Unclassified **DAF/COMP/LACF(2010)23**

Organisation de Coopération et de Développement Économiques
Organisation for Economic Co-operation and Development **09-Sep-2010**

English - Or. English

DIRECTORATE FOR FINANCIAL AND ENTERPRISE AFFAIRS
COMPETITION COMMITTEE

DAF/COMP/LACF(2010)23
Unclassified

LATIN AMERICAN COMPETITION FORUM

-- Session III: Strategies for Competition Advocacy --

Contribution from Colombia

8-9 September 2010, San José (Costa Rica)

The attached document from Colombia is circulated to the Latin American Competition Forum FOR DISCUSSION under session III of its forthcoming meeting to be held in Costa Rica on 8-9 September 2010.

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JT03288015

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LATIN AMERICAN COMPETITION FORUM

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Session III: Strategies for Competition Advocacy

-- COMPETITION ADVOCACY IN COLOMBIA--

1. Introduction

1. I wish to thank the OECD, the Inter-American Development Bank and the Competition Advocacy Commission of Costa Rica (Coprocom) for their kind invitation to participate in this forum, convened for the purpose of debating strategies for competition advocacy.

2. With a view to this debate, the OECD has suggested a number of questions to guide participants' contributions. It also urged us to comment on additional aspects resulting from each country's experience.

3. Within this frame of reference indicated by the organisers of the forum, the Superintendency of Industry and Trade (SIC) of Colombia offers some thoughts in response to the questions suggested. In the first place, we shall comment on the guidelines we have proposed to give certainty to regulators and to the SIC as to the conditions and procedures applicable for use of this instrument. Discussion on this proposal has moved forward significantly, delineating the scope that the instrument should be given in practice within the country's institutional organisation. Second, and although advocacy work has been underway for only one year, we have already issued opinions on draft regulations dealing with different sectors of the economy. Thanks to this effort we have learned some lessons that we consider useful to present as a contribution to this forum.

2. Adoption of advocacy

4. Competition advocacy was not an express function of the SIC or of any other authority in Colombia until July 2009. The SIC was responsible for advising the national government and helping to formulate policies on consumer protection, competition promotion, industrial property and other matters within its jurisdiction. That function continues to be one of the tasks of the SIC. Although its scope was different from that of competition advocacy, the fact is that, in pursuit of its functions and even before it adopted advocacy, the SIC occasionally offered opinions on the potential competition effects of draft laws at its own initiative.

5. Upon approval of Law 1340 of 2009 by the Congress at the initiative of the national government, the SIC was recognised expressly as the only competition authority in the country, and as part of that central mandate it was given the power to conduct competition advocacy in all sectors of the economy.

6. That law signalled two central aspects of competition advocacy. In the first place, it provided that the SIC is the authority that must exercise it, that its role is to consider proposed regulations that the government authorities intend to adopt through administrative acts, and that it should issue opinions, which would be nonbinding on regulators. In the second place, it provided that the authorities proposing a regulation must inform the SIC, but left it to the SIC's discretion to render an opinion or not.

7. As adopted by the new law, this function implies assessing proposed regulations in order to determine what impact they may have on free competition. Advocacy, then, is not applicable to regulations already issued.

8. The law intended that an authority such as the SIC, which has no legal mandate to promote sectoral interests, should through its opinion help ensure that economic regulation promotes free market participation by businesses, the efficiency of the economy as a whole, and the general welfare of consumers.

9. As to the optional nature of this responsibility for the SIC, we should note that this allows the competition authority to focus on examining draft regulations that it considers most significant for their impact on free competition.

10. This legal framework for advocacy, it must be recognised, did not concern itself with such aspects as criteria for assessing the impact of a regulation on free competition or the procedures for interaction between regulators and the SIC.

