



Improving Governance of the Energy Sector **Leonardo Giacchino, Ph.D.**

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What is Regulatory Independence?

- You ask this question to 100 people and you might get 100 different answers;
- The fundamental economic goal of regulation is “to mimic a competitive market outcome, even when the underlying market is not competitive;”
- What is regulatory independence is answered when understanding the three main tasks by a regulator:
 - Protect consumers (avoiding non competitive prices);
 - Provide for the industry viability (allowing regulated companies the opportunity to recoup their costs and obtain a reasonable return); and
 - Implement government policies;
- The regulator looks after the interests of the many parties involved and cannot be judge and party at the same time.

How is Regulatory Independence Shaped in a Certain Jurisdiction?

- The operating environment shapes how a regulator looks after the interests of the many parties and acts more or less “independently:”
 - The legal system is key. International experience shows different outcomes depending on common and civil law frameworks;
 - A solid regulatory compact fortifies the reliance on the regulator;
 - Length of regulatory system in place;
 - Trust of stakeholders in institutions;
 - Time consistency of decisions by different governing political parties; etc.
- In some countries regulatory independence could be present in a period and gone the next, undermining investments in the industry;
- Regulatory independence is more than a concept or a fashionable phrase, it must be adopted and implemented.

Policy, Implementation or Both?

- It is important to discern between the roles of policy making and policy implementation:
 - Policy making refers to providing input into political and economic policies that inform laws and regulations; and
 - Policy implementation refers to the practice of taking policy as given by statute of Ministry rule and implementing regulations to put that policy into effect;
- Regarding international best practices, there is strong consensus that the role of the regulator should be limited to policy implementation. This results in a more disciplined regulator, who must work within a given set of parameters to achieve a fair and neutral outcome;
- By contrast, a regulator that is too involved in the policy making process has incentives to affect policies for the sake of determining a specific short-term outcome rather than acting to ensure the long run viability of public policies;
- Too much involvement in policy might affect the perception of how “independent” a regulator might be.

More “Regulatory” Concepts

- Regulatory experts love to attach the word “regulatory” and increase the number of concepts discussed in the field:
 - Regulatory Independence: that is what we are discussing;
 - Regulatory Discretion: the consensus is that the less the regulator has to be involved, the better; and
 - Regulatory Certainty: always demanded by the investors. In some places, they only talk about regulatory uncertainty and/or regulatory surprise;
- Regulatory discretion is not so bad if you had a good independent regulator that is fair;
- Unfortunately, fair and independent regulator are not constant through time;
- Regulatory discretion could be bad in a civil code country. The preventive move is to have all procedures and methods written down, minimizing discretion. Though this last sentence works everywhere;
- Regulatory discretion and regulatory certainty are very correlated. The more (bad) discretion, the (less) regulatory certainty.

Ultimate Goals in Designing a Regulatory Framework

- Independent regulator from other branches of government and the parties in the industry;
- Judiciary in the path of appeal;
- The regulator implementing policy and acting as consultant in policy issues to the energy agency in the Executive;
- Procedures and methodologies developed by the policy agency;
- Well written procedures and methodologies, reducing the discretion on the part of the regulator; and
- Regulatory certainty is just a result of good implementation of the concepts discussed above.



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