Stakeholders and Power Relations in Regulation

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Stakeholders play at least two roles in utility regulation: Some receive benefits, such as customers protected from monopoly power. Stakeholders also influence regulation by, for instance, commenting in proceedings. Most studies on stakeholder relations focus on engagement, such as through advisory groups and public hearings. Largely missing are analyses of power relationships. Some stakeholders, such as lawmakers, have formal authority over regulatory bodies. Others have little formal authority. Stakeholders also vary in how and the degrees to which regulators affect them. This paper examines these relationships and illustrates them with a survey of regulatory agencies in the Caribbean.

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If men were angels, no government would be necessary… In framing a government which is to be administered by men over men, the great difficulty lies in this: you must first enable the government to control the governed; and in the next place oblige it to control itself.

- James Madison, *The Federalist No. 51*

Institutions like independent utility regulatory agencies are unusual in modern government systems in that they regulate both the governed and the governing. In his classic text on utility economics, Martin Glaeser (1927) explained that utility regulation emerged from a need to protect customers from being exploited by enterprises that play an essential role in the economy and that are monopolies. He also described how regulation by political bodies was whimsical and ineffective, and bankrupted some service providers. The development of the expert, independent agency enabled both the protection of customers from the enterprise, and the protection of the enterprise from politics, resulting in an investment environment where service could grow. (Jamison 2015)

These institutions by necessity engage with stakeholders in both formal and informal ways. The quasi-judicial nature of many regulatory agencies makes engaging with stakeholders important because the agency needs information for decision-making. The quasi-legislative nature of agencies makes stakeholder engagement important because the agency needs legitimacy, i.e. consent (informally) for its work by allowing stakeholders to have a voice, to learn about the regulatory process, and to develop relationships with the agency without leading to biased decisions.

Most of the literature on regulation and stakeholders addresses the processes the agencies should use to obtain information and legitimacy. IPART (2012) examines how customers' views can be represented in price reviews, including

who should engage with customers of regulated businesses, how regulators can best gauge the views of average households, and how customer engagement should feed into future price reviews. OFWAT (2002) describes its consultation processes and how stakeholders can participate. Smith (1997a, 1997b) and Jamison (2007) explain how transparency, hearings, and due process affect regulatory decisions and provide the public with the sense of regulating the regulator.

Missing from this literature is an examination of the power relationship in regulation, i.e., stakeholders' differing abilities to affect the regulatory agency and the variations in the agency's ability to affect stakeholders. This paper examines this issue by describing the regulator's position in the governance system for utilities and regulation, examining the nature of the relationships, and illustrating the imbalances in relationships based upon a survey of Caribbean utility regulators, the responses to which have been kept confidential. The paper places stakeholders in quadrants based upon their abilities to affect the regulator and the regulator's ability to affect them. Then the paper examines what each stakeholder wants from the regulator and what the regulator wants from the stakeholder. The results of this analysis provide a foundation for examining power relationships and developing strategies for reshaping them where appropriate, and for more effective resource allocation according to relationship priorities. This analysis uses a broader definition of stakeholders than do some papers: Often the term stakeholders is limited to those directly included in the regulatory process, namely customers and utilities. This paper uses the term to include all those with a strong interest in regulation, including politicians and media.

The paper proceeds as follows. The following section summarizes literature on stakeholder relationships and the regulatory system. Section two describes our survey and the results, and analyzes implications. Section three is the conclusion.

I. Framework for Analyzing Stakeholder Relationships in Regulation

Regulation by what are called independent agencies developed largely in the US. Legislative bodies formed the agencies because of weaknesses in regulation performed directly by political bodies and weaknesses in regulation through private action, such as private lawsuits. Political bodies lacked the technical expertise necessary to make economically sound decisions, were sometimes captured by the regulated entities, and could not be depended upon to keep commitments. Regulation by lawsuit lacked coherence and favored those with the means to engage in private action. (Glaeser 1927)

Agencies are considered independent if they are governed by laws that clearly define and circumscribe their authority, are empowered by their governance structure to operate at arm's length from short term political pressures and from industry interests, and are required by law to engage in decision making processes that emphasize information and rigorous analyses. To ensure that the independent agency regulates under the law to serve the collective interests of the stakeholders rather than the interest of one or a small group of stakeholders, independent agencies should have arm's-length relationships with regulated firms, consumers, other stakeholders, and politicians. Examples of mechanisms for ensuring arms-length relationships include appeal processes, transparency, restrictions on corruption and conflicts of interest, and publication of an explanation for every decision. (Smith 1997a 1997b)

