

# private sector

## Regulatory Reform

### Institution Building: Lessons from Mexico

**During the 1990s Mexico undertook some of the world's most far-reaching reforms of business regulations. Many factors, including trade liberalization and firm political commitment, drove this process. But critical to its sustained success was the early development and then legal strengthening of a regulatory reform agency dedicated to pursuing consumer welfare and ensuring public scrutiny of regulations. This Note documents the agency's role in creating an environment for improved business regulation and greater transparency.**

Private business in Mexico had been heavily regulated since the 1930s, with serious effects on the economy. A turning point came in 1986, when Mexico joined the General Agreement on Tariffs and Trade (GATT) and unilaterally started to open its economy. Many factors moved the regulatory reform process along. Top officials were strongly committed to revamping the legal and regulatory framework. Entry into international trade agreements imposed policy discipline and made it harder to reverse reforms. Greater international competition demanded measures to lower the cost of doing business. And the atmosphere of financial crisis in the mid-1990s maintained fiscal discipline and rallied private sector support.

But another key factor in sustaining the reforms over a long period and multiple governments was the creation in 1989 of a central-

ized agency dedicated to advocating regulatory efficiency and improvement. Political support for this agency proved crucial: the Economic Deregulation Unit (UDE) was created only with the backing of a newly elected president and the support of a disciplined incumbent party in control of Congress. It was established by presidential decree within the Secretariat of Trade (now Economy), but with broader powers than the secretariat itself.

The agency started out using a top-down approach. But as a more contested political system evolved and an economic crisis developed, the agency built more consensus through wide stakeholder participation. As the political outlook for reform became more uncertain, the agency was transformed into a body backed by law, with greater autonomy and transparent, institutionalized regulatory reviews—a big change within a culture of opacity and bureaucratic discretion.

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The agency enjoyed some early successes. It helped to dismantle price controls, repealed legal barriers to the entry of new firms, and simplified cumbersome commercial court procedures. It also simplified federal procedures for starting a business, reducing the time required from 90 days to just one. Parallel fast-track schemes for business start-up have been created at the municipal level.

### Defining a strategy

From the outset UDE's effectiveness depended on the scope of its mandate. Charging it with simply reducing red tape would have been less threatening to federal agencies and thus politically easier. But cutting red tape without tackling the underlying legal and regulatory framework would not have been enough: red tape was merely the consequence of the poor regulation, not its cause. The challenge was to develop a mandate that would be politically acceptable yet give the agency sufficient authority and flexibility to exploit opportunities to improve regulation as they arose. The solution was to limit its mandatory authority (what it *must* do) to reviewing new regulations proposed by federal agencies while giving it broad optional authority (what it *could* do) to review and propose amendments of existing regulations.

### Mobilizing private sector support

UDE capitalized on the 1994 "tequila crisis" to muster broad stakeholder support. Faced with increasing competition, private firms lobbied for government protection, but fiscal stringency, the crisis, and the North American Free Trade Agreement (NAFTA) ruled out direct support. To placate business, the government instead created the Deregulation Council, in 1995, to bring the private sector and other stakeholders into the reform process. Chaired by the trade secretary, the council comprised key government officials and prominent representatives from labor, business, academia, and sector organizations. Its role was to advise UDE and monitor the performance of federal agencies in overhauling their regulations.

### Formalizing transparent reviews

As a first step toward formal regulatory reviews, a 1995 presidential decree ordered federal agencies to compile an inventory of business regulations

and procedures as well as proposals for reform, using a standard template. In 1996 UDE and the council introduced the more systematic regulatory impact assessment, based on cost-benefit concepts, as a tool to evaluate regulatory proposals. Federal agencies were required to submit such an assessment with any proposed regulation. UDE could then publish, within 30 days, a nonbinding opinion of the proposal and its assessment—a big break from the past practice of showing proposals only to selected interest groups. The sponsoring agency would then redraft or withdraw its proposal, and Congress or the president would issue final approval. In 1997 UDE opened the process to public feedback through a new Web site. The reform agency, in its new incarnation, continues this process today (figure 1).

