

MEXICO: UNLEASHING REGULATORY REFORM AT THE LOCAL LEVEL

Governments around the world face challenges when pursuing broad regulatory reform: identifying bottlenecks, obtaining political support, getting the resources needed, gaining buy-in from stakeholders, bringing agencies together in one coordinated effort. Mexico illustrates the challenges of regulatory policy making when it involves different levels of government and regulation.

Mexico's 31 states and 2,441 municipalities, along with Mexico City, have extensive regulatory powers, allowing them to design, implement and enforce regulations.¹ So regulatory reform has required not only horizontal coordination among ministries, agencies, and legislative and judicial bodies at the federal level, but vertical coordination with entities at the state and municipal levels. The regulatory reform initiative in Mexico has used an exercise of benchmarking business regulation in all 31 states and Mexico City to support this coordination and stimulate change.

Gathering momentum

Regulatory reform efforts started as early as the 1980s as Mexico, seeking rapid integration with the global economy, joined large international trade agreements and the OECD. Greater openness to international markets and increased competition required measures to lower the cost of doing business for its 75 million people.² In the early 1990s the reform initiative was led by the Office of the President and a small group of technical advisers. The consequences of the 1994-95 economic crisis helped intensify the focus on small and medium-size enterprises as an engine of employment growth.

But the success of the reform efforts was undermined by lack of effective monitoring, transparency and public support. Changes in the political landscape after the 1997 midterm elections weakened the government's support in Congress, where the president's party lost its 68-year majority in the lower chamber. Now none of the 3 major political parties had an absolute majority. In this fragmented political environment the unilateral top-down approach was seen as

no longer viable. Compounding the problem was the lack of outreach to other stakeholders: Congress, the judiciary and the public administration.³

In 2000 the Office of the President set up the Federal Commission for Regulatory Improvement (known by its Spanish acronym Cofemer) with the aim of establishing a long-lasting reform effort and a systematic approach to regulation. But while this agency became the main driver of change, continuing political obstacles at the local and national levels limited its effectiveness. In late 2003 the first *Doing Business* report ranked Mexico above the global average on the ease of doing business. Yet Mexico trailed behind such competitors as Chile, Malaysia and Thailand—and even further behind OECD high-income economies such as the United Kingdom, Australia and Germany.

The Office of the President saw an opportunity to use the *Doing Business* report to drive improvements. But because the president's support in Congress eroded even further in the 2003 midterm elections, reforms failed to pass. With a national presidential election looming in mid-2006, the Office of the President simply did not have the political clout to carry out broad reforms, which usually take several years to plan and implement.

Thanks to Mexico's federal structure, however, states could start reform efforts immediately. In 2005 the Office of the President requested a subnational *Doing Business* report that would go beyond Mexico City. The first such report, launched in 2005, benchmarked 12 states in addition to Mexico City. A second one extended coverage to all 31 states in 2006. A third report repeated the benchmarking in 2008. A fourth is under way.

What has worked?

The subnational *Doing Business* reports, by providing a fact-based set of indicators that capture differences in local regulation and local implementation of national laws, prompted first dialogue and then action on regulatory reform. Along the way they have also led to the sharing of experience, to competition and to collaboration, all of which have helped to promote and sustain change.

Sharing experience

The subnational *Doing Business* project has provided a vehicle for peer-to-peer learning and sharing of good practices among Mexican states. Cofemer organizes a conference twice a year at which plenary sessions allow every state to share its experiences with regulatory reform, as well as lessons learned. Peer learning also takes place even more informally, on visits by policy makers to good performers such as Aguascalientes and Guanajuato. A visit to Sinaloa, where policy makers learned more about how this state issues land use authorizations electronically, led Colima to set up a similar system on its own website.

Sharing experience makes sense, because differences across states in what entrepreneurs encounter in doing business can point to opportunities for improvement. For example, *Doing Business in Mexico 2007* showed that business registration fees varied greatly from state to state. In Michoacán the registration cost for companies was the equivalent of \$16; in Chihuahua it was \$1,035, more than 60 times as much. And while some states set fixed fees, others charged percentage-based fees, calculated on the basis of the company's capital.⁴ The 5 states with the most expensive business start-up processes used percentage-based fees.⁵ The story was similar for property transfer fees. Yet a company registration or property transfer takes the same amount of work regardless of the size of the company's capital or the value of the property.

The many similarities across states—such as bottlenecks faced by entrepreneurs trying to start or expand a business—provided just as much reason for sharing experience. In registering a business or transferring property, the biggest hurdle was filing documents with the company or property registry. *Doing Business in Mexico 2007* reported that the property registration procedures with the public registry took between 73% and 87% of the total time for registering property. But *Doing Business in Mexico 2009* could report that 13 states had focused on updating their property and commercial registries. Many states have also been working to consolidate procedures in one place. Most now have a

one-stop shop that centralizes procedures and provides advice to entrepreneurs.