Two main aspects of regulatory processes are the existence of mechanisms to receive stakeholders´ inputs and to solve stakeholders' complaints in an intermediate, administrative body. Regulatory processes generally allow stakeholders to present their opinions through open processes like public hearings. Stakeholder confidence can often be enhanced by having well-established, ordered, and open interactions between the regulator and stakeholders. However,

formal hearings can be legalistic, costly, and slow, so regulators with a tradition of formal processes have begun using alternative procedures, such as negotiated settlements and arbitration. Some countries have experimented with informal processes, but issues of transparency lead many to add elements of formality.

These formal structures provide *de jure*, but not *de facto* independence and coherence. Regulatory systems are incomplete contracts, meaning that the formal structures cannot address all contingencies. Thus successful regulatory performance depends in part upon people who are willing to develop and embrace informal practices that adapt to changing circumstances while still aligning with the purposes that underlie the formal laws.

An independent regulatory agency is in a fairly unique position compared to other institutions involved in making utility services work well for a country. (Jamison 2007) Elected officials are sanctioned by voters in democratically-oriented systems. Civil servants working in ministries and government departments are authorized by elected officials. Utility managers are effectively hired by their owners. In contrast, independent regulators, even though they are chosen and empowered according to the legal processes of a country, by design are not intended to please anyone in particular. Instead they are authorized to do their work, whether formally or informally, by a range of stakeholders whose cooperation is needed for the system of laws, financial mechanisms, contracts, communications, and the like to function, resulting in customers receiving the utility services they need to be economically and socially successful.

Figure 1 illustrates a typical system of relationships for making utility regulation work. Each stakeholder is represented by a rectangle and the arrows show the relationships in terms of transactions. For example, in the relationship between the industry regulator and the media, the industry regulator provides information to the media and, in exchange, the media uses at least some of that information in its reporting. The system in Figure 1 is complex and each

participant or stakeholder has its own interests and has multiple relationships that are important to those interests. In some situations, but not in others, a stakeholder's interests and relationships result in the stakeholder being deeply affected by the regulator's work. Also in some situations, but not in others, the regulator is deeply interested in and affected by the stakeholder. These situations represent differences in relationship power between stakeholders and the regulator.

[PLACE FIGURE 1 ABOUT HERE]

Because (1) independent regulators do not have a constituency that sanctions their work, but rather a network of stakeholders whose acquiescence enables the regulator's work, (2) each stakeholder has its own aspirations regarding what the regulator should do, and (3) it is generally physically impossible for the regulator to satisfy all of these aspirations, the critical skill for a regulator to operate independently and well is to know how to disappoint stakeholders at a rate at which they can endure. (Jamison 2015) It is the work of the regulator to distribute losses among the coalition of stakeholders – lawmakers, customers, investors, managers, journalists, judges, and the like – together so that the system can perform.[1]

Figure 2 stylizes the Figure 1 relationships in a regulator-centric fashion. The vertical axis represents a stakeholder's power to affect the regulator, with power being higher at the upper part of the axis. The horizontal axis represents the regulator's power to affect things that are important to the stakeholder, with the right hand side representing higher power. In the upper left quadrant, the stakeholder has more power in the relationship than does the regulator. In the lower right quadrant the reverse is true. In the upper right and lower left, the stakeholder and the regulator have roughly equal power.

[1] We would like to thank Marty Linsky for this insight.

[PLACE FIGURE 2 ABOUT HERE]

Freeman et al. (2007) explain that stakeholders can be grouped into two tiers reflecting the nature of their ability to influence an organization. The first tier, also called the primary stakeholders, includes those that are vital to the effectiveness and survival of the regulatory agency. These could include the government institutions that provide financial resources (such as legislatures or treasuries) and laws (such as legislatures and courts), utilities that provide needed information, and employees. The second tier, called the secondary stakeholders, includes those that influence the regulator primarily by influencing the primary stakeholders. Second tier stakeholders could include the media, special interest groups, and utility customers. Secondary stakeholders may be very important – for example, protecting utility customers from exploitation is a primary purpose of a regulatory agency, but customers are in the second tier because their power over regulators is primarily through their power over elected officials.

