

**DIRECTORATE FOR FINANCIAL AND ENTERPRISE AFFAIRS
COMPETITION COMMITTEE****Working Party No. 2 on Competition and Regulation****Tools for addressing Competitive Neutrality – Note by Mexico****3 June 2019**

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1. Introduction

1. Competitive neutrality is a principle according to which all firms, public or private, domestic or foreign, national or local, should compete on the merits and should not benefit from undue competitive advantages derived from government's ownership or involvement in the marketplace, in fact or in law.¹
2. In this document, the Federal Telecommunications Institute (IFT, by its acronym in Spanish) describes the range of tools at its disposal to address competitive neutrality concerns arising from public ownership or interventions, as well as four recent relevant cases, regarding the telecommunications and broadcasting sectors in Mexico.
3. The IFT, as the national competition authority and sectorial regulator in telecommunications and broadcasting, employs competition policy, tools and criteria to assure that no public entity, regardless if it acts as a competitor, regulator, provider or customer, unduly benefits from its public nature.

2. The legal and administrative framework

4. In Mexico, the IFT uses the tools provided in the Federal Economic Competition Law (LFCE, by its acronym in Spanish) and the Federal Telecommunications and Broadcasting Law (LFTR) to protect and promote competition and the efficient development of the sectors.
5. The LFCE applies to “all economic agents” in “all sectors of economic activity” within the national territory.² The scope of application includes the State, its agencies, and all State-owned enterprises (SOEs) when acting as economic agents, i.e., when participating in economic activity, not acting as an authority or outside *strategic areas*.³

¹ See OECD (2015). *Competitive Neutrality in Competition Policy (Issues paper by the Secretariat)*. Available at: [http://www.oecd.org/officialdocuments/publicdisplaydocumentpdf/?cote=DAF/COMP\(2015\)5&docLanguage=En](http://www.oecd.org/officialdocuments/publicdisplaydocumentpdf/?cote=DAF/COMP(2015)5&docLanguage=En).

Also, see OECD (2018). *Scoping Note on Competitive Neutrality as a long-term theme for 2019-2020*. Available at: [http://www.oecd.org/officialdocuments/publicdisplaydocumentpdf/?cote=DAF/COMP/WD\(2018\)5&docLanguage=En](http://www.oecd.org/officialdocuments/publicdisplaydocumentpdf/?cote=DAF/COMP/WD(2018)5&docLanguage=En)

² Articles 1 and 3 of the LFCE.

³ Article 28 of the Mexican Constitution defines strategic areas reserved for the Mexican State: postal system; telegraphs and radiotelegraphy; radioactive minerals and generation of nuclear energy; the planning and control of the national electricity system, as well as the public service of transmission and distribution of electric energy, and the exploration and extraction of oil and the rest of hydrocarbons. These functions exercised exclusively by the State shall not constitute monopolies and, thus they are exempted from the LFCE.

6. In addition, LFCE's tools more effectively used to address competitive neutrality issues, when public entities act as a provider, customer or regulator, are:

1. To carry out special administrative proceedings to determine: i) the existence of essential facilities or barriers to competition and free market access, and (ii) market conditions (effective competition, the existence of substantial market power or other analogous terms);⁴ and
2. To issue its opinion or authorization in the awarding of licenses, concessions, permits, transfers or sale of shares, about concessionaires or permit holders, in terms of the provisions of the article 98 of the LFCE.

7. That is, the LFCE empowers competition authorities to assess and issue a non-binding opinion and recommendations to enhance competition about other authorities' acts and regulations, but it does not provide said authorities with the powers to mandate State legislation to be modified if it hampers competitive conditions.

8. In the previous LFCE (issued in 1992), the Federal Competition Commission (CFC, by its acronym in Spanish) was authorized to deal with anti-competitive government regulation in one circumstance that was where a state or local agency undertook to restrict interstate or foreign commerce. Article 117, section V of the Mexican Constitution reserves the regulation of such trade to the federal government and prohibits State interference. The 1992 LFCE's 14th article implemented this Constitutional provision by providing that "the acts of state authorities of which the direct or indirect objective is to prevent the entry or exit of domestic or foreign goods or services into or from the state's territory, shall have no legal force or effect." Although the CFC could not order the state to repeal the offending regulation, article 15 empowered it to declare that the regulation constituted an interstate trade barrier. This decision effectively made the regulation void under Article 117, section V, and private parties could then ignore that provision with legal impunity. This relevant power was left out in the new LFCE. Nowadays the IFT can only request the federal branch to promote an unconstitutionality action against the offending regulation.