Creating competition

Competition between states was the biggest catalyst for reform. Faced by almost identical federal regulations, mayors and governors had difficulty explaining why it took longer or cost more to start a business or register property in their city or state. States that did poorly could not justify their poor performance, and they were inspired by the reform efforts of other states.

This showed up in an accelerating pace of change. *Doing Business in Mexico 2007* reported that 9 of 12 states (75%) had implemented reforms in at least one area measured by the report. Two years later, *Doing Business in Mexico 2009* reported that 28 of 31 states (90%) as well as Mexico City had implemented *Doing Business* reforms. Mexican states were improving their regulatory environments, and the impulse for regulatory reform persisted even through changes in government.

The pace of reform was maintained thanks in part to the regulatory reform units that states were beginning to create. Puebla set up the first, in 2003. By 2005, 5 states had regulatory reform units. Today about 20 states do. Nuevo León created the most recent one, in 2010. All the units have been created at the state's initiative, with technical assistance from the federal government through Cofemer.

Promoting collaboration

Delegating the reform agenda to local authorities proved to be an essential part of the national reform effort. This fostered commitment, a sense of collaboration and better communication among federal, state and municipal authorities.

Early on in the reform process the federal government collaborated with the states to improve business registration through the Rapid Business Opening System (SARE). A system of one-stop shops for local procedures, SARE was created to coordinate municipal procedures so that low-risk companies could get their license and start operating in a few days. The improved

collaboration through Cofemer helped expand the system to more municipalities across more states.

Today the system has been implemented in 186 municipalities across 30 states.⁶ According to a recent study, the SARE initiative has had a significant impact.⁷ After the introduction of SARE's one-stop shops, the number of registered businesses increased by 5% and wage employment by 2.2%.

After a few years of steady improvement at the state and municipal levels, the Office of the President saw a need for broad regulatory reforms at the federal level. One impetus was a perception that the subnational reform efforts needed another boost. Mexico City's poor performance in the subnational rankings on the ease of doing business pushed the federal government to collaborate more closely with Mexico City's 16 boroughs to coordinate reform efforts. A second impetus was Mexico's performance in the global rankings. While several regulatory reform programs had been introduced at the federal level in 2005–09, these had not been enough to propel Mexico into the ranks of the best performers—such as New Zealand, Korea and Denmark, which were then among the top 35 on the ease of doing business.

In September 2009 the Office of the President announced its intention to transform Mexico's regulatory environment. The aims were to build a regulatory framework centered on and involving the citizen, to increase competitiveness and to promote development. The Mexican government secured technical assistance from the World Bank Group to identify opportunities for regulatory reform and to provide expert advice.

The initiative has already produced results in business registration. Previously there had been little coordination between federal agencies and the state and municipal organizations involved in the process. Now an online one-stop shop, Tuempresa, launched in August 2009, coordinates the federal procedures and is adding state and municipal procedures.⁸ Public notaries have been granted access. Today the online system processes about 100 new business registrations a month in Mexico City, or 7% of the

total. Mexico has also improved construction permitting, by merging and streamlining procedures related to zoning and utilities.

More areas are being worked on. Reforms continue in trade, construction permitting, and business, property and collateral registration.

Seeing results

There are encouraging signs that strengthening different areas of the business environment at the same time produces better overall results for business creation. A study performed after the introduction of SARE in several states found that the program had a significantly greater effect on the number of new businesses created in areas with a better overall investment climate.⁹

Changes are also apparent for firms. The share of senior management's time spent dealing with requirements imposed by government regulations fell from 20% in 2005 to 14% in 2009. During the same period the share of businesses that had applied for an operating license increased from 4% to 23%.¹⁰

Conclusion

Regulatory reform in Mexico has become an ongoing process. The government has taken steps to continue the subnational *Doing Business* project. In a first for such projects, the methodology is being transferred to a reputable, independent think tank in Mexico, which expects to continue to do the study every 2–3 years. The federal and state governments have taken the lead on the funding side as well. The first *Doing Business in Mexico* reports were financed in part by donors (such as USAID) and the World Bank Group and in part by the Mexican government. The fourth is being fully funded by the federal and state finance ministries.

The hope is that by tracking progress over time, continued periodic benchmarking by an independent third party will create incentives to maintain the reform effort through changes in government. The *Doing Business in Mexico* reports, capturing the progress of regulatory reform over time, show that it was not a one-time initiative—but instead an effort that has strengthened with continued benchmarking.

NOTES

1. García Villarreal 2010. Information on the number of municipalities is from National Institute for Federalism and Municipal Development (INAFED), "Los últimos municipios creados," <http://www.e-local.gob.mx/>.
2. Population in 1985 from World Bank 2010b.
3. Cordova and Haddou-Ruiz 2008.
4. World Bank 2006a.
5. World Bank 2008a.
6. Information provided by Cofemer.
7. Bruhn 2011.
8. <http://tuempresa.gob.mx>.
9. Kaplan, Piedra and Seira 2007.
10. World Bank Enterprise Surveys (<http://www.enterprisesurveys.org>).