11. A legal framework such as this, flexible in some aspects and restrictive than others, requires guidelines. The SIC has presented a proposal to this effect, which has not yet been adopted. However, as noted below, public debate on this proposal has helped establish the limits and possibilities of developing this mechanism. For this reason, we consider it timely to describe for this forum some of the most important aspects that have arisen as part of this public debate.

3. Public debate on the proposed guidelines for competition advocacy

12. To ensure that regulators and the SIC alike have certainty as to the scope of competition advocacy, the proposed guidelines seek to lay the basis for interaction between regulators and the competition authority. To this end they strive for clarity as to what the authorities must report about their draft regulations, it establishes applicable criteria for identifying how a regulation may impact free competition, it includes some exceptions to the duty to report, and it determines the procedure by which those effects must be assessed.

3.1 Regulatory instruments subject to advocacy

13. According to Law 1340 of 2009, the duty to report to the SIC is applicable for drafts that the authority seeks to adopt through administrative acts. Advocacy, then, does not cover regulations adopted by law.

3.2 Authorities that must report to the SIC

14. The law establishes that competition advocacy may be applied to draft government regulations. As highlighted during the public debate, this concept embraces regulations issued by the national, departmental or municipal authorities.

15. The proposed guidelines require that the SIC be informed of proposals by the national authorities. This scope is explained by the fact that regulatory powers in economic, social, environmental and health matters are assigned primarily to national authorities. Thus, the SIC may focus its available resources for competition advocacy on examining regulations that may affect markets at the national level. This does not prevent it from extending its purview to draft regulations proposed by departmental or municipal authorities.

3.3 Criteria for identifying an undue restriction on free competition

16. The proposed guidelines establish that the authorities must inform the SIC of draft regulations that have the object, or could have the effect, of limiting the number or variety of competitors in one or several relevant markets. They must also report on those proposals that would define or change the conduct required of firms or consumers, when their purpose or their possible effect is to limit the capacity of firms to compete, or when they would reduce incentives to compete or limit free choice or information for consumers. These assessment criteria have been proposed in light of OECD recommendations in this area.[1]

17. During the process of public consultation it was argued that in some economic sectors, such as finance, insurance and securities, these criteria could be found inapplicable for assessing the impact of regulation on free competition. For that reason, the proposed guidelines provide that if an authority considers those criteria inapplicable, it must explain the reasons underlying that conclusion. If the SIC finds that conclusion substantiated, it will conduct the assessment bearing in mind the potential impact on market structure, the competitive process or consumers in the relevant market or markets in which those effects could occur.

3.4 Regulations excluded from advocacy

18. The proposed guidelines would exclude certain draft regulations. During public debate on the proposal some sectors maintained that exceptions were necessary to ensure certain public policy goals, such as stability of the financial sector. Conversely, other commentators insisted that exceptions could make the advocacy mechanism inapplicable at the whim of the regulator.

19. The proposed guidelines require the regulator to substantiate the requested exception. Thus, advocacy cannot be declared inapplicable in the absence of substantiation. In fact, one of the exceptions applies to regulations that have their origin in unpredictable or irresistible events that make regulation necessary on a temporary basis in order to preserve the stability of the economy or of the sector or to guarantee security in the supply of an essential public good or service. Only if a regulation is temporary,

[1] OECD Competition Assessment Toolkit, Version 1.0, 2007, available at the OECD webpage.

and adopted in response to extreme situations, will the regulator be released from assessment of its competitive impact. But when the restriction is permanent, it must be reported to the SIC.

20. Another exception is the act by which an "exclusive service zone" is established, in order to extend public utility services to low-income persons. This is the case with water and sewage systems, environmental sanitation, domestic distribution of gas and electricity. In practice, few such exclusive zones have been created. In any case, they can only be created by decision of the competent authorities through a process of competitive selection of the service provider. Before that process begins, the regulator has the duty to verify that the extension of service is the motivation for its creation.

