

# Proceedings of the SAFIR workshop on regulatory strategy

# Proceedings of the SAFIR workshop on regulatory strategy

(held on 12 and 13 September 2000 in  
Dhaka, Bangladesh)

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## Foreword

Technological change and regulatory innovation have extended the preference for competition in production and delivery of infrastructure services to new corners of the world. This has modified the traditional belief that only monopolies can be allowed to handle such services. The need for privatizing and liberalizing the infrastructure sector was felt in only a few countries in the 1970s and 1980s. In the 1990s, more countries began to feel such needs as permitting the market to have its say increasingly manifested its benefits.

In South Asian countries, the private sectors' participation in infrastructure sector has so far been minimal. Of late, competition has made a hesitant entry in some areas of the sector still dominated by monopolistic elements. The government will however remain a player for quite sometime to come. To secure a level playing field, alternative regulatory frameworks have been introduced in some areas of the sector. Since independent regulation is new to South Asia, the challenges for managing the transition from controlled monopolies to an environment of competition would be many and would require sustained organized efforts at learning lessons of independent regulation and allied matters for the benefit of all stakeholders.

The region has nearly twenty independent regulatory bodies already in place. Prices for infrastructure services have long been regulated in the region. However, economic regulation by independent bodies separated from government departments and operating on principles of transparency and cost reflective pricing is a fairly new concept in South Asia. In embarking on these policies, this region is following a path traversed by many countries in Europe, Latin America, and East Asia over the last two decades.

In response to needs identified by regulators from the region, and following recognition of the challenges that need to be addressed head-on for the path to be cleared for new and more efficient agencies, SAFIR (South Asia Forum for Infrastructure Regulation) was established in May, 1999 with support from the World Bank and PPIAF (Public-Private Infrastructure Advisory facility). Functioning

under the umbrella of the IFUR (International Forum for Utility Regulation), the SAFIR initiative is guided by a Steering Committee of experienced regulators from the region. It seeks to build regulatory decision-making and response capacity in South Asia, assists in gaining acceptance for regulatory authority and approaches from stakeholders, develops sustainable training programme to serve regulatory agencies in the long term, spurs research in regulatory economics, and provides a databank of information relating to regulatory reform processes and experiences. Covering Bangladesh, Bhutan, India, the Maldives, Nepal, Pakistan, and Sri Lanka, SAFIR is designed to assist in the building of regulatory capacity in the electricity, natural gas, telecommunications, water, and transport sectors.

In this context, SAFIR organized a workshop on Regulatory Strategy in Dhaka in September 2000. The publication of the workshop proceedings is expected to assist capacity building, apart from providing insider's perspective on issues.

We hope and expect that the book will be useful to regulators, policy makers, and others including regulated entities in the region in carrying forward the agenda of regulatory reforms for improving consumer welfare and enhancing the efficiency of sectors critical to country's development.

I hope the book will meet its expectations.



(M S Verma)

Chairman of the SAFIR Steering Committee and  
Chairman, Telecom Regulatory Authority of India

## **Preface**

The infrastructure sectors in South Asia are going through a period of rapid change, particularly in respect of redefinition of responsibilities and the emergence of independent regulatory structures. Given the far-reaching consequences of changes currently in hand, it is important that the countries of the region learn from each other individually and from the experience of the outside world collectively. Such an approach would ensure that movement up the learning curve of new regulatory organizations and those organizations that are being regulated takes place rapidly. It would also ensure that changes taking place in the countries of South Asia fully include and reflect the special characteristics of the common situation prevailing in the countries of the region.

This volume which represents the proceedings of the workshop that took place in Dhaka in September 2000 is a compilation of knowledge and experience developed in the region to benefit all the stakeholders associated with regulatory changes taking place in the SAARC region. The approach outlined and elaborated on in these pages deals with several sectors ranging from electric power to telecommunications, and derives lessons from experiences in South Asia as well as in other parts of the world. The importance of proper regulatory practices is particularly important in poor societies, as exist in most of the countries of South Asia, because good regulatory practice must lead to efficient use of all the resources employed in the production and distribution of services and ensuring that the consumer gets the best possible deal. There are also technology-related issues, which make independent regulation a complex and highly specialized business. This is particularly true of the telecommunications industry. Some of these facets of regulation have been covered specifically in the context of South Asia in these proceedings.

