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LATIN AMERICAN AND CARIBBEAN COMPETITION FORUM

**Session I: Disruptive innovation in Latin America and the Caribbean:
Competition enforcement challenges and advocacy opportunities**

-- Contribution from Mexico --

12-13 April 2016, Mexico City, Mexico

The attached document from Mexico (COFECE) is circulated to the Latin American and Caribbean Competition Forum FOR DISCUSSION under Session I at its forthcoming meeting to be held on 12-13 April 2016 in Mexico.

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LATIN AMERICAN AND CARIBBEAN COMPETITION FORUM



14th Latin American and Caribbean Competition Forum 12-13 APRIL 2016, Mexico City, Mexico

Session I: Disruptive innovation in Latin America and the Caribbean: Competition enforcement challenges and advocacy opportunities

-- CONTRIBUTION FROM MEXICO (COFECE)*--

1. Introduction

1. In the business world and in the context of regulatory systems, it is now extremely common to hear that technological innovations are changing the way in which businesses offer their goods and services and, therefore, the way in which we consume them.

2. By definition, something which appears suddenly or is disruptive threatens the *status quo* in both economic and political terms. The characteristic elements of technological or disruptive innovations are therefore the transfer of control towards consumers, more accessible goods and services, and an increase in available options. In other words, disruptive innovations help to place **consumers at the heart of business strategy**, hence the great socio-economic value of innovation and the clear role the competition authorities are required to play.

3. The purpose of using mobile platforms, for example, is to facilitate exchanges of resources between individuals, and in fulfilling this goal they have offered a model for capitalising on underused goods. Businesses of this kind generate profits by charging a commission or fee for linking providers and consumers of a good or service through **collaborative consumption**, a phenomenon whereby individuals create and share goods, services, spaces and money.

4. In this context, collaborative consumption is defined as a socio-economic system based on the shared use of material and human resources, encompassing the creation, production, distribution, exchange and consumption of goods and services by different persons and organisations. These systems are variable

* Comisión Federal de Competencia Económica (COFECE) [Mexican Competition Authority].

and very often leverage information technologies to help empower individuals, companies, non-governmental organisations and government, allowing surplus goods and services to be reused.

5. Mobile platforms such as Uber, Airbnb and RelayRides facilitate exchanges of resources between individuals by linking the supply of a good or service to the demand for it, giving rise to:

- a reduction in transaction costs;
- better use of underused resources;
- an increased supply of goods and services.

2. Specific case of mobile app-based Transportation Network Companies (TNCs)

6. On the basis of the development of smartphone technologies and global positioning systems (GPS), a number of companies have recently emerged which act as an interface between transport service providers and users by means of mobile phone apps (Transportation Network Companies or TNCs).

7. Passengers use this type of platform to request mobility services via mobile apps on the basis of price, quality and number of drivers they can have access to. A pool of drivers meanwhile offers services by means of the same mobile app. Their decision to connect is therefore based on the prices, quality and number of users the app allows them to access.

8. TNCs have taken on two different forms since their creation:

- Supplementary platforms. These connect consumers of point-to-point transport services with taxi drivers already registered with the public service. Easytaxi and Yaxi are examples of these systems in Mexico.
- Independent platforms. These use an app to connect to drivers who offer their private services to consumers without being registered as part of the public taxi service. Uber and Cabify are examples of these systems in Mexico.

9. The use of mobile apps has become an efficient solution for correcting the **asymmetric relationship between drivers and passengers**, since: (a) routes are planned automatically by the mobile platform system, eliminating the possibility that drivers will go off-route and charge higher prices or fares; (b) some companies that provide this type of service have sought to offer consumers quality-oriented advantages such as ratings systems; and (c) clarity is ensured with respect to waiting times for starting journeys. This type of service has also improved the information available for drivers or service providers, thereby ensuring that supply is more consistent with demand over time and in different geographic locations. This is possible because these systems provide access to both historic and real-time information on the conditions of demand so that drivers can adjust their routes to maximise customer numbers.

10. The benefits meanwhile go beyond a technological solution to information asymmetries, since the leading companies (especially independent platforms) seek to make use of unused capacity in the vehicle fleet to meet the demand for transport, favouring efficiency of vehicle use.

11. It has even been argued that the expansion of such mobility services could lead to a reduction in the total number of hours during which taxis do not carry passengers, a consequent reduction in the number of vehicles required to meet demand, and a reduction in polluting emissions.

12. Because TNCs are a recent innovation, no studies are available to estimate the size of the market they serve or, in the absence of the latter, the percentage of the market that traditional taxis have given up. Efforts that have been made to calculate the size of this market, however, suggest a share of around 10%.¹ What is more, the accelerated growth of these platforms has occurred in different markets throughout the world², including in areas usually occupied by traditional taxis.³

13. Nevertheless, the fact that independent platforms (Uber, Cabify) use private drivers who do not provide a public service has led to conflict between organised groups of taxi drivers, TNCs and TNC service user groups.

