

## Survival Guide for the Independent Regulator

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When the Governor of Iowa appointed Dennis Nagel to be chairperson of the Iowa Utilities Board several years ago, the only thing the Governor requested is that Dennis not do anything that would cost the Governor the next election. The Governor didn't mention protecting consumers, protecting shareholders, or obeying the law. The Governor asked only that Dennis not cost him the next election.

Reality for regulators is that their job is to provide stability so that long-term investments that benefit consumers can be made (Goldberg, 1976; Levy and Spiller, 1996; Spiller and Savedoff, 1999; Belt, 2004). However, in real life, regulators are frequently at the center of controversy. Consider the following headlines:

- “The RIC – are they really here to protect?” is a story criticizing Trinidad and Tobago’s Regulated Industries Commission for protecting the incumbent telecom operator, TSTT, by shutting down rival Voice over Internet Protocol (VoIP) services. (*Trinidad & Tobago Express*, 2004)
- “OUR budget still awaiting cabinet approval,” is a story about the Jamaican government’s delaying funds to the Office of Utility Regulator (OUR) (*Jamaica Gleaner*, 2000)
- “Unhappy with consumer protection, OUR,” is a letter to the editor complaining that the OUR protects operators and managers with fat salaries, not consumers. The letter calls for the OUR to be independent! (*Jamaica Gleaner*, 2001)

What happens when your job is to provide stability, but you find yourself in the middle of controversy? The regulator in the Netherlands lost certain elements of its independence when it had to remake numerous decisions that had been based on faulty data. In Slovenia a regulator lost his job when he let both prices and profits increase (Ajodhia et al., 2004). In Zambia a regulator was fired for allowing a politically unpopular price increase even though the increase was required by law. In Tennessee politically active commissioners lost their jobs when the legislature rewrote the utility laws specifically to make commissioners less active politically.

These examples show us that being an independent regulator is dangerous work. This is true for at least two reasons. First, for the regulator to become independent, someone else must lose something valued:

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- A minister gives up political power and some ability to control political tensions.
- An operator loses opportunities to apply political pressure.
- Some consumers lose means for gaining favorable treatment.

Sometimes people who suffer a loss attack what they believe to be the source of the problem, which in this case is the regulator. The second reason regulation is dangerous work is that in developing and refining its independence, the regulator becomes a player in a political process.

My purpose in this paper is to explain why the work of the regulator has perils and to describe some ways regulators can survive and thrive. The techniques I describe can be done even without formal authority. I begin by explaining what I mean by independence and summarize hazards of regulatory work. I then describe the regulator's leadership role and some tools that regulators can use to succeed.

### **Independence**

Regulatory independence generally means arm's-length relationships with operators, consumers, private interests, and political authorities, and organizational autonomy with respect to the government (W. Smith, 1997). An arm's-length relationship with the operator generally involves restrictions on regulators and regulators' family members having stakes in the operator's financial success. For example, regulators in the Bahamas had to sign affidavits affirming that a licensing decision was not influenced by a staff member's relative, who happened to have a financial interest in the licensee (J. Smith, 2004).

Organizational autonomy and an arm's-length relationship with the political authorities are generally accomplished through earmarked funding, fixed terms for appointment and restrictions on removal from office without cause, statutory or constitutional authority, and court reviews of decisions rather than ministry reviews. Decisions by the Uganda Communications Commission (UCC), for example, are reviewable only by special court tribunal, not by any ministry. Political independence also means limits on ex parte communications with politicians. When Dan Fessler became Chairman of the California Public Utilities Commission several years ago, he began receiving phone calls from politicians telling him how he should vote on upcoming decisions. Dan dealt with this by saying, "I appreciate your sharing your insights. In California, the Public Utilities Commission is required to base its decisions on the public record. If you would please send me a letter stating your request, so that I can put it in the public record for all to see, I will give it full consideration." The calls soon stopped.

But independence does not mean that the regulator answers to no one, as Benskin-Murray (2004) has pointed out. The regulator is constrained by laws, political realities, public sentiments, budgets, and license provisions, for example. Independence is not absolute because trade-offs exist between independence and accountability, between certainty and flexibility, and between long-term goals and short-term viability. This lack of absolute independence is generally considered desirable because it ensures that the regulator doesn't simply follow a personal agenda.

## **Independence is Dangerous Work**

When trade-offs have to be made, stakeholders sometimes lose things that they value and are tempted to strike back, for example, by trying to marginalize the person or agency that they perceive as the threat. This is what happened in Panama when the regulator tried to enforce service quality rules on Cable & Wireless. The operator renegotiated its license with the ministry in a way that removed the regulator's ability to enforce service quality standards. In South Dakota, a regulator was marginalized when a judge recused him from all cases involving the incumbent telephone operator, US West, because the regulator and the company had become involved in personal disputes that eventually led to lawsuits.