3.5 Procedure for selecting draft regulations

21. The proposed advocacy guidelines recognise that the SIC does not have to be informed of every proposed regulation. As part of the public debate, some sectors held that the SIC should consider all proposed regulations. By contrast, others maintained that examining all drafts would prevent the SIC from issuing timely opinions, as the work burden would be excessive for the SIC and the regulatory authorities alike.

22. The proposed guidelines provide that if a regulator concludes, after the assessment that must be conducted on the basis of the objective criteria indicated above, that an administrative act will have an impact on free competition it must report it to the SIC. In particular, the regulator may only refrain from reporting if that assessment shows that the draft contains no undue restriction on free competition. To that end, the proposed guidelines consider that there is no such restriction when the response to a set of questions contained in the assessment questionnaire is negative. To refrain from reporting a draft regulation, then, cannot be simply the result of subjective considerations of the regulator.

23. In turn, when the response of the regulator to any of the key questions contained in the questionnaire is affirmative, before sending the draft to the SIC the regulatory authority may amend it or consider other regulatory options. In one case or the other, the regulator must offset or mitigate the restrictions on free competition in ways that will achieve the proposed regulatory purposes but will place fewer restrictions on free competition in the relevant market or markets where the act could produce effects.

3.6 The regulator and the competition authority must conduct separate but complementary assessments

24. The regulatory authority will conduct its examination of the draft before the SIC does so. The proposed advocacy guidelines provide that, when a draft is reported, the regulator must submit to the SIC the study it has performed to respond to the questionnaire, as well as any observations received during public consultation on the draft.

25. That consultation may provide the SIC with elements of judgment as to the restrictive effects on competition identified by the targets of the regulation themselves. In turn, the study conducted by the regulator must involve a serious evaluation. In any case, public observations and the regulator's study do not absolve the SIC from making its own assessment.

26. The proposed guidelines create several means for ensuring that regulators will take into account the opinions of the SIC. In the first place, they must keep a record of whether they have consulted the SIC or not. Second, they must indicate in their own administrative act whether the SIC has issued an opinion. Third, they may deviate from the SIC's opinion, but they must explain the reasons for doing so.

3.7 Advocacy and co-operation between authorities

27. In summary, to identify and minimise unduly restrictive effects of regulation on free competition, the proposed guidelines seek to encourage cooperation between the regulator and competition authority.

28. The regulator must assess the draft regulation during the preparation stage, and must substantiate that assessment. This stage includes procedures for public consultation on the draft. That procedure ensures that the SIC will have access to the suggestions and observations of consumers and businesses, as well as other authorities.

29. It is only after that assessment and public consultation that the regulator must report to the SIC on the draft, so that it may issue an opinion. Consequently, when the SIC conducts its own assessment it may have access to useful elements of judgment from interested parties themselves. In particular, the regulator's study must indicate the policy purposes pursued and the manner in which they are to be articulated with free market participation, consumer welfare, and economic efficiency.

30. Cooperation between the SIC and the regulators flows from a constitutional provision in Colombia, under which the defence of competition is not assigned exclusively to the competition authority. For that reason, both the SIC and the regulatory authorities must participate in evaluating the potential anticompetitive effects of a regulation.

3.8 The role of advocacy on proposed regulations

31. The OECD suggested examining the function that conducts advocacy in our countries, in two contexts. First, in relation to restructuring programmes that imply the industrial reorganisation of a sector and the establishment of the basic regulatory groundwork. The OECD suggests comparing that role with the one played by advocacy in respect of proposed regulations that simply develop the functions assigned to regulators as part of the initial restructuring.

32. As competition advocacy in Colombia is conceived, it is applicable in both these contexts. However, the main restructuring programmes were carried out in the last decade, in sectors such as public utilities, banking, health and ports. At that time the SIC did not have a competition advocacy function.

33. For this reason, the kinds of proposals on which the SIC has issued opinions during the year since competition advocacy was introduced in Colombia relate to simple developments of basic policies adopted by the country some years ago.