14. The roots of the conflicts that have arisen because of the entry of TNCs lie in the fact that independent platforms contact drivers who wish to be self-employed and who use vehicles which are considered to be for private or personal use. This situation has been perceived as unequal or unfair competition caused by the regulatory vacuum surrounding TNCs, since there are mandatory requirements for drivers wishing to offer public taxi services, while standards for TNC services depend on each network.

3. Competition and disruptive innovation

15. In the same way that disruptive innovation leads to paradigm shifts, competition policy may help to ensure that innovative and differentiated products and services are offered to consumers at better prices. In Latin America in particular, this means that traditional public policy solutions should also be innovative and new forms in which regulation and competition can develop should be explored.

16. In this context, the work of competition authorities is very important in proposing pro-competitive regulatory responses to preserve and encourage innovation. Their responsibility is precisely to protect the competition process, and they are therefore in a privileged position to make governments aware that their long-term success depends on their ability to adapt to new technologies and provide a place for these innovations.

¹ Aswath Damodaran estimates that Uber accounts for 10% of the market. Bill Gurley – a director of the company – believes that that percentage does not take positive network effects into account. See “How to Miss By a Mile: An Alternative Look at Uber’s Potential Market size”, in *www.abovethecrowd.com*, available at <http://x.co/8bTcn>. In Australia, Uber has been estimated to have a market share of 8.8%. See “The Rise and Rise of Uber in Australia”, in *www.getpocketbook.com*, available at <http://goo.gl/ZdkbwN>. In Mexico, TNCs as a whole are estimated to have around 8% of the market. In particular, Cabify and Uber jointly have some 700 vehicles in the Federal District, which would represent 0.7% of all traditional taxis operating in Mexico City. See “Apps de taxis ‘aceleran’ en el DF: alcanzan 9.6% del parque vehicular” [“Taxi apps are ‘gaining speed’ in Mexico City, accounting for 9.6% of the vehicle fleet”] in *El Financiero*, 22 October 2014.

² In the case of Uber, it was forecast in 2013 that the year would end the year with USD 1 billion gross turnover and USD 213 million net turnover. In 2014, Business Insider confirmed that these figures would rise to USD 10 billion and USD 2 billion respectively (a ten-fold increase in just one year). In 2014 and 2015, Uber attracted almost USD 5.9 billion in capital (seven times that achieved by Lyft). See “Uber contra Lyft, la desigual batalla entre dos de las grandes startups de transporte” [Uber v Lyft, the unequal battle between two of the major transport start-ups], in *El Blog Salmón* (consulted on 25 March 2015), available at <http://tr.im/6k0TB>.

³ In New York in 2013, its UberX service, with a price similar to or lower than the traditional taxi market, went from 10% of its portfolio of services to become the leading one with around 40%. Business Insider, “Internal Uber Deck Reveals Staggering Revenue And Growth Metrics”, consulted on 25 March 2015, available at <http://goo.gl/MC6dtR>.

17. Regulation of this type of market must take into account the cost of government intervention on the one hand and the way in which business develops to allow increasingly greater self-regulation on the other.

4. COFECE's opinion regarding TNCs

18. On 4 June 2015, the plenary session of COFECE issued an opinion on the impact that mobile platform-driven passenger transport services have on the competition process and free access to markets. COFECE found that traditional public transport services, specifically taxis, suffered from at least two problems that may distort service provision to the detriment of consumers:

- **Information asymmetries:** consumers do not have sufficient information on important aspects such as driver reliability, safety, price visibility and quality of service. This reduces incentives to improve service quality or to innovate, since the captive market position of consumers is exploited to some extent.
- **Co-ordination problems:** times from meeting points are uncertain both for consumers and for drivers, which has an impact on demand, supply and efficient vehicle use.

19. COFECE also examined international experience in regulating TNCs and found that different legislation does not always seek to promote innovation and therefore to satisfy consumer needs. COFECE additionally considered that such services can be clearly differentiated from traditional public transport services, the risk therefore being to try to regulate them or treat them as equals. COFECE examined the various reactions to, and interpretations of, the legal and regulatory treatment to which TNCs have been subjected by some administrative, legislative and legal authorities around the world, specifically Colombia, Madrid, France, Germany and the USA. Special attention was also paid to some US cities' experience of TNCs (Chicago, Houston, New York and Washington D.C., among others), and it was found that the predominant regulatory trend was to recognise these new mobile app-based schemes which connect drivers and passengers while safeguarding public policy transport objectives.