This volume, it is hoped, would be a valuable addition to the growing literature that is developing in this part of the world on a

subject that would have major relevance for the growth and development of infrastructure in the region and, therefore, for the economic development of South Asia.



(R K Pachauri)  
Director-General  
TERI



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SAFIR (South Asia Forum for Infrastructure Regulation) gratefully acknowledges the help, support, and guidance that it received from various sources in publishing this book. Special thanks are due to all the authors who have contributed to this publication. Special mention must be made of the indispensable guidance and support provided by Mr Clive Harris, Senior Economist, the World Bank, New Delhi; Mr M S Verma, Chairman, Telecom Regulatory Authority of India; and Dr Leena Srivastava, Director, Regulatory and Governance Division, TERI. SAFIR also acknowledges the support received from PPIAF (Public-Private Infrastructure Advisory Facility), a multi-donor technical assistance facility aimed at helping developing countries improve the quality of their infrastructure through private sector development (for details see the web site at [www.ppiaf.org](http://www.ppiaf.org)), in publication of this book.

Mention must also be made of colleagues at TERI: Ms J Ram Mohan and Mr Kaushik Das Gupta for editorial assistance; Mr R Ajith Kumar for typesetting; Mr R K Joshi for cover design; Ms K Radhika for secretarial assistance; Mr P K Jayanthan for indexing the book; and Mr T Radhakrishnan for supervising the production of the book.

## Welcome speech

*A F K Golam Mowla\**

Representatives of the World Bank from the New Delhi and Dhaka offices, representatives of the Asian Development Bank, representatives from USAID (United States Agency for International Development), Dhaka, members of TERI, distinguished speakers from different countries, distinguished delegates from different regulatory agencies of the South Asian countries, distinguished delegates from different utilities, ladies and gentlemen.

On behalf of SAFIR (South Asia Forum for Infrastructure Regulation), I have the privilege to welcome you all in this workshop on Regulatory Strategy organized by SAFIR with the help of World Bank, New Delhi, and TERI.

During this two-day workshop, discussions will be held on many regulatory issues. I hope these will be immensely beneficial for all of us engaged in regulatory activities or in providing different types of services like electricity, telecommunication, water supply, gas supply, ports and shipping, road transport, etc.

Regulatory issues are increasingly becoming important for all of us in this region because of introduction of reforms and restructuring in different utilities and introduction of competition by allowing private operators to work side by side with the government-owned utilities with the objective of providing quality services in economic and efficient manner to the consumers while also making the utilities commercially viable.

Earlier the government was the service provider and at the same time was also the regulator but now with the private operators joining the business it has become necessary to create separate regulatory authorities that will ensure a level playing field for all the operators engaged in the business.

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Government of the People's Republic of Bangladesh*

Regulation is a new field for all of us, and SAFIR is a new association of the existing regulators and would-be regulators of the different services in the South Asian countries, created with the objective of capacity building of the regulatory authorities in this region through training, seminars, workshops, etc. and for building up a database related to the subject. The main initiative in this regard was taken by the World Bank in early 1999 and Mr Clive Harris of the World Bank's New Delhi office played an active role in encouraging the different regulators and would-be regulators in the region to form such an association. A steering committee was formed consisting of representatives of the existing regulators and would-be regulators of the region to prepare the policy guidelines for SAFIR, and the first meeting of steering committee was held in New Delhi in May 1999. Substantial progress has since been made by SAFIR for realizing these objectives, and TERI has been engaged as professional and administrative partner of SAFIR. The USAID has subsequently joined in providing necessary assistance in this field under the umbrella of SARI (South Asia Regional Initiative).

As a first venture, a two-week training programme on regulatory issues was organized in Agra, in April 2000 by SAFIR along with World Bank and TERI. A big avenue for learning and cooperation on regulatory issues among the countries of the region has been opened up with the formation of SAFIR.

I hope this workshop will provide an opportunity for intensive discussions and interaction on the various issues involved and that the workshop will be a success. I would like to thank the steering committee of SAFIR, the World Bank's New Delhi office, and TERI for convening this workshop in Dhaka. I hope from now on such workshops would be held at regular intervals in other countries of the region so that we can learn and benefit from them.

Thank you.