4. The application of advocacy

4.1 General characteristics

34. To date we have had the opportunity to examine proposed regulations in six sectors of the economy. These include 14 proposals relating to electricity and gas generation and marketing in the wholesale market; seven in telecommunications; five in water and sewage services; two in food and hygiene; two in the marketing of air travel tickets; one relating to technical conditions for gas transportation; one on the handling of subsidies for the provision of health services; and one on batteries.

35. The regulatory proposals examined refer primarily to two types of regulation. First, economic regulation of public utilities and the prices of air tickets; second, regulations that establish technical conditions for the protection of consumer health.

36. Of all the proposals that the SIC has assessed, only in one case did it find the possibility of restrictions on competition.

37. The bulk of proposed regulations in the various sectors have not been reported to the SIC. This is explained largely by the fact that the proposed guidelines on advocacy, described above, have not yet been issued.

38. The fact that only one proposal out of 34 has been considered by the SIC to be potentially restrictive of free competition shows that regulators are assessing the competitive impact of their regulations. As a result, they have attempted to achieve public policy objectives with the least possible restriction on free competition.

4.2 Some concrete cases

4.2.1 Administrative tariff for the sale of air tickets by Internet

39. The Civil Aeronautics Administration, the authority responsible for air transport in Colombia, reported to the Superintendency on a proposed regulation that would establish an administrative tariff or fee for the sale of air tickets via Internet.

40. In 2006 it established an administrative tariff for the in-person purchase of tickets, one which differed from that applicable to Internet purchases. In the first case, the tariff was mandatory, in order to do away with the management fee that airlines were paying to travel agencies. In the second, airlines and travel agencies can set their own tariffs without being subject to the limits fixed by the authority.

41. The proposed regulation sought to impose an administrative tariff for the sales of tickets through Internet. The tariff for 2010 was established in a range between 5,000 pesos and 38,800 pesos, for air tickets within the country, and between US$5 and US$95 for international flights. This regulation sought to ensure conditions of equality on the air tickets market, recognising the growing use of the Internet as an alternative channel for selling tickets and the user fee that airlines were charging for using that channel.

42. The SIC considered that the establishment of this tariff could lead to higher prices for the final consumer, with no clear justification in terms of economic efficiency. In this case the SIC held as follows:

> *"In general, from the viewpoint of the effect on competition and according to economic theory, the regulatory measures that the Civil Aeronautics Administration must take should be designed to regulate the tariff system in those situations where there is not sufficient competition, where there is a market failure, or where the quality of services offered is not up to the required levels.*
>
> *State intervention in the transport sector is justified by its nature as an essential public service. However, that sector is also governed by the principle of free enterprise, and the Aeronautics Authority has issued various resolutions prohibiting agents from engaging in anticompetitive practices. For the airlines in particular, they are expressly prohibited from discriminating among purchasers, when the purpose or effect of such conduct is to reduce competition or restrict access by travel agencies to the market.*
>
> *With respect to the market for air transport services, the evidence suggests that travel agencies can compete with the airlines. In fact, according to market data supplied by the Civil Aeronautics administration, in 2009 the travel agencies were the biggest channel of distribution for the sale of air tickets: 61% of tickets were sold by agencies and only 39% by the airlines. It is not clear that use of the Internet has affected the situation significantly, since the share of ticket sales through this means is marginal, according to data provided by the Aeronautics Authority in its communication.*

Nor is it to be expected that use of the Internet will have anticompetitive consequences in the future. It is true that Internet platforms have made it simpler to search and compare prices and, accordingly, the differentials in the prices paid by comparable users have been reduced, reflecting greater competition in the market. However, the competitive advantages that the Internet may represent are the result of an innovation in this sector which favours the market, i.e. they are a manifestation of legitimate competition and not of unequal conditions. If the added value of face-to-face intermediation is sufficient – if, despite the existence of the Internet, the cost of searching prices is very high or the differences between prices are great – the agencies will enjoy demand for their non-virtual services. On the other hand, if Internet platforms are an adequate substitute for the search service – and thus if they are also a mechanism for promoting competition between airlines – then the travel agencies can implement these technologies or find a way to differentiate themselves to constitute an option adding value to their services. This consideration is consistent with the gradual reduction of the marketing commission for air transport services, which has been underway since 2006.

