

# Stand-alone funds to support regulatory independence: Has their time passed?

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## Introduction

Sri Lanka was an early adopter of telecom reforms. The process began with a unit headed by the late Ambassador Vernon Mendis as early as 1986-87. Due to the second JVP insurrection of 1987-89, the reforms could not be completed except for some elements such as the conversion of the Department of Telecommunications into a corporation and the establishment of the Office of the Director General of Telecommunications as the regulatory agency. I was told by some officials I interviewed for a book chapter in 1992 that the then Secretary of Treasury had vetoed a proposal to create a separate fund for the regulatory agency, saying that such funds would lack the safeguards built into the Consolidated Fund.

In 1996, Act No, 26 of 1991 was amended to strengthen the regulatory agency. This time, the fund proposal made it through. The reasons were many. It was considered best practice to fund national regulatory agencies through regulatory fees levied from the entities subject to regulation, rather than through general funds. Given instances of governments exerting pressure on regulatory agencies through the control of purse strings, a stand-alone fund controlled by the regulator was seen to be an important element of regulatory independence. In Sri Lanka, additional motivations included the need to compensate staff at levels higher than those in government. It was thought that paying salaries out of a separate fund would enable the Commission to shake free from government scales.

The recent High Court decision, *Democratic Socialist Republic of Sri Lanka v Pelpita* (HC 8026/15), found the Chair and Director General of the Telecommunication Regulatory Commission guilty of criminal misappropriation of LKR 600 million (USD 3.9 million) from the Fund. The decision is under appeal. Given the jail sentences and rather large fines that were handed down to two very senior officials (the former Secretary to the President was the second accused), the decision has been subject to much public discussion. The purpose of this note is to examine the implications for regulatory practice.

## Were the controls adequate?

Section 22F(3) of the Sri Lanka Telecommunications Act, No 25 of 1991 as amended, stated: "There shall be paid out of the Fund of the Commission all such sums of money as may be required to defray any expenditure incurred by the Commission in the exercise and performance of its powers and duties." The powers and duties are set out in Section 5 of the Act. The High Court Judge ruled that transferring money to an account of the Presidential Secretariat for the distribution of items of clothing accompanied by election propaganda through religious establishments in the week prior to the Presidential Election did not fall within the scope of the powers and duties set out in Section 5. He also found that the required approval by the Commission, comprising five persons including the two accused, had not been obtained prior to the transfer of funds.

The Sri Lanka Telecom Regulatory Commission is perhaps unique in having as its Chairman the Secretary of the Ministry responsible for the subject of telecommunication. This results in a rather unusual and power-laden dependence on the Ministry by the Regulatory Commission. The position of the Secretary is a powerful one. In addition to serving as the head of the policy making entity, under the Minister, the Secretary also serves as Chief Accounting Officer for all agencies under the Ministry. To make matters worse, since around 2005, the Executive President has chosen not to assign the Telecom Regulatory Commission to the Minister in charge of the subject of telecommunications. By default, the President then becomes the Minister referred to in the act and his Secretary, the most powerful of all government officials, becomes ex officio the Chair of the Commission.

The Director General (the CEO of the Commission, and the first accused) authorized the transfer of LKR 600 million from the fund of the Commission to an account controlled by the Secretary to the President, who also happened to be the Chair of the Commission and the Chief Accounting Officer of the Commission. The then President stated after the judgment was given that he gave the order, but he was not among those charged in the original case and there were no records of his order in the material considered by the Court. That the transfer was done without Commission approval appeared to the Court to be driven by the urgency of completing the distribution of the gifts of clothing before the election. But a plain reading of sections 22F(3) and 5 suggests that even if the Commission approved it, it would be unlawful. The fact that the Commission had already budgeted LKR 100 million for corporate social responsibility suggests that the Fund was being used for purposes not covered by section 5.

The High Court found that criminal misappropriation had taken place. One may be tempted to conclude that this was a singular aberration in the context of a re-election campaign that was not going well, the enormous power concentrated in the executive presidency prior to the 19<sup>th</sup> Amendment and in the President's Secretary in relation to the peculiar constitution of the Telecom Regulatory Commission in the period since the Commission came under the President. But the problem appears to be systemic.

Currently, the Chair serves ex officio. He/she ceases to function as Chair if removed as Secretary which the President can do anytime without giving reasons. Similarly, the only full-time Member, the Director General, serves at pleasure and can be removed by the Minister (the President in this case) without cause. The other three part-time members are appointed by the Minister and may be removed for cause or resign. If their principal livelihoods are dependent on the government, as has been the case for most of the time the Commission has existed, they are not likely to be truly independent. On many occasions, Members have been asked to resign and have meekly complied.

Unlike money in the Consolidated Fund of the government, Parliamentary approval is not necessary for disbursements from the Fund of the Commission. The safeguards are a collegial body that has to make decisions on the record and statutory provisions that strictly delineate the purposes for which the money can be expended. The details emerging from the court case suggest that the safeguards have been ineffective.

The extraordinary powers concentrated in the Chair of the Commission (even if the position is held by a common Secretary) and the fact that various government functionaries have been appointed as Members for the past 17 years suggest that without independent Members there can be no independent Commission. Without an independent Commission the safeguards for the fund cannot be effective.

## Should we get rid of stand-alone funds?

India's regulatory agency, the Telecom Regulatory Authority of India (TRAI), was created around the same time as when the Sri Lanka Telecommunications Act was amended to establish a separate fund for the Sri Lankan regulatory agency. However, TRAI does not have its own fund. Its staff are governed by the general rules applicable to government officials. It has functioned with funds obtained from the consolidated fund for two decades.

Does this suggest that stand-alone funds are unnecessary? It appears that stand-alone funds may be losing their appeal. The draft legislation to establish the Myanmar Communications Regulatory Commission did not include provisions for a fund. But, the draft is quite weak in terms of regulatory independence overall.

The rationale that a stand-alone fund would allow the payment of high salaries to regulatory commission staff and the ability to obtain the services of consultants may still hold true in certain countries. Therefore, it is important to identify safeguards for the stand-alone funds that remain.

## Safeguards that will work

The first and most important thing is that the amount of money in the Fund should not be excessive. Monies going into a regulatory fund should not include extraordinary or one-time payments such as those resulting from license or spectrum auctions. Such one-time payments should go directly to the Consolidated Fund. If the regulatory agency is responsible for managing subsidy programs such as universal-service programs such funds should ideally be maintained separately from regulatory funds. Mechanisms such as preset reductions in the levies when amounts accumulate above defined levels should be implemented to prevent undue and wasteful accumulations.

In addition, the regulatory agency's budget should be placed before Parliament every year and published for comment on the website. Another option is to approve the budget through a public hearing. This will create an opportunity for stakeholders who would benefit from an agency which lacks the resources to do its job well to advance their interests by hobbling the agency. Therefore, the approval procedure should be handled with caution. All funds in excess of the budget plus a margin such as 10 percent should directly flow to the consolidated fund.

Minimizing the quantum of money in the Fund should reduce the opportunities for abuse. If LKR 600 million was not lying around in the Fund, the criminal misappropriation would not have occurred.

The decision makers must be truly independent of government, but accountable. This would preclude the kinds of appointments made to the Sri Lanka Commission. Accountability is best enforced through transparency. Right to information requests can make financial decisions by the Commission transparent. Proactive disclosure is advisable.