An independent regulatory agency using the framework shown in Figure 2 would place each stakeholder name in one of the four quadrants, denote whether each stakeholder is tier 1 or tier 2 (perhaps with color coding), and on a separate table write the nature of the transaction that occurs between the agency and the stakeholder. We use the term transaction to recognize that the stakeholder wants something from the agency and the agency wants something from the stakeholder. Figure 1 illustrates possible transactions. If the transactions break down with powerful stakeholders, the agency's ability to do its job is threatened.

Power relationships should be analyzed from the perspective of the organization of primary interest – in our case, the independent regulatory agency – and from the stakeholders' perspectives as well. For example, an agency completing a stakeholder analysis should complete a Figure 2 for key politicians so that the agency leaders can see itself through the eyes of each politician, and see the politician-agency relationship in the politician's context, namely as one of many

relationships that the politician manages to achieve his or her goals. This is especially important if some of the agency's other stakeholders show up on the politician's grid because, in such cases the agency's relationships with one stakeholder affect its relationships with other stakeholders.

So far we have examined stakeholder relationships as primarily institutional. These relationships change as the agency takes up different issues, so the relationships should also be analyzed issue by issue. Heifetz et al. (2009) provide a useful framework. They categorize stakeholders' relationships to issues as allies, opponents, senior authorities, casualties, and dissenters. Allies are those who might be supportive of the agency's likely position on the issue or supportive of the agency itself. The key questions for examining allies are to consider why they are supportive, their main objectives, and how relationships with them can be used to help the agency be successful.

Opponents stand to experience a loss if the agency is successful on the issue. Key considerations for opponents are to understand the nature of their losses, what affects how and when they experience their feelings of loss, and ways of possibly mitigating their losses.

Senior authorities provide critical resources for the agency and authorize its work. Sometimes regulatory work raises tensions in a country, which affect senior authorities, such as parliaments. The key questions to address regarding senior authorities include: (1) Why are they important? (2) What signals are they giving about the agency's work? And (3) what actions are needed to ensure continued support by the senior authorities?

Casualties are those who will exit the scene should the agency be successful, such as employees who might lose jobs because of an efficiency-improving initiative. Casualties are rare in regulatory contexts. The primary considerations in their regard are to ensure the agency is ready to cope with the casualties losses

(our better natures lead us to avoid inflicting pain on others) and has done all it can to soften the casualties' losses.

Dissenters are those whose nature leads them to champion radical ideas or raise uncomfortable challenges. Sometimes they raise important insights, so the agency should consider which of the dissenters' ideas are most valuable, how the dissenters might be enabled to constructively present and develop those ideas, and how the agency can help the dissenters avoid being marginalized.

II. Regulatory Power Relationships in the Caribbean

We utilize some aspects of Section I's framework to examine power relationships between utility regulators and stakeholders in the Caribbean. We accomplish this by surveying utility regulators in the region in the fall of 2016. In particular we sought volunteers within agencies that are members of the Organisation of Regulatory Utility Commissioners (OOCUR). We contacted people directly and OOCUR also distributed the survey. All responses were voluntary and anonymous.

The survey asked four questions. The first question was:

1. Identify the four stakeholders on whom your agency has the greatest impact. Consider each stakeholder's highest priorities and degree to which your agency impacts them.

Each respondent was given 11 options: (1) Media; (2) Government; (3) Opposition Parties; (4) Prime Minister/ President; (5) Politicians; (6) Industrial Customers; (7) Residential Customers; (8) Electric Utilities; (9) Water Utilities; (10) Telecom Operators; and (11) Other. Then the respondent was asked:

2. For each stakeholder that you chose as one of your top four, describe in detail what each stakeholder most wants from your agency. Please be as complete as possible.

The third question was:

3. Identify the four stakeholders that are most able to affect your agency. Consider what is most important for your agency to be able to do its work and the ability of each stakeholder to affect ability to do your work.

Respondents were given the same options as with the first question. Then the respondents were asked:

4. For each stakeholder that you chose as one of your top four, describe in detail what you need from that stakeholder.

Forty-one individuals responded to the survey, although not all of them answered all four questions.