A small team of dedicated professionals carried out the agency's work, with regular input from the council and from peer agencies in Canada, the United Kingdom, and the United States. The council's support was pivotal, especially in pressuring laggard agencies, through the threat of public exposure, to improve their regulation. The council met quarterly, with secretaries required to present their cases personally.

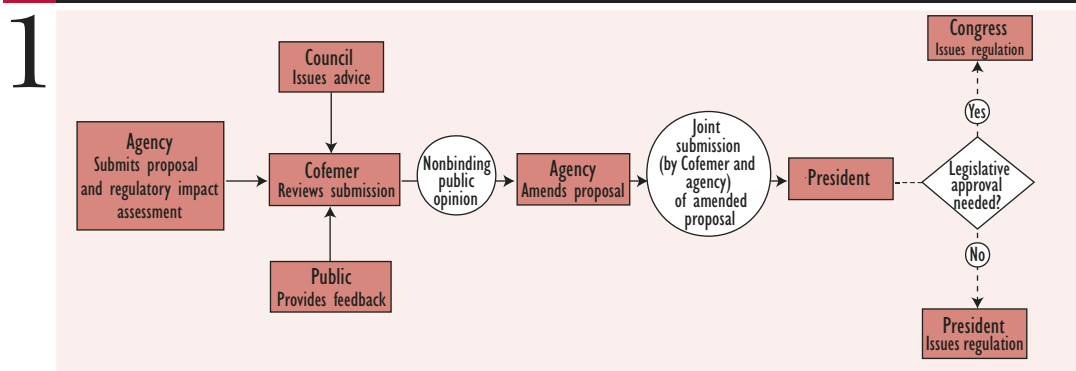
UDE performed its review of federal agencies strategically, to build experience and credibility over time. It started with agencies expected to be cooperative, then moved on to the more reluctant ones. The agency exercised its optional authority with similar selectivity, proposing regulatory amendments only if believed to be economically and politically feasible.

Regulatory impact assessments proved especially challenging. Federal agencies often blamed UDE for creating a bureaucratic bottleneck when it issued critical reviews. A few secretaries openly opposed the agency's active role, as it threatened vested interests and the traditionally opaque way of creating and applying regulations. But the opposition was thwarted by strong presidential support and the trade secretary's ability to demonstrate that the complaints were a sign of the agency's effectiveness.

### Sustaining reform

In the late 1990s UDE and the council became concerned about the fragility of the process under a presidential decree. Success so far had

Figure Review process for proposed federal regulations



depended heavily on a few individuals—a group of energetic technocrats with strong support from the president. There had been a few cases of noncompliance by government agencies. And agency heads often pressured UDE into refraining from criticism of impact assessments or issuing opinions too quickly and thus undermining the credibility of the review process. Moreover, the fast-track business start-up program in Mexico City was abandoned in 1998 under a new administration, pointing to both the possibility of the same occurring at the federal level and the need for an effective process of coordination across different levels of government.

### Transforming the reform agency

UDE thus sought to put itself on a more permanent footing—to strengthen incentives for compliance, sustain reform through changes in administration, and improve coordination with subfederal entities. Key to success here were the president’s legal counsel, who supported the initiative out of a belief in the agency’s usefulness, and the council, which provided backing crucial in obtaining congressional support. The proposed changes also came at the end of an administration, when line secretaries felt little opposition to a law that would be applied after their tenure.

In 2000 UDE was transformed by law into the Commission for Regulatory Improvement (Cofemer), an autonomous body established within the Secretariat of Economy and headed by a presidential appointee. The agency acquired new optional authority to undertake cost-benefit analysis of how federal agencies operate and how they apply and enforce regulations. Cofemer also

acquired a bigger staff and budget—and the legal backing and tools to become a powerful advocate for regulatory improvement.

