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Government overlooks COFECE authorisation to regulate LPG prices

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Introduction

In the past few months, prices of LPG have risen to an all-time high. According to data reported by the Energy Regulatory Commission (CRE), the average price of liquefied petroleum gas (LPG) in June 2017 was 8.77 pesos (\$0.43) per litre, while the average price in June 2021 was 12.94 pesos (\$0.64).⁽¹⁾ In light of this, the Federal Economic Competition Commission (COFECE) launched an ongoing investigation⁽²⁾ on 31 May 2021 to determine whether effective competition conditions exist in the LPG market. COFECE is also investigating possible anticompetitive behaviour in the market⁽³⁾ similar to its previous studies, which provided multiple recommendations to promote competition in the market.⁽⁴⁾

Nevertheless, final consumers and political figures have been lobbying for direct government intervention in the LPG market. The Ministry of Energy and the CRE have consequently imposed price caps without seeking the necessary declaration of lack of effective competition conditions in the LPG market from COFECE, as provided for in the Hydrocarbons Law (LH) and the Federal Economic Competition Law (LFCE).

In accordance with Article 82 of the LH, retail prices of hydrocarbons are to be kept consistent with the conditions of the market. Similarly, Article 77 of the Regulation of the Activities in Title Three of the LH provides that price regulations will not apply to the distribution of LPG, with the exception of pipeline distribution, unless COFECE decides otherwise through the procedure to determine the effectiveness of competition conditions in a particular market established in Article 96 of the LFCE.

LPG price regulation

On 28 July 2021, the Ministry of Energy published the Emergency Guideline for the Welfare of the LPG Consumer (the Guideline)⁽⁵⁾ in the Federal Official Gazette. In the Guideline, the Ministry of Energy determined that it was necessary for the Mexican Government to intervene in LPG pricing in order to prevent further increases. The Guideline urged the CRE to issue emergency regulations within three days to establish the price caps on LPG for final consumers.

In accordance with the provisions of the Guideline, the CRE published an act in the Federal Official Gazette on 29 July 2021 regulating maximum prices of LPG for final consumers (the CRE Act).⁽⁶⁾ The CRE Act was reportedly issued to correct the unjustified increases in LPG prices and, consequently, to achieve the following:

- protect final consumers;
- facilitate an efficient and affordable supply of LPG;
- promote the purchase of LPG at affordable prices;
- avoid undue discrimination;
- reflect the LPG market conditions; and
- obtain a margin that allows the recovery of costs from marketers, distributors and retailers of LPG in order to engage with the development of the industry.

Moreover, the CRE Act provides that the determination of prices will be calculated by a methodology that considers different regions of the country and modalities of sale to final consumers.

The formula considered in the methodology is calculated by the average sales price per point of sale in a region, adding the estimated cost of freight from the shipping centre to the distribution plant in the region, and the estimated marketing margin for the week and region plus the modality of sale; multiplied by an adjustment factor used as a method to control the price when the variation of the maximum exceeds inflation plus the value added tax.

Based on this, CRE started publishing a list of maximum LPG prices for final consumers according to region and sale modality, which it has updated weekly since 31 July 2021.⁽⁷⁾

Comment

The regulation described above raises two main competition concerns:

- it overlooks the mechanisms provided by law that allow authorities to regulate LPG prices; and consequently,
- it may generate negative effects for competition in the LPG market.

Each concern is addressed below.

Overlooking LPG price regulations

As described above, the law states that LPG prices must be determined in a free price regime. Authorities may only suspend this regime



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and establish maximum price caps when COFECE issues a declaration of lack of effective competition conditions in the market and recommends the imposition of relevant measures.

In this case, even though COFECE has already initiated a procedure to determine the existence of effective competition conditions in the LPG market, both the Ministry of Energy and the CRE overlooked this requirement and issued the CRE Act. COFECE responded to this by issuing a communiqué on 28 July 2021, urging CRE to respect the due process established in the law and wait for COFECE to issue its findings.⁽⁸⁾ Such findings could give the CRE grounds to set maximum prices for the sale of LPG to final consumers.

Negative effects on LPG competition

By overlooking COFECE's procedure, the CRE Act may have an undesirable impact on the competition in the LPG market. The requirement for COFECE to issue a declaration of lack of effective competition conditions in the market in order for authorities to set price caps is intended not only to avoid unnecessary price regulation (from a competition standpoint), but also to ensure that authorities establish mechanisms suitable for handling competition concerns identified by the competition authorities. That is, the government must diagnose and analyse the lack of effective competition conditions in each case to identify a solution for the lack of effective competition conditions and that does not generate further competition issues.

In the absence of a thorough diagnosis regarding the lack of effective competition conditions in each case, it is difficult for the authority to possess all the facts necessary to make a correct evaluation of the causes. This may lead authorities to impose unnecessary or undesirable regulations that generate harmful effects on consumers such as market distortions, supply shortages (if price caps are too low) and encourage the LPG black market, etc.

In response to this issue, producers, marketers and distributors may contest the CRE Act through *amparo*⁽⁹⁾ actions before the federal courts, requesting a court cautionary measure that suspends the effects and applications of the Act until a final judgement is issued. In case of a favourable judgement, the CRE Act will be suspended permanently and CRE will need to wait until COFECE's resolution to determine whether it can establish price caps in the LPG market. Similarly, COFECE has the authority to file a Constitutional Controversy⁽¹⁰⁾ claiming that the issuance of the CRE Act constitutes a violation of due process and an intrusion of its exclusive authority to determine the lack of effective competition conditions in the LPG market.

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Endnotes

(1) Further information is available [here](#) (in Spanish).

(2) Further information is available [here](#) (in Spanish).

(3) Further information is available [here](#) (in Spanish).

(4) Further information is available [here](#) (in Spanish).

(5) Further information is available [here](#) (in Spanish).

(6) Further information is available [here](#) (in Spanish).

(7) Further information is available [here](#) (in Spanish).

(8) Further information is available [here](#) (in Spanish).

(9) An *amparo* action is a constitutional procedure before the federal court to dispute acts of public authorities and protect human rights recognised in the Constitution.

(10) A Constitutional Controversy is a procedure filed before the Mexican Supreme Court of Justice through which an authority may dispute acts of a different authority that intrude in its powers and competences.