The fact that some airlines are not charging additional tariffs for tickets sold online, while others are doing so, as the Civil Aeronautics Administration mentions in its request for a decision, can be explained in light of the relevant cost structure. The administrative tariff in question must depend on the costs of processing and issuing tickets via Internet, and those of implementing and maintaining Internet platforms. To the extent that these platforms offer economies of scale, the observed pattern of additional charges is justifiable, as the costs of each agent may vary, depending on the current technological conditions of the airlines or the travel agencies. Different airlines have in fact already made the investments needed to implement the infrastructure and platform for offering such services. That is, for those agencies that have implemented the technology and recovered their costs, or are enjoying economies of scale, the resulting tariffs may be close to zero. In fact, we understand that this is already the case, according to evidence from the Civil Aeronautics Administration in its communication.

In conclusion, after analyzing the conditions and dynamics of the sector on the basis of the elements of judgment proposed by the Civil Aeronautics Administration, we see no convincing evidence that, from the viewpoint of free competition, would support setting a floor under the administrative tariff for sales via Internet. In light of the available information we consider that a measure of this kind could lead to higher prices for the final consumer without any justification in terms of economic efficiency.

Measures such as Resolution 890 of 2010, which seeks to guarantee access for travel agents to the tariffs that the airlines offer directly to the public, generate transparency in the market and are more suitable for fostering equality of conditions among agents participating in it.

Notwithstanding the foregoing, it is possible that subsequent analyses may show that the market for sale of air tickets via the Internet presents market failures because of problems of asymmetrical information and price discrimination. If this were to be the case, we consider that an alternative for regulation could be to design mechanisms that encourage travel agencies to update their technological platforms, consistent with current market demands, as foreseen in article 2 of Resolution 890 of 2010."

4.2.2 Conditions of access and use relating to essential facilities in television broadcasting

43. The National Television Commission (CNTV) advised the Superintendency of a proposed regulation to regulate the conditions of access to and use of public and private network infrastructure for television broadcasting.

44. This measure sought to introduce competition in the television market by allowing free access to essential facilities, which would have to be remunerated. However, this posed two fundamental problems. First, the proposed regulation did not determine what should be considered a reasonable profit from remuneration for access to essential facilities and networks. Second, it gave the SIC the power to settle disputes over remuneration. In this case the SIC held as follows:

> *"1. Although the regulation proposed by the CNTV is a measure that seeks to introduce competition in the television market, particularly in those portions of the network that are considered unattackable, there must be a recommendation about remuneration. To avoid ambiguity in application of the rule, certain parameters must be set to determine what is understood by 'reasonable profit'.*
>
> *Definition of this aspect is important in order to avoid any discretion in setting the price of access, which could possibly lead to the setting of an inefficient price and violation of the principle of non-discrimination among agents participating in the market.*
>
> *2. The proposed regulation provides, in article 6, a procedure for settling disputes over the conditions of access and/or remuneration thereof, and gives the SIC the competence to resolve them when they may involve anticompetitive conduct.*
>
> *On this point, it is important to differentiate disputes over access from practical restrictions on competition. The first has to do with a specific question inherent in the ex ante regulatory function, relating to the application for access that an operator submits to the owner of a network deemed essential, where disputes generally arise over such matters as pricing or tolls, conditions of interconnection, or denial of access, and they are bilateral in nature. The second refers to anticompetitive acts or agreements, abuse of dominant position, which are analyzed in relation to the impact on the market in general and on the development of the ex post control function, which falls to the competition authority.*
>
> *In this respect, we suggest eliminating article 6 because it could exceed the powers of the CNTV by assigning to the SIC functions that can only be established by the competent authority through rules with higher rank."*

4.2.3 Electrical interconnection with Panama

45. The regulation was intended to establish a regulatory framework for international energy trading and reliability between Colombia and Panama and to facilitate coordination of interconnections between Colombia and Panama with the MER (Regional Electrical Market in Central America).