### Recent achievements

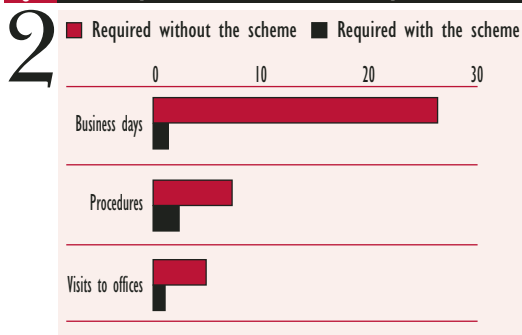
Using its optional authority, Cofemer deepened transparency by drafting a 2002 law requiring federal agencies to open their files to the public. A one-year “regulatory moratorium” to discourage agencies from proposing new regulations unless clearly needed has cut submissions by a third. And a powerful new law designed to reduce bureaucratic discretion and abuse requires automatic cancellation of any new regulatory procedures not published in the federal register by their implementing agency.

In addition, Cofemer has promoted fast-track business start-up at the subfederal level. With regional competition creating pressure for change, the program has spread to more than 20 cities, and initial results are promising (figure 2). Further progress will require tackling problems in the underlying legal and judicial framework.

### Remaining challenges

Cofemer can exercise its full powers only if it enjoys broad support and acts decisively. One challenge is sustaining the support of the private sector. Earlier, rallied by the domestic crisis and strong political support, the private sector took on an active role in pressuring agencies to improve regulation. Today many factors contribute to a more passive role: the loss of founding members of the council through turnover, a review process whose success has reduced it to routine, and the diminished role of the council,

**Figure 2** Initial results of fast-track business start-up schemes at the municipal level



Note: Data cover nine municipalities before and after schemes were introduced.  
Source: OECD 2004; authors' estimates.

which now serves mainly as a forum for announcing successes. And new political circumstances and a fragmented Congress have shifted the private sector's lobbying efforts from the executive branch toward Congress.

Moreover, as recent events highlight, Cofemer's will to exert its optional authority in controversial areas has weakened. In 2003 it waived its right to issue an opinion on proposals defining the powers of the regulator for the underperforming telecommunications sector. It also has failed to publicize the fact that no federal department has published its procedures in the federal register. So the powerful new law that automatically repeals any unpublished procedures has not yet been enforced.

Another concern is Cofemer's location in the Secretariat of Economy. Because of the secretariat's narrower scope and the lack of strong political support, that situation has created institutional conflicts making it hard for Cofemer to exert its broad optional powers. A better location would be in the Finance Secretariat, where Cofemer would enjoy a consistent oversight capacity and a better ability to assess the budgetary effect of proposed measures. Such reform would bring Cofemer closer to its Canadian and U.S. counterparts.

## Conclusion

Mexico's experience offers a key lesson: create institutions and procedures early in the process that can support reform over the long haul. As the political and administrative system slowly internalizes the improvements, adherence to principles of transparency, accountability, and consumer welfare becomes vital to signaling the credibility of the

new regulatory culture. Empowering institutions such as Cofemer can promote compliance and sustainability, and using technologies like the Internet can reduce the time and costs of institutionalizing the principles.

Many of the circumstances are specific to Mexico. But any country carrying out regulatory reform will face similar challenges and can learn from its experience. Competitive pressures arising from trade liberalization, along with a domestic crisis, provided a powerful impetus for reform. An institutional advocate was needed to achieve fundamental change in procedures and promote beneficial regulations. Decisive leadership and strong support from political and other stakeholders were critical to exploiting the reform agency's full potential. And a key factor was proper design:

- A broad legal mandate, based on advocacy of consumer welfare, to address both the root causes and the consequences of a flawed regulatory framework.
- An oversight body, with broad stakeholder participation, to review results and compliance by federal agencies while using public exposure to punish noncompliance.
- Active and sustained commitment of the private sector, especially the small and medium-size firms that had been on the losing side of the business lobby.
- A track record of well-publicized successes to build credibility.
- Promotion of regulatory improvement programs across all levels and branches of government.

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## viewpoint

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