20. In this respect, COFECE found that governments around the world have adopted different regulatory measures to address the issues mentioned and to secure optimal conditions in which to provide the service in the traditional ways: “[...] *Governments throughout the world – normally at local level – have sought to regulate various aspects, also with varying degrees of success [...]*”.⁴

21. Demand for this type of service in Mexico was found in a sector of the population which enjoys access to credit cards and smartphones. These services established a new base of consumers and led to a migration from traditional taxis to TNCs, leading to the following advantages:

- consumers are familiar with information regarding the driver before getting into the vehicle = **safety**
- routes are planned automatically = **no diversions**
- fares are dynamic according to supply and demand in real time = **quality**
- the availability of the service and waiting times are known in real time = **supply**

⁴ Biggar, D. (2 September 2011), “Why and how should we regulate taxis?”, prepared for the Victorian Taxi Inquiry Roundtable, available at: <https://www.yumpu.com/en/document/view/28077780/why-and-how-should-we-regulate-taxis-taxi-industry-inquiry>.

22. According to COFECE's assessment, the repercussions of TNCs on competition are:

- **Correction of market failures:** the self-regulation model is more efficient and transparent. TNCs offer a solution which addresses market failures, with a direct impact on consumer welfare.
- **Innovation:** efficient integration of key technologies such as smartphones, global positioning systems (GPS) and electronic payment systems, which have contributed to consumer welfare because they can generate better service offers than exist or meet needs which are currently not met.
- **Network efficiencies:** since the value of the platform on which TNCs operate depends on the number of drivers and consumers that use it, these companies have an incentive to consolidate and grow, while efficiencies are generated because of reduced transaction costs. Consumers also benefit from the existence of a number of TNCs, allowing them to use them simultaneously or to shift between options at no cost.

4.1 COFECE public policy recommendations

23. When the opinion was published, the prevailing Mexican regulations did not cover these new transport services, which is why the opinion specifically recommended that they should be recognised and regulated. It was also pointed out that regulation should be limited to ensuring essential public policy objectives, such as consumer safety, and should avoid:

- authorising or restricting vehicles or restricting their quantity by imposing additional requirements such as plates and badges;
- regulating charges.

4.2 Relevant regulatory responses

24. On 15 July 2015, Mexico City's Department of Transport issued two decisions regulating the registration and operation of TNCs (supplementary and independent platforms). This action is generally consistent with the opinion issued by COFECE, in which traditional transport services are differentiated from TNCs.

25. With respect specifically to independent platforms, the decisions put COFECE's recommendations into effect by not limiting the number of vehicles, which can be determined only by supply and demand. This regulation also takes into account COFECE's comments on the associated benefits, such as the identity of drivers, waiting time reductions and service improvements. In general, the proposal of the Government of Mexico City is compatible with COFECE's opinion and coincides in particular in the following three areas:

- TNCs are recognised as transport services,
- the regulatory approach is differentiated, and
- technological innovation is allowed to develop while essential public policy objectives are ensured.

26. In addition, on 22 August of the same year, the legislature of the State of Puebla adopted an amendment to its transport law which regulates the registration and operation of TNCs (both supplementary and independent platforms). The proposed law makes specific reference to COFECE's opinion. The amendment thus defined a new transport category entitled "Executive Service", which coincides with the term "independent platform" defined by COFECE.

27. The most interesting point is that this Law states that “Executive vehicles are private units which, without being subject to the granting of a concession, permit or authorisation by the Department, are used by private individuals for the carriage of persons and are registered as TNCs”.

28. Although some restrictions could be regarded as barriers, such as the various requirements laid down for the automobiles involved, this proposal put forward by the Government of Puebla is compatible with COFECE’s opinion in the following three areas:

- TNCs are recognised as transport services,
- the regulatory approach is differentiated for taxis, and
- technological innovation is allowed to develop but principally ensures public policy objectives.

4.3 Legal action against the regulation by Mexico City

29. In response to the decisions regulating TNCs in Mexico City, a group of taxi drivers filed a constitutional appeal, better known in Mexico as an “*amparo*” [action for infringement of fundamental rights and freedoms]. On 21 September 2015, a district judge denied the application on the following grounds:

- the decision issued by Mexico City’s Department of Transport has a valid purpose;
- TNCs are private transport services and cannot be deemed to be public because: (i) TNC vehicles do not have physical signs distinguishing them from standard vehicles, and (ii) the services are requested by means of a platform and pick-up points are clearly defined;
- the Department of Transport is not required to request the same obligations that taxi drivers have to fulfil (concessions) because the latter have an effect on public transport services.

5. Conclusions

30. While there is no doubt that disruptive technologies and innovations give rise to important benefits for competition and for consumers, there is also no doubt that they may raise public policy concerns and therefore generate calls for their regulation.

31. The competition authorities play a crucial role in advocating pro-competitive regulatory responses and assisting the transition brought about by these innovations.

32. The challenge lies in the ability of traditional public policy solutions to take on innovative forms and explore different ways in which regulation and competition can develop.