9. The LFTR contains additional provisions for delivering competitive neutrality, since it:

1. Defines competition neutrality as the obligation of the State consisting of not distorting markets, when participating as entities' owner, and
2. Establishes a specific regime for SOEs (public entities or public private partnership/PPP) that obtain a concession to deliver telecommunications services with commercial purposes. Namely, under the sectoral law, SOEs:
 - Are subject to competition neutrality principles and restricted to provide wholesale services;
 - Must offer total infrastructure sharing, complete disaggregation of their services and capacities, competitive pricing and non-unduly discrimination;
 - Must carry separate accountancy for telecommunications and broadcasting activities;
 - Must submit to authorization all the agreements on capacity, infrastructure or services with preponderant economic agents; and

⁴ Articles 94 and 96 of the LFCE.

- Must issue public referential offers of its services.

10. Thus, in the telecommunications and broadcasting sectors, SOEs can apply for: i) public concessions granted to public entities to exercise their public duties, or ii) commercial concessions, therefore subject to a specific competition neutrality legal regime.

3. The role of the competition authority to ensure the level playing field in the telecommunications and broadcasting sectors

11. According to OECD, one reason for concern about State involvement in the marketplace is that this could blur the distinction between the State as a provider, a customer, and a regulator.⁵ This concern is particularly relevant since, as the OECD also recognizes, after the financial crisis, some countries have been taking a renewed interest in active industrial policy and the idea of an entrepreneurial role for the State.⁶

12. A public entity may participate in economic activities as an economic agent or as an authority.

13. When the public entity participates as an economic agent –a competitor– the LFCE handles its every move, treating said entity with neutrally and indistinctly as to all those other economic agents playing in the level field.

14. When the public entity acts as an authority, it can do so as a customer, a provider or a regulator. Each nature comes with unique qualities, and the IFT approaches them with unique policy tools and criteria.

15. When the State is the seller, it provides the market with a public resource, e.g., the spectrum in the telecommunications sector. On these cases, the IFT issues an opinion on the bidding rules to incorporate pro-competitive criteria and, before the bidding process starts, it assesses every interested candidate to approve their suitability, i.e., discard that its participation could hamper competition for the market or in the market. Such assessment assures a level playing field for all participants, as well as transparent and unbiased bidding processes.

16. When the public entities act as customers in public acquisitions, the IFT must enact its powers to issue non-binding opinions and, although force-limited, publicly state the competition authority's expert position in each tender, invitation or direct acquisition. The IFT must protect the constitutional principle of efficient assignation of public resources, acquiring at the best price and the best conditions.

17. Now, if the State is buying from an SOE acting as an economic agent, the IFT must issue its opinion carefully securing that said SOE will not take advantage of its position and that it holds a real ability to compete in the market in a viable and efficient manner.

18. When the authority acts as a regulator, the IFT must recommend, within its expertise, the best provisions, and standards to create a homogenous playing field, without favouritism or special treatment.

19. In Mexico, for several decades the State undertook a process of decreasing its direct participation in the production of goods and services, which even involved the reclassification of activities that were previously considered strategic to allow private

⁵ See OECD (2015). *Competitive Neutrality in Competition Policy (Issues paper by the Secretariat)*

⁶ See OECD (2018). *Scoping Note on Competitive Neutrality as a long-term theme for 2019-2020.*

participation. However, the emphasis has been placed recently on particular public objectives that require direct involvement of the State in the economic activity, for example, through public-private participation schemes.

20. The telecommunications sector is an example of those cases mentioned above, since the 2013 Constitutional Amendment on Telecommunications promoted the development of operators with public participation, as it is the case of the *Red Compartida* project, a wholesale shared network aimed at providing broadband coverage to 92.2% of Mexican population by 2024.

21. In this scenario, there is a need to strengthen the role of the competition authority to ensure that the State's involvement in the marketplace is consistent with competitive neutrality principles.

