

# Rationale for ex-ante, sector-specific regulation

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# Form of regulation under discussion

- Ex-ante as opposed to ex-post
  - Instead of waiting for bad things to happen (ex post), we act to prevent bad things from happening and to make it more likely that good things will happen → more intrusive → requires more specialized knowledge
    - Of course, consistent practices in ex-post regulation can have ex-ante effects
- Sector-specific as opposed to general (telecom regulation v competition regulation)
  - Also requires knowledge specific to industry + economic knowledge about competition/monopoly + law

# Historically . . .

- Infrastructure services were not supplied by governments
- Were first supplied by private entrepreneurs
  - Who were then subjected to various forms of controls
  - And were then “nationalized”
    - Except in the US, Canada, the Philippines, Latin America, and a few other places
- Starting in 1980s, remedies sought for weaknesses of integrated government-owned monopolies

# Current thinking on how infrastructure services should be supplied

- Markets
  - Which are subject to varying degrees of market failure
- Responses
  - Use non-market mechanisms: Government supplies directly OR
  - Remedy specific market failures with targeted solutions that will hopefully not exacerbate other problems

# Responses to market failure

- The cure must be no worse than the disease
- “Primum non nocere” (Above all, do no harm)
  - The oath of the physician is also applicable to policy maker

# **REGULATION IN THE CONTEXT OF SOLVING PROBLEMS**

# Problem: Supply inadequate for demand

- Government or government-owned companies have difficulty making necessary investments
- Solution: Stop prohibiting / encourage private investment in supply
  - Secondary problem 1: Because infrastructure investments take time to yield returns and are anchored in place, they are vulnerable to administrative expropriation by government
  - Secondary problem 2: If one of the suppliers is government-owned, will others be treated fairly? “Level playing field”

# Expropriation

- In the 1960s, governments expropriated directly
  - Bad outcomes
  - Investment guarantees
- Administrative expropriation is the nibbling away of profits and even capital by
  - Imposing unanticipated or retrospective taxes and levies
  - Asking for donations in ways difficult to refuse
  - Not giving promised price increases built into business plans
  - Compelling transactions with uneconomical suppliers, etc.

# Level playing field

- No level playing field if, e.g.,
  - Private suppliers get spectrum on less favorable terms than government-owned supplier
  - Government only purchases from its supplier
  - Government supplier gets privileged access to universal-service funds
- Perception matters, even if reality is different, e.g.,
  - If employees of NRA and government supplier move back and forth

# Solution: Independent regulatory agency

- Minimal definition from GATS Fourth Protocol
  - “The regulatory body is separate from, and not accountable to, any supplier of basic telecommunications services. The decisions of and the procedures used by regulators shall be impartial with respect to all market participants.”
- Value in making GATS commitments
- And going beyond the minimal

# **REGULATORY APPROACHES**

# Regulatory approaches

- Command and control
- Structural regulation
- Conduct (or behavioral) regulation
- Technical (or safety) regulation

# Core problem of regulation

- Principal agent problem
  - In non-regulated industries
    - E.g., early electricity or early transport industries
  - Within government
    - After nationalization
  - In regulated industries
    - Government/private suppliers regulated by an independent agency

# Principal-agent problem

- How to get the employee or contractor (agent) to act in the best interests of the principal when the employee or contractor has **an informational advantage over the principal** and has **interests different from those of the principal**

# P-A problem in regulated industries

- Pure case
  - Government as regulator (Principal)
  - Private firms/operators (Agents); no government operators
- Actual case in most countries
  - Independent (?) regulator within government (P)
  - Private firms and fully/partially government owned firms (As)
- Peculiar forms
  - Independent (?) regulator within government (P)
  - Fully government owned firms (As)
    - Given tradition of massive intra-government litigation, may make sense in India
    - But elsewhere?

# Command & control regulation?

- Can the C&C approach used within government be applied to private actors?
  - Legislation, regulations, licenses constrain actions
  - C&C is likely to add a superfluous layer of management
- Intrusive actions may work with regard to information
- But giving orders will completely negate benefits of private ownership/management

# Structural regulation

- What type and how many organizations can engage in which activities
  - Entry regulation
  - Concessions and licenses
- Enforcing functional separation such as vertical and horizontal disintegration
  - E.g., New Zealand and UK solution of different companies for backhaul and access
- Merger control
  - Market share of incumbent firms

# Problems with structural regulation

- The boundaries/interfaces shift in dynamic markets such as telecom
- Policing the interface may require sophisticated regulatory interventions
- Most importantly, prior commitments in licenses may preclude compulsory disintegration

# Conduct (or behavioral) regulation

- Permitting (or not permitting) behavior of organizations
  - Product price regulation
  - Access price regulation
  - Regulation of non-price behavior (anticompetitive behavior)
  - Regulation of service and product quality and
  - Environmental regulation

# Technical/safety regulation

- Standard setting and monitoring
  - A form of conduct regulation
- Technical/safety regulation can affect market entry (structural) and competition (conduct)

# Problems with conduct regulation

- Is highly resource and information intensive
- Requires significant expertise within regulatory agency
- Thin line between conduct regulation and command-and-control

# What is actually practiced: Hybrid

- Some elements of structural regulation to ease work load and friction
  - Some times regulator and operators can agree on vertical disintegration, e.g., BT Openreach
- Significant amount of conduct regulation
  - Tempered by regulatory forbearance, complete (India) or within a band (Bangladesh)
- Small component of C&C
  - Information reporting requirements
  - Security/emergency related