Figure 3 shows the results from question 1. Because respondents represented agencies that vary in which sectors they regulate, we combined the results for water, energy, and telecommunications utilities. We compiled the results by counting the number of times each stakeholder was included in a respondent's top four and dividing each count by the result for the stakeholder that was included the most. The regulators believed that they most affected utilities, then residential customers, then industrial customers, and then the government.

[PLACE FIGURE 3 ABOUT HERE]

Figure 4 shows the results from question 3. As with question 1, we combined the results for water, energy, and telecommunications utilities, and we compiled the results by counting the number of times each stakeholder was included in a respondent's top four and dividing each count by the result for the stakeholder that was included the most. The regulators believed that they are most affected utilities, then the government, and then equally by politicians and the media.

[PLACE FIGURE 4 ABOUT HERE]

We are interested in the imbalance of power between the agency and stakeholders. We do not believe that power should be balanced because, while regulatory institutions should be independent, they would also be held

accountable for their work. Accountability can be effected only if there is an imbalance of power.

Figure 5 illustrates how we combine the results of questions 1 and 3 to examine power imbalance. We construct Figure 5 by subtracting the results for question 3 from the results for question 1, so Figure 5 represents the power imbalance from the regulator's perspective. The regulator has the greatest power deficit relative to the government, which is probably appropriate since the regulator is held accountable by the government. (Jamison and Castaneda 2014) However, for the regulatory agency to maintain independence, this power imbalance has to be regulated by the authority, budgetary, and other system processes mentioned in section 1.

[PLACE FIGURE 5 ABOUT HERE]

The regulators believed their next greatest power deficits were with the media, the heads of government (prime ministers and presidents), and politicians. As in the case of government, a power imbalance is appropriate in the case of heads of government and politicians as this enables accountability. The imbalance with the media is unsurprising and indicates a need for regulatory agencies to manage their media relationships well by ensuring that each is comfortable with the other, understanding the media's contexts, performing well in the transaction with the media, and analyzing the media issue by issue. Erickson and Ward (2015) provide a manual on this work.

Figure 5 also shows that the regulators believe that their power relationship with utilities is balanced relative to other relationships. Since our data are ordinal and highly aggregated we cannot say that the regulators believe that power in the relationship is indeed balanced. If the regulators experience the power as balanced, then they would also experience frustration in trying to hold the energy, water and telecommunications providers accountable for performance. The net

power that regulators believe they have relative to customers is indicative of the customers being in the secondary tier of stakeholder relationships.

We analyze the results of questions 2 and 3 using word clouds. A word cloud visually represents the relative prominence of words in a text. Words that are more prominent are represented with a larger font than less prominent words. For these questions, survey respondents were asked to describe what stakeholders want from the regulatory agency and what the agency needs from them. In effect this looks at the stakeholder transaction. We processed their answers by removing unimportant words, such as "the"; adapting text so that synonyms (such as reliable and dependable) were represented by the same word; and hyphenating words that belong together (such as reliable service) so that the word cloud does not separate them.

Figure 6 shows what the regulators believe the government wants from the agency. The most prominent words are those that relate to keeping the citizenry happy (low prices, quality and satisfied voters) in accordance with the way the government wishes the regulated companies to perform (follow policies) and providing revenue for the government (license fees). The prominence of the word "control" would imply that some regulators believe that the government would like to manage the regulatory agency closely.

[PLACE FIGURE 6 ABOUT HERE]

Figure 7 shows what the regulators indicated that they want from the government. The prominence of words like "independence", "non-interference", "clear policy", "relevant policy", "clear roles", and "funding" indicate that the regulators view themselves as largely wanting to be clear on what their jobs are, and to have the authority and resources to perform their jobs. Comparing Figures 6 and 7, a story emerges that, from the regulators' perspectives, their ability to gain authority and resources is sensitive to whether the citizenry is comfortable that the regulators are doing a good job. This is consistent with Heifetz's (1994)

explanation that people grant authority to others, whether formally or informally, only as long as the person receiving the authority uses it to provide the services that the others want.