Regulation is also hazardous work because when you play a role in developing and shaping policy, you have become a player in a political process. Sometimes regulators are thrust into playing formal roles in policy development. The U.K. government asked its regulators to provide input on a review of regulation in the country. The U.S. Federal Communications Commission (FCC) was asked to testify before the U.S. Congress during the writing of the U.S. Telecommunications Act of 1996. Because making policy is a political process, regulatory participation creates an unavoidable friction between the regulator's policy-making role and the regulator's political independence.

Even if you as a regulator do not play a formal policy role, you always play an informal leadership role in policy development because your actions define your independence. For example, the decision by the Bahamas Public Utilities Commission to defend its licensing work made the PUC a player, but remaining silent would not have been a neutral act either (J. Smith, 2004). In Trinidad and Tobago, the RIC had to choose whether or not to fill the regulatory void that occurred when the government delayed establishing the Telecommunications Authority. Both action and inaction had implications for how the RIC would be viewed by the ministries, the Parliament, the Telecommunications Authority, and other stakeholders.

## **Authority versus Leadership**

Leadership in an informal policy role is different from the regulator's formal authority role. Regulators are given authority to provide answers and stability, maintain norms and order. In contrast, leadership is about "mobilizing people to tackle tough problems" (Heifetz, 1994, p. 15). Leadership raises questions and forces people to face difficult problems.

Let me illustrate the difference between leadership and authority with a story from my experience at Sprint, where I worked from 1993 to 1996. The passage of the U.S. Telecommunications Act of 1996 presented a difficult dilemma for Sprint. The Act pitted long distance companies against traditional local telephone companies, and Sprint was in both lines of business. Up until that time, Sprint had played both sides of the fence in regulatory debates and sometimes held contradictory policy positions because it was effectively two companies – a long distance company and a local telephone company.

My colleagues and I thought the Act would force the corporate executives to set Sprint's business direction. We were wrong, which left us frustrated. I asked a colleague what I should do. She advised me,

“Mark, just act like you are in charge and see what happens.” To make a long story short, even though I was at a low management level in the company, I took her advice ... and it worked. I identified issues, recruited teams to draft unified policy positions, announced deadlines, and kept everyone in the loop: Within the company, the work was completely transparent. The executives noticed and adopted our work as the official corporate policy agenda. I had no authority to do this, but by defining the work and asking people to get involved, I helped bring about a positive change in Sprint’s corporate identity.

A regulator may need to exercise leadership in doing the work for which he has formal authority. This was the situation that Rohan Samarajiva faced when he became the Director General of Sri Lanka’s Telecommunications Regulatory Commission in 1998. Sri Lanka had recently adopted telecommunications reforms that included significant domestic price increases. Samarajiva was required to allow the price increases, but he knew there would be a large public outcry. He quickly established an arm’s-length relationship with the operator by demanding complete documentation of the price increase. He signaled a new form of transparency for the agency by holding the agency’s first-ever press conference and by hosting consumer call-in programs on broadcast radio, which also demonstrated that he cared about the impact the price increases would have on consumers. He further recognized the effect of the price increases on consumers by requiring the operator to offer a low-use tariff (Samarajiva, 2001).

### **Get on the Balcony**

What are the steps a regulator can follow to exercise leadership and not only survive, but thrive? Entire books are written on this topic (see, e.g., Heifetz, 1994; Heifetz and Linsky, 2002; and Laurie, 2000), but I will summarize some of the main techniques based on my experience; namely, getting on the balcony, identifying the adaptive work, creating a holding environment, and modeling behavior.

Getting on the balcony is a metaphor for seeing what is really going on. When you are dancing on a dance floor, you can see yourself and the people immediately around you. That gives you one perspective on what is happening. But if you leave the dance floor and get up on the balcony, you can see everything that is going on, i.e., who is dancing and who is not, how the music affects different dancers, where dancers are on the floor, etc. You also see that your dancing is affected by things that you cannot see from your vantage point on the floor (Heifetz and Linsky, 2002, pp. 51-74).

I failed to get on the balcony when working for the regulatory agency in Iowa. I was given the task of rewriting rules on how the telephone companies would perform cost studies. I attacked this as a technical challenge and wrote a proposal that correctly applied the most current economic theories. I then invited industry economists to join me in what I thought would be a series of consensus-building workshops. I was wrong. The workshops were a disaster. Industry economists derailed the first two workshops by debating issues tangential to my proposal. The people who derailed the first two workshops didn’t attend the third, so I was able to get consensus on an outline of a new policy. However, when I presented this outline to my commissioners, they flatly rejected it. My process stalled. I had failed. But

my failure was not a result of my not understanding the issues – it was a result of my not getting on the balcony.

