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LATIN AMERICAN COMPETITION FORUM

-- Session III: Strategies for Competition Advocacy --

Contribution from Spain (CNC)

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

The attached document from Spain 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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LATIN AMERICAN COMPETITION FORUM

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Session III: Strategies for Competition Advocacy

-- CONTRIBUTION FROM SPAIN (CNC)¹ --

1. Advocacy in the Framework of the Protection of Competition Act

1. Spain's Law 15/2007, the Protection of Competition Act (Ley de Defensa de la Competencia, or LDC) charges the National Competition Commission (Comisión Nacional de la Competencia, or CNC) not only with consistent enforcement of legislation designed to protect and guarantee the competitive functioning of markets, but also with promoting effective competition in all productive sectors and throughout the national territory.

2. Its advocacy activities include:²

- Producing general reports on sectors and markets, as well as reports on government action – including public assistance – that could impede effective competition in markets.

The CNC is responsible for analysing the criteria applying to such assistance, and has an information system that keeps it abreast of the principle assistance packages granted in Spain. Furthermore, the Commission is required to issue an annual report on instances of government assistance (LDC, Art. 11).

¹ The CNC (*Comisión Nacional de la Competencia* or National Competition Commission) is the Spanish National Competition Authority.

² LCD, Art. 26.

- Proposing regulatory and normative changes for government agencies in order to remove restraints on competition, and developing policy guidelines for the Ministry of Economy and Finance so as to ensure that competition is protected when designing economic policy.
- Co-ordinating with sectoral regulatory agencies, and co-operating with the relevant bodies of the autonomous communities as well as with the relevant jurisdictional bodies, in order to ensure consistent enforcement of competition law and regulation throughout the nation.

3. Co-ordination with the authorities of Spain's autonomous communities relies on various instruments, including periodic meetings of specific working groups, and use of the computer application known as the Spanish Competition Network (Red Española de Competencia, or REC). Through this network, the various authorities provide their counterparts with reports on their competition advocacy, as well as providing other information relevant in their opinion to the functions for which they are responsible.

2. Advocacy Activity

4. The advocacy activities of the CNC principally take the form of various types of reports. These include sector studies, reports on normative proposals and reports on government assistance packages, all of which help to make firms in the sectors involved aware of practices that may limit competition. The Commission also provides recommendations to help public agencies maximise the pro-competitive character of their market interventions.

5. The present document focuses on two aspects of the questions set forth in the call for contributions for this Latin American Forum: (1) the advisory role of the CNC as it relates to issues of competition involved in legislative proposals of both central and regional governments, and (2) the activity that the Commission engages in to promote a culture of competition in general.

2.1. Sector Studies

6. Since its creation, the CNC has issued numerous reports on competitive conditions in a wide range of sectors and activities, including professional services, rights to broadcast football games, fuels, quality and safety certification standards, telecommunications, merchandise transport and intellectual property rights.

7. The Commission's most recent studies include a report published a few months ago on competition as it relates to the agrifood sector. In that report, the CNC explained its position on the current debate regarding the extent to which the activity of the first link in the agrifood chain (agricultural producers – whose functioning is shaped by sector-specific normative provisions of the European Community as set forth in the European Union's Common Agricultural Policy, or CAP), might be exempted from strict enforcement of competition rules. The Commission reiterated its opinion that the current framework for the applicability of competition rules to agricultural producers should continue to govern the sector's activity. The report adduces various arguments in support of this position.

8. On one hand, the Commission maintains that the rationale for exempting the agricultural sector from enforcement of competition rules is insufficient. Under the principle of free enterprise enshrined in Article 38 of the Spanish Constitution, government intervention to exempt a particular economic activity from competition rules is justifiable only when needed to correct market failures inherent to a sector's functioning, or to achieve other public objectives. Such market failures do not seem to be present in the agricultural sector to an extent that prevents free competition, especially if the sector is regarded as a whole. Nor, if there are indeed such market failures, would exempting the sector's operators from competition rules be the regulatory response best calculated to improve the market's functioning.

