in operating in this market, due to the existence of an unsatisfied demand for this service. Therefore, the Ministry of Transport and Communications (hereinafter, the Ministry) initially authorized the entry of new competitors into the market. However, in 2008, the arbitration proved Lidercon to be right, so it had to reject the requests for authorization and renewal of these operators based on the existence of an exclusivity clause in the concession contract between the Municipality and Lidercon.

22. In this regard, the Commission for the Elimination of Bureaucratic Barriers of Indecopi received complaints from companies affected by not being able to obtain authorization from the Ministry to access or remain in the vehicle technical inspection market, and carried out an analysis of the legality and reasonableness of such measure, resolving that the Ministry's refusal to grant and renew authorizations from firms to carry out vehicle technical inspections constituted an illegal bureaucratic barrier and, therefore, the Ministry should allow operators to enter and remain in the market.

23. It is worth mentioning that it was found that there would be two characteristics of the market for technical vehicular revisions that may restrain rivals' access to provide the service under analysis. On the one hand, its natural monopoly characteristics, associated with economies of scale and sunk costs, allow to establish efficient tariffs with a single operator

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<sup>13</sup> Requirement established by the National Vehicle Regulation, issued by the Ministry of Transport and Communications in 2003. Available at:

<[http://transparencia.mtc.gob.pe/idm\\_docs/normas\\_legales/1\\_0\\_1957.pdf](http://transparencia.mtc.gob.pe/idm_docs/normas_legales/1_0_1957.pdf)>

<sup>14</sup> Lidercon sued the Municipality before the Arbitration Center of the Lima Chamber of Commerce in 2007.

for a given geographical area, and on the other hand, the existence of legal barriers established by the exclusivity clause of the concession contract for the case of Metropolitan Lima.

24. In the geographic area of Metropolitan Lima, it is not clear that the market for technical vehicular revisions has the characteristics of a natural monopoly, since there is no study that support the decision of granting the concession to a single company. On the other hand, the growth of the demand side, the delay of Lidercon in the opening and operation of technical plants and the regulatory flexibility have allowed new companies to enter the market in Metropolitan Lima. For example, the size of the vehicle fleet went from 123 to 175 vehicles per thousand inhabitants in the region of Lima between 2009 and 2016<sup>15</sup>. Indecopi's position has been consistent with the evidence that the market for vehicular technical revisions is not necessarily a monopoly, so it is crucial to promote competition in the market, so that more firms can enter, rather than allow the participation of a single firm.

### *3.2.1. Policy recommendations*

25. Indecopi recommends that the institutions in charge of bidding for various products and services carry out a prior analysis about the convenience of establishing competition in the market or for the market. The final goal is avoid restricting competition through legal mechanisms. In the event of a bidding process, it is important to determine the appropriate number of bidders needed by geographical area, in order to close the gap in the service to be covered.

26. In general, all regulation on citizens and firms must result from assessing the benefits and/or positive impact that the intervention would generate, internalizing the costs and/or negative impact of the measure for the economic agents directly affected, as well as for other stakeholders or market conditions (e.g. competition level). In the specific case of the vehicular technical inspection market, the restriction to a single firm would have had an important effect on the conditions for providing the service, such as the price level and availability of inspection plants throughout the granted geographical area.

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<sup>15</sup> According to statistics from the National Environmental Information System of the Ministry of the Environment.