Lessons from the World's Utility Regulators

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When utility regulators from around the world get together for intensive discussion of their most challenging issues, everyone learns a lot, including the teachers. This is the experience of the Public Utility Research Center (PURC) at the University of Florida. PURC, which is sponsored by the Florida PSC and Florida utility companies, conducts international training programs for utility regulators. Our biannual flagship program, the *PURC/World Bank International Training Program on Utility Regulation and Strategy*, has trained over 600 regulators from 90 countries since its inception in January 1997. In addition, PURC has conducted specialized programs for the Florida PSC, Australia and New Zealand regulators, Latin America telecommunications policy makers, the Caribbean telecommunications government officials, Peru's water regulators, Argentina's gas regulators, the Alabama PSC, the New York PSC, and the Massachusetts DPU. PURC has also lectured on regulation China, Mexico, Hungary, Brazil, and Saudi Arabia. (More comprehensive information can be found at http://www.purc.org.)

The insights that regulators from developing and developed countries alike can share never cease to amaze us. Each country's situation and problems are unique, but there is a common set of principles and lessons that each country can draw upon to fashion its own policies. As US state and federal regulators continue their work with regulators from other nations, it is useful to review some lessons that have emerged from PURC's outreach and research.

The market model is critical to all other decisions.
Governments should consider how much competition will occur and where it will occur before settling issues such as privatization, interconnection, incentive regulation, and universal service. The UK started with pure price cap regulation for BT, but had to shift to something closely resembling rate of return regulation because competition did not develop as quickly has had been hoped. US policies for long distance, Internet, and local telephone interconnection, and for telecom line-of-business restrictions, were created under continually changing assumptions about the nature and extent of competition. All of the old assumptions have proven false and now out-of-date regulatory tools sometimes shackle US regulators.

Uncertainty causes investors and businesses to worry and they avoid situations that present continual surprises. Some energy companies have pulled out of international markets because of uncertainty over profits. Because the success of utility market reform depends upon business incentives to serve customers, improve efficiency, and expand capacity, policy makers should provide an environment in which managers can plan and investors can earn profits commensurate with their risk.

Deciding the market model is difficult, so governments often delay the decision or continually revise it. Chile led the world in opening electricity markets to competition. Because it was first, Chile made mistakes and so is revising its market and regulatory models. The UK abandoned its duopoly in domestic telecommunications when Mercury proved to be ineffective competitor for

BT. Globalization made Hong Kong's telecommunication monopoly unsustainable, so Hong Kong compensated Cable & Wireless for bringing its exclusive license to an early end. Companies in Colombia bought long distance licenses for US$150 million each, only to find that private lines and voice over IP made it impossible for the government to keep others from providing substitute services. India has experienced delays in power projects because changes in government policy made investors back off.

Independence and transparency are essential for effectiveness.
One of the primary purposes of regulation is to provide for the long-term efficiency of utility services. Too often regulators are pressured to avoid decisions that cause short-term political or financial pain. In Hungary, government elections caused delays in electricity price increases even though investors had been promised the higher prices. Mexican regulators have been reluctant to force Telmex to lower its long distance access prices, which are higher than Telmex's retail prices for long distance. Clear statutory authority, budgets independent from the operator and ministry, and fixed terms of office help regulators resist this pressure, but a strong will is critical. For example, the regulator in Jamaica developed its independence by challenging the government on a price increase for Cable & Wireless.

Transparency means that regulators operate in the open, including public decision making, published decisions, and explanations of decisions. The energy regulator in Ontario established public working groups to address gas competition issues. The UK water regulator provides an extensive web site of information, but other UK regulators have been criticized for not explaining decisions. Transparency safeguards regulators' independence and leads to legitimacy and credibility. Legitimacy means that consumers trust the regulator because they view the regulator as independent from the industry. Credibility means that investors trust the regulator because they view the regulator as dependable and able to withstand shifting political winds.

Commitment and flexibility are important for investment and efficiency.
Without commitment, businesses lose confidence in the government. New entrants have been slow to develop their businesses in certain Latin American countries where regulators are seen as favoring incumbents. Several energy companies pulled out of the UK after the government clawed back profits that had been earned under the government's incentive regulation schemes.

Businesses should bear their normal business risks and be allowed keep profits that are due based on the commitments policy makers have made. When regulators let businesses, consumers, or politicians change the rules when the going gets tough, investors see this as increasing risk and require higher returns and shorter payback periods. Higher required returns mean higher prices, which make customers worse off. Regulators can often be better off opting for competition and deregulation, which research has shown generally reduce costs, improve services, and cause businesses to focus on markets rather than political processes.

Today's regulators share jurisdiction and issues.
Technology change and economic globalization are revolutionizing infrastructure. Telephone service is a thing of the past. Soon, voice telecommunications will simply be a software application provided by the likes of America Online, and issues that have occupied regulators for many years -- cost allocations, subsidies, billing practices, telephone numbers, etc. -- will become moot. Companies and markets are becoming regional and global, forcing regulators to collaborate across national boundaries and to increasingly work with antitrust authorities around the world. The EU, US DOJ, and US FCC regularly communicate with each other on telecommunications mergers. Norway and Sweden have formed a common energy market.

Countries in Africa and in the Caribbean have held discussions about creating regional regulatory agencies in their respective areas.

We have much to learn from each other.
A recent attendee of our biannual program, who was from a developed country, commented to us on how much he learned from the regulators from developing countries: "I thought that regulators in my country had done a superior job addressing regulatory issues. Seeing so many other countries solving problems in so many creative ways showed me that we could all learn from each other." As we move forward in improving the world's utility infrastructure, we will all share this regulator's experience.