9. Also, setting minimum prices or providing anti-competitive profit guarantees for producers as a way of seeking public objectives such as food security, conservation of the rural environment or environmental protection in general would be disproportionate strategies when measured against the harm done to consumers by higher prices and by the possible erosion of agricultural product quality. Such action would also create disincentives to the sector's improved functioning and innovation, not to mention the fact that it would be discriminatory vis-à-vis other sectors.

10. The CNC analysis points out that there is a wide range of instruments that government and private-sector operators can employ to address the problems of agricultural producers without eroding current pro-competitive regulations. For example, under certain conditions, promoting co-operatives, making formal contractual arrangements between producers and clients a more universal practice, and establishing codes of conduct along with instruments to ensure compliance, can be effective ways of guaranteeing appropriately ordered relations between producers and the rest of the economic agents in the chain without jeopardising competition protections.

11. Another sector that has been the object of special attention by the CNC is intercity bus transportation, which the Commission has been studying since the 2008 publication of its report on the subject ("Competencia en el transporte interurbano de viajeros en autobús en España"). The report suggests a general approach to models of intercity transport, proposing one based on open access to the market for authorised operators, and on competition for the market through bidding for concessions.

12. Within the concessional model, which is the one currently in effect in Spain, the report points out some very serious restraints on competition in the behaviour of public administrations, such as the quasi-automatic extensions that some of the autonomous communities have granted (see below). It also analyses the protocol designed to support the upcoming renewal of 107 state concessions in the coming years. These concessions are based on agreements signed by the Ministry of Development and various sectoral associations.

13. Although the report acknowledges that the protocol is more pro-competitive than simple automatic extension of concessions would be, it warns that there are still serious deficiencies as regards protecting competition in the proposed future design and organisation of competitive bidding for concessions. Specifically, this is a consequence of the fact that both the law and the corresponding regulations give the current beneficiary of a concession a "preferential right" to renew the concession. The criterion is that when the value of the current concessionaire's bid and that of another bidder are "similar" (i.e., when the current concessionaire's bid is no more than 5% less than the highest bid), an extension of the concession is granted to the current holder.

14. The report also points to the need for changes in the weighting of factors when evaluating competitive bids. This includes increasing the weight of variables important to consumers, such as price and frequency of trips, and decreasing that of currently highly weighted factors associated with a variety of sectoral policy objectives. The pre-emptive "preferential right" of current concessionaires also functions as a major distorter of competitive market functioning.

15. Following the introduction of various changes in the sector's regulations, and decisions to renew a number of concessions, the CNC decided to follow up with two more reports on the sector, one focusing on the national level, and the other examining developments in the autonomous communities.

16. The follow-up report on the renewal of intercity bus transportation concessions, which was published in the spring of 2010, provides a new assessment of this sector's competitive conditions in the wake of the changes in the protocol that were introduced as a consequence in part of the previous CNC report.

17. In general, the CNC considers these latest changes inadequate, especially as regards the design of forms for competitive bidding, which are highly unsatisfactory from a competitive point of view. The Commission's report analyses the 14 competitive bidding events carried out to date (both prior to and following the publication of the 2008 report), and their results corroborate the fears expressed in the 2008 report. Thus, both the modified version of the protocol and the old one are deficient in their competitive structure.

18. Consequently, the CNC proposes that before undertaking the renewal of the bulk of the concessions for which the Ministry of Development is responsible (which is scheduled to begin in 2012) new in-depth changes be made to the protocol to enhance the competitiveness of the bidding process, following recommendations that to a large extent reiterate those embodied in the 2008 report. The recommendations call for eliminating the "preferential right" of current concessionaires whose bids are "similar" to those of competing entities; granting greater weight in the overall evaluation of bids to the two principle variables affecting consumer decisions (cost and frequency of service); modifying the existing mechanism that caps scores; and respecting the maximum timeframes for concessions contemplated in the EC normative structure, as well as linking those timeframes with the amortisation period of the investments needed for the activities connected with a concession.