[PLACE FIGURE 7 ABOUT HERE]

As Figure 5 shows, another relationship where the regulators viewed themselves has having less power is with the media. No respondents completed question 2 regarding what the media wants from the regulatory agency, but they did answer question 4 with the media as a stakeholder. Figure 8 shows that the regulators want reporting that accurately reflects what the regulators believe are the most important facts and reporting without a particular slant. The other side of the transaction is to give the media things that it wants. As Summerville (1999) explains, successful media enterprises give readers, listeners and viewers something to be excited about that reflects urgency and importance. So for regulatory agencies to be able to get into the media what they want, they should help the media frame the information in a way that attracts an audience.

[PLACE FIGURE 8 ABOUT HERE]

The other significant relationship according to our survey is that between the regulated operators and the regulatory agency. The survey respondents believed that the regulator had more power over the utilities than over any other stakeholder, and that the utilities had more power than any other stakeholder over the regulatory agency.

In the regulators' view, utilities vary in what they want depending on the sector. Telecommunications operators largely want minimal regulation and symmetric treatment of all service providers. This is different than what water and electric utilities want probably because telecommunications is largely competitive and regulatory oversight could be seen by service providers and interfering with their abilities to complete. In the less competitive sectors – water and electricity –

utility regulators oversee prices and so directly affect these providers' commercial viability.

Because survey respondents viewed the water and electric sectors similarly, we show only the results relative to the electric sector. Figure 9 shows what respondents believed electric utilities want from regulators and figure 10 shows what regulators want from electric utilities. The utilities emphasize commercial success and freedom to respond to customers as they understand the customers' interests. The regulator's greatest interest is in obtaining information. This is consistent with one of the primarily motivations for having an agency devoted to regulating a sector, namely to build and apply expertise. Beyond that the regulators varied in what they want, with cooperation, reports, participation and transparency being consistent with the desire to build and provide expertise, and issues such as avoiding unfair lobbying, no unnecessary challenges, non-interference, and respect being consistent with the regulators' desire for independence and latitude to perform their work. Desires such as fairness, reasonable costs, effectiveness, efficiency, and compliance relate to regulators' desires to satisfy their political authorities by satisfying customers.

The overarching picture that emerges, as we see it, is consistent with Jamison's (2015) view that regulation is about disappointing people at a rate that they can endure, and Heifetz's (1994) idea that authority is a transaction for services. The regulators appear to desire relationships that provide them with the tools and information needed to be accountable to their political authorities. They appear to be keenly aware that they will be allowed to do their work only if they manage the losses that politicians and customers experience when customers view prices as high or increasing, or service as sub-standard or declining, and the losses that utilities experience when they struggle with profitability and customer satisfaction.

III. Conclusion

In this paper we examine power relationships in utility regulation by exploring the beliefs of utility regulators in the Caribbean regarding their relationships with utilities, customers, the media, and politicians. We find that regulators appear to view their relationships in a context of the work they have to do and the importance of managing those relationships in a way that enables cooperation. In effect the regulators do not give each stakeholder everything it wants, but instead distributes losses in a way that allows the regulatory system to be sustainable.

It would be interesting as a next step to see how some of the stakeholders view the situation. A proper stakeholder analysis looks at relationships in context, so future research should survey politicians, operators, and media to understand their networks of relationships and how they consider their relationships with utility regulators.

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Figure 1. Who delivers what in utility regulation