4. Case Study 1: Wholesale broadband shared network (Red Compartida)

22. One of the most important provisions of the 2013 Constitutional Amendment on Telecommunications is the Transitory Article 16, which contains the obligation to adjudicate by auction the *Red Compartida* project to a PPP, with no telecommunication service provider having any influence on its operation.

23. *Red Compartida* is then a project mandated directly by the Constitution and its main characteristics and obligations were determined by the legislative power, without the participation of the competition authority. The Legislative Branch expressed that this measure was adopted to tackle the severe challenges and limitations in the Mexican telecommunications and broadcasting sectors, which required taking direct and immediate solutions.

24. In this respect, in the Constitutional Amendment process, the legislature pointed out that the wholesale nature of the network guarantees the optimal use of the spectrum, ensuring that no service provider for the end user can influence the operation of the infrastructure for its benefit. Therefore, the competition generated by the virtual operators will allow transferring the efficiencies and savings of the shared network to the consumers.

25. Notwithstanding, when drafting the LFTR, the legislative branch recognized its duty to ensure that the granting of concessions to SOEs for commercial uses does not generate distortions in the market affecting private entities, but, on the contrary, it must enhance effective competition conditions. That is, the legislature recognized that the State must guarantee the competitive neutrality of its projects, and included a specific chapter in the LFTR that regulates the operation and objectives of those SOEs to which the IFT grants concessions for commercial use.

26. According to the legal framework, before the auction of the *Red Compartida* project in late 2016, the IFT issued a competition assessment to the interested companies to determine if they complied with the obligation of avoiding that any telecommunications operator got influence in the project's operation.

27. One of the evaluated companies (Rivada Networks) was subjected to conditions because one of its shareholders (EchoStar) was a telecommunications operator and its identified participation in the company could potentially get influence in the operation of the project. Because of this, the shareholding of EchoStar in the consortium was capped to 10%, with limited voting rights, and access restrictions to the project's operational information.

28. After the IFT completed the competition evaluation, the auction was issued, and the winner contestant was Altán Redes, which is currently designing, setting and operating the wholesale public network.

29. Its concession title contains the following provisions regarding transparency of its contracting activity with public authorities, to detect situations that could unduly distort the market:

- Altán Redes must inform the IFT within the first quarter of each year, and include in its annual financial statements, in a disaggregated manner, all contributions, supports, subsidies, and transfers it has received from public authorities after the signature of its concession title.
- Altán Redes shall submit annually to the IFT, within the first quarter of each year, detailed information on the procedures and conditions under which it enters into contracts or agreements with public authorities.
- If the IFT detects behaviors that unduly distort competition in the market, it may order the necessary measures aimed at preventing or correcting the identified distortions.

5. Case Study 2: Radio FM broadcasting service

30. According to the sectoral law, public concessions are granted: i) exclusively to governmental institutions and agencies to exercise their public duties (it contains a ban to obtain commercial gains or speculative profits); ii) directly and without compensation; and iii) with preference over third parties.

31. This includes SOEs not acting in commercial activities; thus, its operation is not subject to a specific competition neutrality legal regime. Notwithstanding, considering spectrum as a scarce resource, the IFT assesses, on a case-by-case basis, the possible effects of granting a public concession on:

- The availability of spectrum for alternative uses (especially commercial uses in highly concentrated markets) within the geographical market involved; and
- The accumulation of spectrum already in concession to the public applicant.

32. In particular, the IFT applies distribution and eligibility criteria when granting concessions to a SOE for FM broadcasting services, as a way to eliminate barriers to entry and to prevent from future competition distortions.

- The IFT uses distribution criterion to protect the efficient assignation of every type of spectrum uses, especially in the following circumstances:
- There is few spectrum availability in the geographical area evaluated;
- Other public entities uphold public concessions; and
- There is high potential demand for alternative uses in the same bandwidth and geographical area.

33. The IFT is aware of the opportunity costs involved in granting a frequency for a specific use and the respective reduction in availability for other commercial and non-commercial uses. Therefore, bearing in mind a balance in the alternative uses of the

spectrum for FM broadcasting services, the IFT uses a reasoning related to competition and opportunity costs to protect the inclusion and efficient distribution of each type of them.