19. The CNC follow-up study on the concessions of the autonomous communities, described in a report on the extensions of intercity bus transportation concessions controlled by the autonomous communities, showed that, in the overwhelming majority of cases, the mechanisms in place provide nearly automatic renewals of these concessions to their current holders without public bidding, through various existing regulatory instruments.

20. The CNC believes that these standards for prolonging the duration of current concessions constitute a serious restraint on competition. In practice, such extension closes the market to competition during the entire period for which the concessions are extended, since the right to engage in the activity is exclusive, and no sufficient rationale has been adduced to show that such renewals are needed to achieve the relevant objectives described in the regulatory documents of the autonomous communities.

21. Thus, it is not clear that there is an imminent risk of cessation of service if these concessions are not extended. Nor, in most cases, is there a relation between the time needed to achieve improved service objectives and the time for which a concession is extended. This casts doubt on the connection between the objective and the extension mechanism. At times, absolutely disproportionate extensions are granted, covering more than 10, or even 15, years in addition to the duration of the original concession – which in many cases was not subject to competitive bidding. Moreover, the criteria for granting extensions do not normally take account of significant differences of contemplated revenues or passenger miles between different concessions. Thus, extensions are available in all cases.

22. Given the lack of response to the Commission's communications and to its calls for rules changes in the autonomous communities, and given the sector's importance and the existing mechanisms' distortionary impact on competition of the existing mechanisms, the CNC has decided for the first time to make use of the legal standing that it has under Article 12.3 of LDC 15/2007 to file two adversarial administrative appeals. It will thus be contesting sectoral rules on the extension of bus concessions in Valencia and Galicia, invoking the arguments previously set forth in the above-mentioned report on extensions in the autonomous communities.

23. This legal instrument, which is one of the most significant innovations of the LDC, gives both the CNC and all autonomous community competition authorities the ability to contest administrative acts and regulations at a sub-legislative level if these involve the creation or reinforcement of obstacles to

competition.³ Underlying this legal instrument is the legislature's recognition of the importance of jurisdictional protection of the general interest (competitive conditions) that these authorities are mandated to defend even when it conflicts with the other general interests that the government is charged with safeguarding. Ultimately, this legal instrument is one additional guarantee of free enterprise in a free market framework, in accord with Article 38 of Spain's 1978 Constitution.

2.2. Reports on Normative Proposals

24. As indicated above, the CNC is authorised to issue non-binding reports on the competitive impact of regulatory changes proposed by government.

25. Among the most recent reports on such proposals is a royal decree (RD) creating a procedure that would permit restrictions on competition in order to ensure supply. It provides preferential treatment for domestic coal used in electrical generation.

26. The decision to encourage the use of Spanish coal for electrical generation is based on the importance of keeping domestic fuels options open, as well as on the importance of domestic coal generation plants, in the belief that both of these factors contribute to the system's reliability and proper operation, and to the functioning and reliability of the electrical supply, the ultimate goal being to ensure the supply of electricity to consumers. The preferential treatment for domestic fuels is in all cases capped at 15% of the total primary energy under Article 25.1 of the Electrical Sector Act (Ley del Sector Eléctrico), and the National Strategic Coal Reserve Plan 2006-2012 (Plan Nacional de Reserva Estratégica de Carbón 2006-2012).

27. These rules have emerged in the context of the sharp reduction in demand for coal for electrical generation, which is due, among other things, to a very significant drop in electrical demand and to the development of new generation technologies, including renewable energy technologies in particular. The result is a large surplus of domestic coal that cannot be absorbed by the country's energy producers.

28. In addition, the RD establishes a new adjustment mechanism in the electrical market, the "procedure to resolve shortfalls in guaranteed supply". This changes the results of the daily market clearing, withdrawing the production of certain thermal plants that has been cleared, and replacing it with the production of domestic-coal generating plants not cleared in the market.