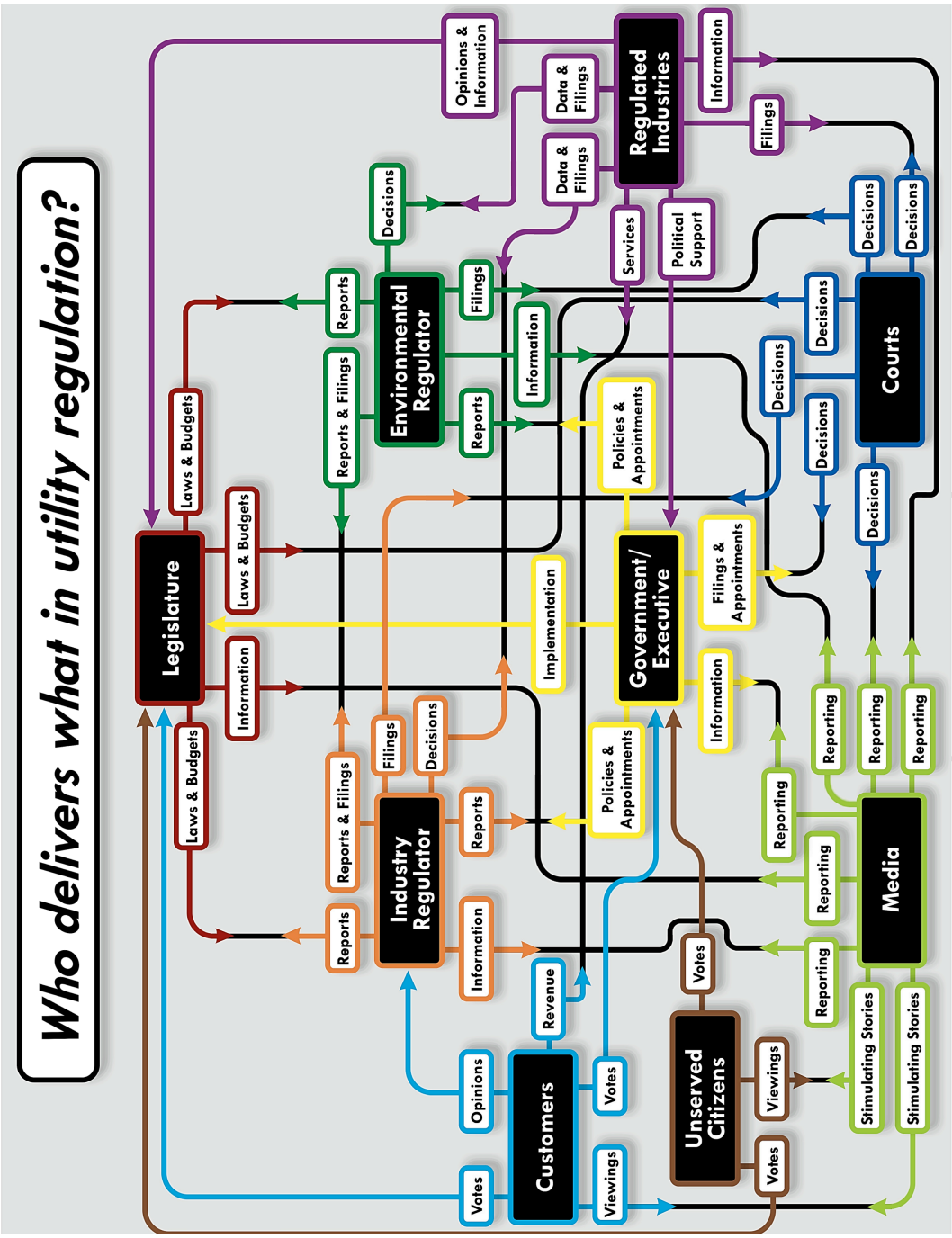

Figure 2. Power relationship matrix

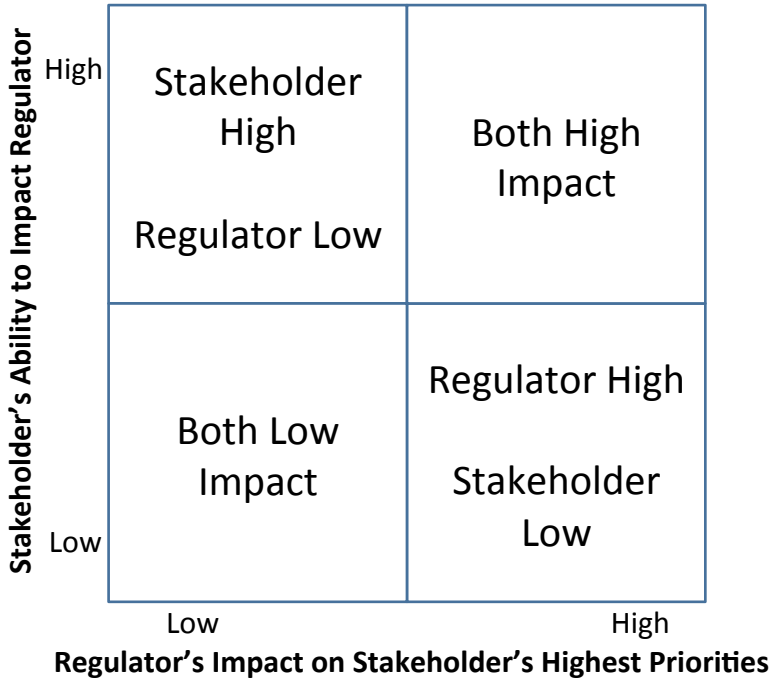

Figure 3. Caribbean regulators' opinions on which stakeholders they affect the most