34. The IFT uses eligibility criterion to choose the best positioned SOE when:

- Different SOEs are interested in the same location, and
- The availability of spectrum is limited.

35. In particular, a SOE with no previous concessions in a location might be considered differently over those who already have one or more concessions.

6. Case Study 3: Access to the poles and rights-of-way of the national electricity system

36. The IFT holds powers to issue an opinion when considered pertinent, or upon request, regarding proposed provisions, rules, agreements, circulars and other general administrative acts that are intended to be issued by public authorities, when these drafts could have adverse effects on free market access and competition in the telecommunication and broadcasting sectors. These opinions have no binding legal effects.⁷

37. In October 2017, the Energy Regulatory Commission (CRE, by its acronym in Spanish) asked the IFT for its competition opinion on the draft of the “General administrative provisions to allow access to telecommunications service providers that use the facilities and rights of way of the national electric system”.

38. Regarding competitive neutrality, CRE, in collaboration with the IFT, the Mexican Ministry of Transport and Communications (SCT, by its acronym in Spanish) and the Federal Electricity Commission (CFE, by its acronym in Spanish) established:⁸

- Objective criteria to determine the capacity of the poles, as well as the conditions to meet access requests and resolve in cases of shortages;
- The obligation of suppliers to provide access under not unduly discriminatory conditions and to refrain from unjustified refusals to deal;
- The neutrality and non-discrimination principles regarding discounts agreements; and
- Objective criteria (i.e. the weight of the installed infrastructure) to determine the monetary considerations

39. These Provisions were published in the Official Gazette of the Federation (DOF, by its acronym in Spanish) on October 2018⁹ and will allow telecommunications companies access to 11 million CFE poles throughout the country.

⁷ Article 12; section XIII, of the LFCE.

⁸ The competition opinion is available in Spanish at: <http://www.ift.org.mx/sites/default/files/conocenos/pleno/sesiones/acuerdolina/pift151117696.pdf>

⁹ Available at: https://www.dof.gob.mx/nota_detalle.php?codigo=5542320&fecha=29/10/2018

7. Case Study 4: Reduction of the restrictions on Foreign Direct Investment (FDI) in the telecommunications and broadcasting sectors

40. Mexico has made substantial progress in lowering the barriers to FDI since 2014. Since the Telecommunications reform in 2013, FDI is now allowed up to 100% in the telecommunications sector and up to 49% in broadcasting sector.

41. This means a relevant reduction of the distortions of competitive neutrality related to an excessively restrictive regulation. FDI inflow increases the economy's capacity to finance infrastructure's upgrades and rollouts, but also provides industrial development and trade opportunities due to additional financial resources, absorption of productive technologies and other factors.

8. Conclusion

42. The principle of competitive neutrality endorses the commitment of the State and authorities to oversee a fair play, i.e., a win-win situation for the market and its consumers. Competitive neutrality is a matter of interest for public policies, especially in the provision of public services such as telecommunications and broadcasting. The explicit enforcement of this principle assures that SOEs should not enjoy an undue competitive advantage or disadvantage simply because of their public bound. It also requires that the State, when acting as an authority, comprehends that private participants in a market have the right to compete on a neutral basis.

43. When applying this principle, the IFT relies strongly on competition law enforcement to address competitive neutrality concerns, given that the LFCE provisions apply broadly. Since IFT acts as both competition and regulatory authority in the telecommunications and broadcasting sectors, part of its advocacy efforts are directed inwards, to ensure that sectoral regulation promotes a level playing field and undistorted markets. External advocacy mainly consists of providing opinions and recommendations for SOE and other public authorities in enhancing competition and adopting competition neutrality principles.

44. Mexico lives today a pivotal change in its public policy's landscape. The role of the State in guaranteeing social welfare, within a market economy, is reshaping. The IFT sees the need to strengthen advocacy to enhance competitive conditions, level playing fields, and prevent any lack of neutral treatment. Its most useful tools on this area are the active collaboration with other public authorities and SOEs to share visions, approaches, experiences, and data to find out concrete and viable solutions, as well as the issuing of non-binding opinions and recommendations towards public entities and SOEs.