29. Under this procedure, certain thermal plants in the regular regime will have to reduce their production schedule. The new system will impose reductions in descending order of the plants' levels of CO₂ emissions. Plants that suffer under this arrangement will be compensated for lost profits by a mechanism designed for the purpose.

30. The CNC concludes that the RD introduces significant distortion in the functioning of Spain's electrical generation market and its price formation mechanisms, and that it creates certain competitive inefficiencies and distortions that are unjustifiable and highly detrimental to the general welfare, since they raise the price of electricity in wholesale markets as a result of the alteration in the firms' comparative economic advantage and as a function of their increased operating costs. Consequently, the CNC recommends reconsidering this measure.

31. The CNC also warns that since the procedure to permit restrictions to ensure supply may possibly constitute governmental assistance as defined by TCE Article 87.1, the European Commission should be notified of the measure.

³ LDC, Art 12.3.

32. Another important recent report – on a normative proposal, at the behest of the Secretariat of the Economy – deals with a proposed royal decree on mandatory licensing by professional associations. This report supplements the broader studies on the provision of services and professional associations conducted in 2008.

33. The Commission's assessment of the proposed decree stresses the pro-competitive nature of the normative changes contemplated. By eliminating the mandatory requirement for licensing in approximately 70 activities where such licensing has not been shown to be necessary and commensurable with the need for regulation, the report says, the change would reduce administrative staffing needs and remove restraints on competition in a wide range of activities. This in turn will lead to monetary and administrative cost savings for citizens and firms, and provide a very significant stimulus to competition within professional areas. The requirement will remain, however, in 10 cases, including construction, blasting and demolition of buildings, manufacture and sale of explosives, mining resources and installation of telecommunications infrastructure.

34. Despite its praise for the reform, the CNC believes that it could have been more ambitious. Specifically, there is not sufficient rationale under the principles of good regulation for requiring a license granted by a professional association as a part of the formal review of the documentation of work (where such review is deemed necessary).

35. In the ten areas where licensing would still be required under the proposed decree, the report finds an avoidable duplication of administrative controls in certain types of work contracted for by government agencies outside the central government.

36. Also, licensing would continue to be mandatory for some types of work where either the relation between the work and the public interest has not been adequately demonstrated or licensing is a redundant mechanism.

37. A significant number of the Commission's recommendations on reducing the types of work still subject to mandatory licensing under the proposal were included in the RD that was ultimately approved.

38. As a supplement to its reports on specific normative proposals, the CNC has produced reports designed to facilitate legislators' assessment of proposed legislation in terms of its effect on competition. These include a 2008 report with recommendations to governments regarding more efficient and pro-competitive market regulation. The report makes it clear that an efficient normative framework must observe a number of principles designed to minimise obstacles to economic activity and impediments to competition in the marketplace. Examples of such principles are that regulations must be necessary and that they be in proportion to the regulatory objectives for which they are designed, that they must generate minimal market distortions, and that measures must be efficacious, transparent and predictable.

39. Along similar lines, as a source of advice to government, the CNC has published a guide for producing reports on competitive aspects of proposed legislation and regulations. The guide provides support in analysing and assessing legislative and regulatory proposals from the point of view of competition by considering the effects that their approval may have on free competition in the marketplace. It also points up that there are sometimes regulatory alternatives for a given objective that have less negative impact on competition than the proposed measures.

40. The guide presents a very simple evaluation scheme structured in three steps:

- Identify constraints on competition associated with the proposed measure. These may include such things as limitations on the number or variety of producers, constraints on their ability to

compete with one another, reduced incentives to compete and so on. When analysis of a proposal indicates that the proposal contains principles or mechanisms that could limit competition, it will be important to extend the assessment process.