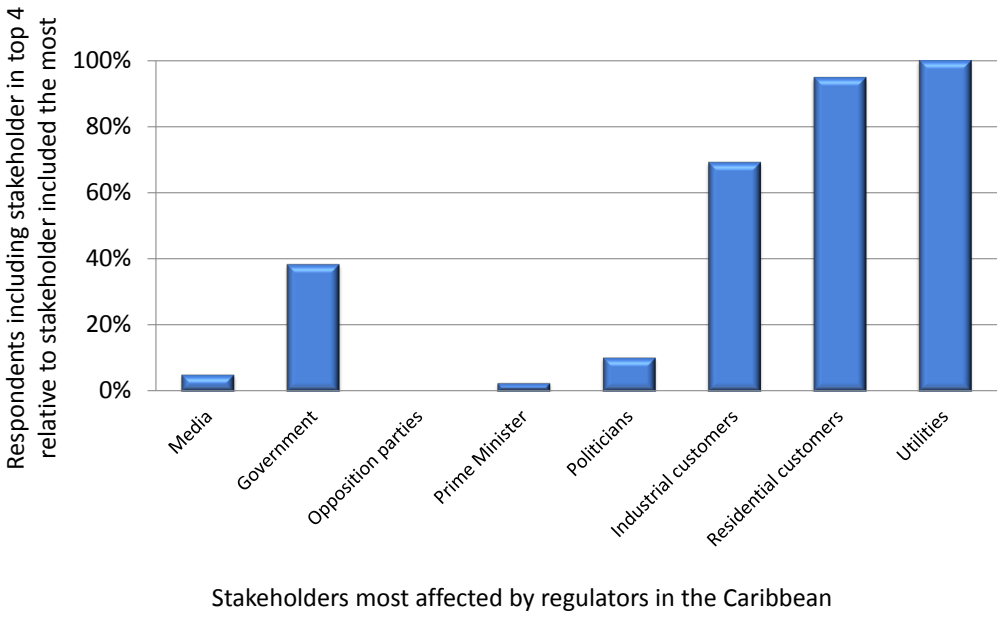

Figure 4. Caribbean regulators' opinions on which stakeholders affect them the most

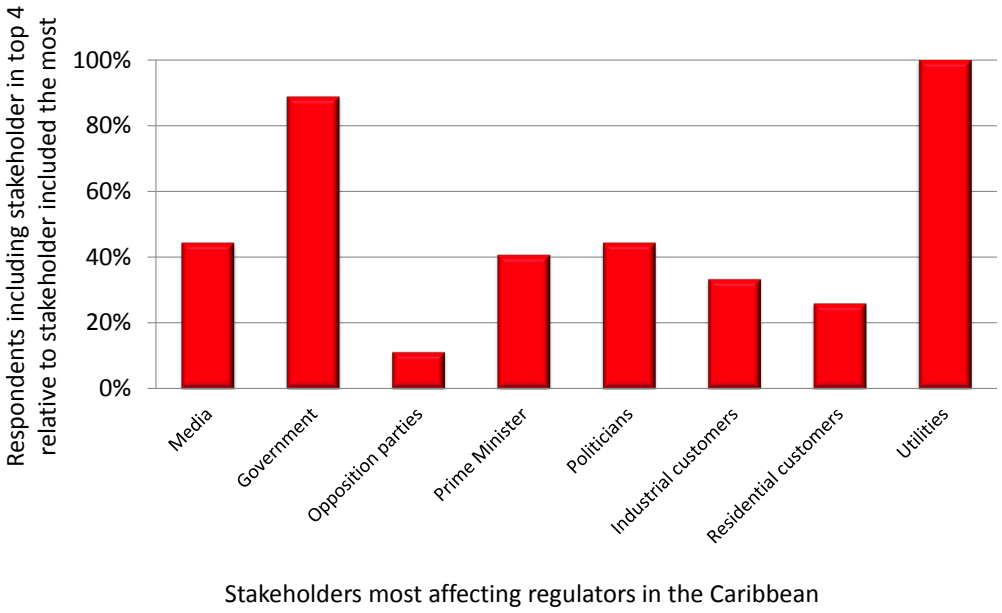

Figure 5. Difference between regulator's power over stakeholder and stakeholder's power over regulator based on Caribbean regulators' opinions