If I had gotten on the balcony, I would have seen that the people who derailed the workshops did so because the industry did not want well-defined costing rules. I would also have seen that my commissioners needed well-defined costing rules so that the rules could withstand court challenges. I would have realized that consensus was impossible and would have adopted a process that defined issues and clarified perspectives, not one that unrealistically sought consensus.

How can a regulator get on the balcony? The first step is to step away from the fray and ask yourself what is going on: Who cares about the actions you are taking? What are their motivations and how are they responding? You should also take notice of what you are doing and why (Heifetz and Linsky, 2002; Laurie, 2000; Goleman, 1994; Cooper and Sawaf, 1997).

### **Identify Adaptive Work**

Another important element of being on the balcony is identifying the adaptive work to be done and who has to do it. Adaptive work involves changes in values, traditions, attitudes, and behaviors that people hold dear (Heifetz and Linsky, 2002, pp. 11-20). Patrick Masambu, the Executive Director of the UCC, helped his country perform adaptive work in the mid-1990s when the government was beginning to move toward privatization and liberalization of the country's telecommunications. As Managing Director of Uganda Telecomm Limited (UTL), the country's state-owned operator, at the time, Patrick looked ahead and realized that these policy changes were important for his country. So he refused the temptation to resist the change and instead helped his people and the labor union see the future. Because he also recognized that privatization would mean a new management team for the company, he left UTL and joined the UCC. He is now using the agency to help the country adjust to global telecommunications by engaging operators, ministries, his staff, and representatives of nearby countries in a dialogue that has involved Public Utility Research Center workshops and exchange meetings with neighboring countries.

### **Create a Holding Environment**

While getting on the balcony is an important step, it is also important to quickly get back into the fray and orchestrate the process in a way that allows adaptive work to be done (Heifetz and Linsky, 2002, pp. 53, 101-122). This involves both lowering stress when people are feeling overwhelmed and increasing stress when people are refusing to engage in the work that needs to be done. This is called creating a holding environment.

Dennis Nagel of the Iowa Utilities Board created a holding environment for his fellow U.S. state commissioners in 1993 when he helped them see that the days of monopoly telephone service, with its implicit subsidies and traditional utility regulation paradigm, was coming to an end. He created a unique event – a regulatory summit for state commissioners only – at Keystone, Colorado. The uniqueness of the summit and the power of the presentations focused attention and shook traditional paradigms. He included

in the event discussion groups that involved commissioners in adaptive work and let them process the things that they were hearing. After the summit, the commissioners continued to work in task groups, which helped them focus on manageable tasks while not losing momentum. In part as a result of Nagel's work, state regulators played a leading role in opening U.S. local telephone markets to competition.

### **Modeling Behavior**

Another important tactic is modeling behavior (Heifetz and Linsky, 2002, pp. 95-98, 108-109). It is important because it shows others that the regulator recognizes what others are giving up (things they value) for change to occur, and it shows that the regulator is willing to pay the price for change as well.

PURC's previous Director, Sandy Berg, used this approach in helping me establish myself as PURC's Director this year. Sandy had been in charge of PURC for approximately 30 years. In a very real sense, PURC was Sandy and Sandy was PURC. People liked PURC because they liked Sandy. Furthermore, he was and is the heart and soul of the PURC/World Bank International Training Program. When he decided to hand the reins of PURC over to me, he faced a difficult problem: How could he remain involved in PURC's outreach activities that he loves so much (Sandy continues to play a very active role in PURC) without undermining my role as Director? He accomplished this by modeling the behavior that he expects of others at PURC. He has completely stopped making the decisions he used to make. He never refers to how things used to be, never compares his and my management styles except to compliment me, and always accepts every decision made in PURC, even when he disagrees.

Ansord Hewitt of the OUR also used this tactic recently. At a University of West Indies seminar, he was asked about a telecommunications policy issue facing Jamaica. The first thing he said was that the OUR does not set policy, then he provided the questioner with the information she sought. In framing his answer this way, he modeled the behavior that is necessary for his colleagues at the OUR and his counterparts in the Jamaican government to exhibit if they are to honor the distinction between the OUR and the government.

### **Conclusion**

In this paper I have tried to describe how a regulator can survive and even thrive in the work of exercising leadership as an independent regulator. I described the difference between the regulator's leadership role and her role as an authority. I also talked about the need to get on the balcony, identify the adaptive work that needs to be done, create a holding environment, and model behavior.

I would like to close with a saying attributed to Lao-Tzu: "A leader is best when people barely know that he exists. Of a good leader, when his work is done, people say, we did this ourselves." I believe this describes the challenge of the regulator exercising leadership. The regulator is sometimes called upon to do the work of leadership, but she must do so in a way that focuses attention on the work and not on her. To do otherwise compromises her position as an independent regulator.

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