- Justify constraints. The analysis here focuses on what the objective of a regulation is, and on the need and proportionality of the constraints that it introduces in pursuing its goal. If the constraints on competition created by a proposed measure cannot be justified, the proposal needs to be modified. If, on the other hand, the measure's need and proportionality can be demonstrated, attention must turn to whether it is correctly structured, and whether there is a regulatory alternative that is less competitively restrictive. This latter step is obligatory and points directly to the final step.
- Analyse regulatory alternatives. The goal here is to demonstrate that there is no alternative mechanism that would achieve the same objective without producing a negative impact on competition, or that would at least limit it less. If a less restrictive alternative is found, it should be adopted.

41. The need for competition-impact assessments of normative proposals was formally recognised by Royal Decree 1083/2009 of July 3, which regulates impact assessment reports on proposed normative measures.

2.3. Public Assistance

42. Beyond the question of their impact on the implementation of the EU Internal Market, the granting of public assistance in whatever form constitutes intervention in the economy and can alter the functioning of markets. At times, it can be detrimental to competition and, far from promoting the public interest, can be contrary to it.

43. The LDC has made it possible to strengthen and expand the functions of Spain's competition authority in relation to cases of public assistance, by making this area a part of the agency's competition advocacy functions. Thus, under the LDC, the CNC has issued reports on assistance regimes and on individual cases of assistance, as well as making recommendations to government on maintaining effective competition in markets. In addition, the Commission is required to publish an annual report on public assistance granted in Spain.

44. Analysis of cases of assistance must deal with both their legal and economic aspects, and may cover factors such as the strategic plan of which the assistance is a part, the regulatory basis for the assistance, and the positive and negative elements of the grant as shown by the so-called "balancing test".

45. Finally, it should be noted that a telematic information centre has been implemented to provide information on the national public grants of assistance published in official organs. The purpose of this is to supplement the registry of state-provided assistance kept by the European Commission.

3. A Culture of Advocacy

46. Competition authorities' advocacy activity should not be directed solely to legislators and government institutions. Efforts must be made to foster a true culture of competition in the society – first because this helps reduce violations of competition law in the private sector, and secondly because such a culture provides greater social support and legitimacy for the advocacy work that competition authorities conduct in the public sector.

47. Among the Commission's initiatives to develop a competition culture are its guide for professional associations ("Guía de Asociaciones Profesionales"), the purpose of which is to offer these organisations guidelines for their members' conduct. The stress is on the principal factors that should be borne in mind to avoid anti-competitive practices.

48. Given their nature as fora in which competing firms meet, business associations should be conscious of the fact that certain of their daily activities may violate pro-competitive laws, and that this can lead to large fines. The guide analyses the principle areas of problems for competition in the market, which include price decisions and recommendations, distribution of markets and other conditions of trade, boycotts, sharing of sensitive or strategic information among associated firms, advertising based on comparisons (among other types), standardisation agreements that unnecessarily introduce restraints on competition, and the establishment of model contracts that threaten the independence of economic operators or tend to make their conduct uniform.

49. From a more general perspective, advocating a culture of competition involves creating effective channels of communication across the society as a whole as broadly as possible.

50. The CNC communications policy includes publishing its texts and press releases on its website, along with all of its sectoral studies, reports on normative proposals, reports on public grants of assistance and guides of all types. Many individuals are registered with the website (attorneys and students, among others) to receive a monthly news bulletin from the CNC.

51. Visits to the CNC website, which are generally quite frequent, increase very noticeably with the publication of resolutions, reports and guides, which are usually announced through press releases sent to a wide spectrum of media outlets.

52. The information published on the website is in many cases available in Spanish and English.

53. The CNC has recently established a presence on the social medium Twitter, through which it hopes to facilitate access to competition-related news for a larger audience.

54. The President of the CNC plays a very important role in publicising the Commission's activity, functioning as its spokesperson in interviews with both economically oriented and general-interest media of all types (print, radio, television). This helps the Commission expand its audience.

55. Competition culture is also promoted by establishing collaboration agreements between the CNC and certain universities and public bodies. One of the most recent such agreements is that signed with the consumers' and user's organisation.