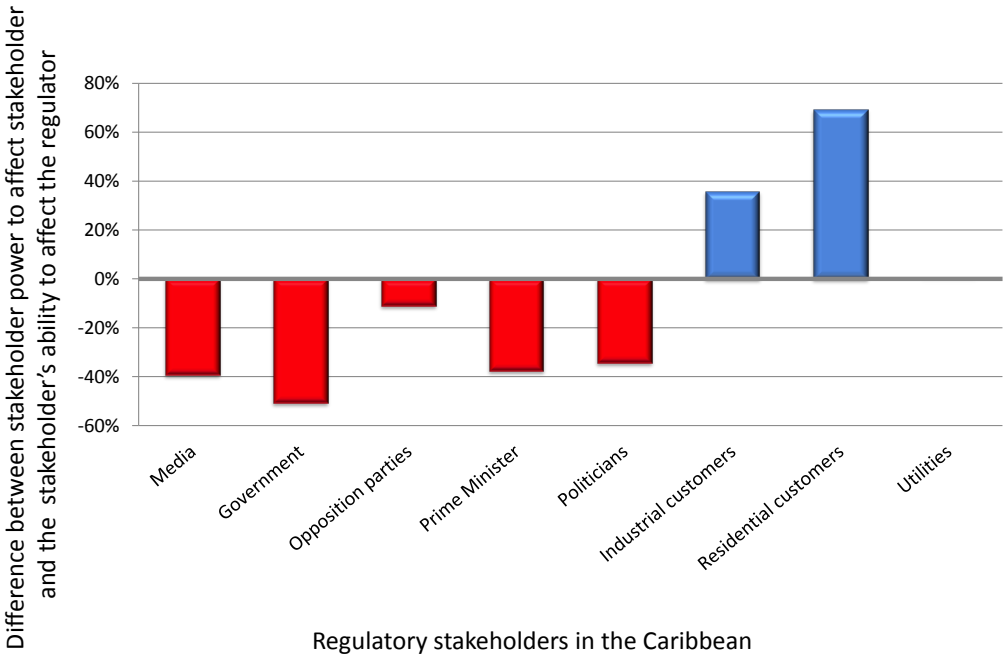

Figure 6. Word cloud of what regulators believe that the government wants from the regulatory agency

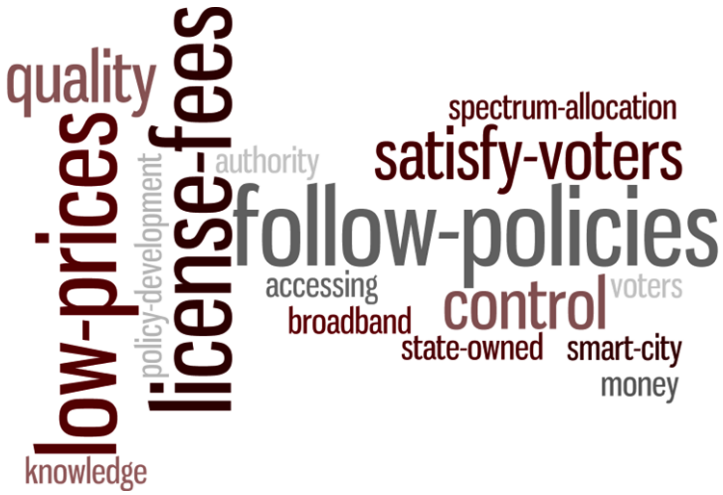

Figure 7. Word cloud of what regulators want from the government

Figure 8. Word cloud of what regulators want from the media

Figure 9. Word cloud of what electric utilities want from regulators

Figure 10. Word cloud of what regulators want from electric utilities