46. The SIC considered that this proposed regulation would promote competition in the sector, increase the number of participating agents, and would have the effect of reducing the final price of energy by promoting a greater number of suppliers. It consequently held as follows:

> *"International energy trading, such as that proposed between Colombia and Panama, is beneficial to the national economy and promotes competition in the sector, bearing in mind that it will: (i) boost demand among large consumers; (ii) promote the marketing of energy through a greater number of agents; (iii) encourage investment, through signs of growth in the generation and transmission activities; (iv) optimise use of existing infrastructure with robust interconnected regional systems; (v) optimise use of energy resources, creating security and reliability in the supply of electricity at efficient prices and lower costs; (vi) increase the supply of energy, through a greater number of generating plants.*
>
> *Nevertheless, in order to achieve the interconnection and its benefits, the authorities of the two countries must make coordinated efforts to harmonise regulation on either side, and make it*

compatible with the interconnection system. This is not an easy task, bearing in mind the different characteristics of the markets involved.

Some of the most important differences between the systems in the two countries are these: (i) dispatch and time zones – dispatch is weekly in Panama and daily in Colombia, and the time difference between them affects Panama's coordination with the Central American market; (ii) the difference in markets – the Panamanian market is cost-based and the Colombian market price-based; (iii) in Panama power can be traded as a product (like energy) and in Colombia this is a payment that is made to the generators.

The proposed regulation deals with the first two questions indicated above, although it requires further development. As to the last question, the contents of the operating agreement that the CND will sign with its Panamanian counterpart, and which will be subject to approval by the CREG in a separate decision, will be very important."

47. In short, the last two proposals were considered pro-competitive because of their effects on market access and the possibility of increasing the number of competing suppliers. On the contrary, the first was considered to restrict competition by affecting the price.

48. It is important to note that, by law, the SIC's opinion with respect to competition advocacy is not binding on the regulators. But if the regulator deviates from the opinion it is obliged to explain the reasons for its decision. In addition, the proposed guidelines provide that the SIC may publish its opinions and that the regulator must keep a record as to whether it has consulted the competition authority and the contents of the opinion issued by that authority. Once the guidelines are adopted, this type of mechanism could lead regulators to be more rigorous in assessing the impact of a regulation on competition.

5. Conclusions

- To achieve effective cooperation between regulators and the competition authority, we consider it necessary to establish an express framework for interaction that will create conditions that give certainty in the application of competition advocacy.

  Certainty over the conditions and procedures of such interaction will allow the competition authority to focus its advocacy efforts on regulations that could have a greater impact on free competition.

- The assessment of the competition effects of proposed regulations, which must first be made by the regulator and subsequently by the competition authority, can help those bodies achieve the policy objectives they are pursuing with the fewest possible restrictions on free competition.

- The lack of such a regulatory framework has limited the practical application of competition advocacy.

- There are some measures that can contribute to the effectiveness of competition advocacy. First, the publication of proposed regulations. Second, the publication of opinions issued by the authority. Third, the regulator must be required to keep a record as to whether it has consulted the competition authority, and the thrust of the opinion it has issued.

  We consider that the effort to create conditions for certainty between regulators and the competition authority as to the conditions and procedures for assessing the competition effect of regulations constitutes a means for achieving consensus on application of such assessment, especially when, under the country's legal system, the task of defending competition is shared between regulators and the competition authority.