## Session 1 Establishing regulatory legitimacy

*Rohan Samarajiva\**

In this workshop we intend to try to learn from each other's experiences in the strategic aspects of regulatory policy in the South Asian region. I do not want to suggest that we have not made any mistakes. But, there are some wonderful lessons that can be discussed. I am sure in Sri Lanka at the time when I was the Director General of the Commission we made mistakes. I still think about the lessons of that period: what was done and what could have been done better. We must use each other's experiences to frame questions for ourselves and then arrive at the answers for ourselves, examining whether any of these principles are applicable in our environments. We all are involved in the day-to-day practice of regulation and what we want from this workshop are the practical solutions to the problems that we all face.

There is the issue of public acceptance of our rulings. We have some indications of this through letters to the editors of newspapers, various kinds of media manifestations of public opinion, etc. Generally speaking, regulators are not very popular, though there have been a few instances where they have attained popularity. The subject that I will be discussing today, rate rebalancing, is one that makes us very unpopular. Certain kinds of tariffs, of extreme importance to the common man, have to be raised while others are lowered. In a populist framework, this is considered to be almost hostile to the public.

Gaining acceptance for regulation within government in our region is quite a serious problem. What are the causes of this? Recognizing that there are some significant variations from the Westminster model in this region, I would still argue that we have the core principles of the Westminster system where the Parliament is sovereign and the independent regulatory agency is

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\* *Former Director General, Telecommunications Regulatory Commission, Sri Lanka*

outside its control. This creates anomalies. The ombudsman mechanism, which was introduced in Sri Lanka in the 1970s or early 1980s, has some similarities to the conception of the independent regulator. Still, it is not a perfect correspondence.

There is moreover a conflict between the roles of the minister and the regulator. While the regulator implements the policies, it is the minister who has to answer questions about them in Parliament. He justifiably feels aggrieved for he has had no say in the making of the decision. There is also the question of classification. Is the role of the regulator judicial? Regulators exercise some form of judicial power. However, they are not subject to the general framework of the judicial system. Then there is the question of accountability. However, as we know from everyday practice, accountability can be taken to absurd lengths. So there are no clear answers and solutions. And the operators who are either present, what we call the incumbents, or the ones who are coming in, have a lot more to say. And in the early period, it is in their interest to weaken the regulatory agency, which essentially affects the rules of the game for years to come. So the pressure is most intense when you are building up your organization and hiring staff and developing competency.

There is also whole business of trying to distinguish regulation from the judicial and administrative styles of working. When you are a decision-maker, you listen to people and take the decision. And they would tell me to do that. And I would say, oh no, this is regulatory commission. I have to go through some proceedings and then I have to take it to the commission. And we have five people in the commission. We have to have appropriate documentation and we have to give notice to the stakeholders. This tends to be seen as almost obstructionist by people who are used to the administrative mindset inside government.

Unlike a judicial body, a commission is required to balance the interests of various stakeholders. It does not simply apply laws to facts. There can be complaints that the commission ignored the interests of one group or the other. So you get hit from both sides. You are not judicial enough on one side and you are not administrative enough from the other side.

There is low trust in our countries, with concern about corruption. When, as a regulatory agency, we engage in actions that result in major changes in wealth distribution, accusations that we may not have been fair in the exercise of discretion surface.

This can also be used very tactically to prevent regulatory organizations from functioning properly.

What we have to understand is that we have to learn to live with these problems. For example, in the US, where there has been regulation at the state level for over 100 years, and at the Federal level for over 50 years, there are continuous appeals. And the British experience is somewhat helpful. I am not talking of all the British commissions of gas, telecom, and so on. But because I have studied telecommunications and am most familiar with it, I will talk about it. It is almost a textbook shift from charismatic to bureaucratic. Under the First Director General, not too many reasons were given and great reliance was placed on his ability to explain, persuade, and justify. Under the second Director General more process-oriented open procedures were adopted.

Through our activities we can try to convert crises into opportunities of gaining legitimacy. There are basically the four sources of legitimacy that we can draw on. I will talk about the importance of communication of these claims later. If these claims don't get communicated to the stakeholders and to the public, then, we are simply talking to ourselves.

I will go through all relevant issues and then discuss them in relation to the difficult problem of rate rebalancing. The statute vesting us with authority is the necessary condition of our existence. There is an element of delegated power in the parliamentary system, which is however not a very good basis for actually conducting business. I think the whole concept of independent regulation goes beyond this. So we cannot rely on delegated power alone to claim legitimacy.

The main claim in the literature and in the general conversation on the issue of regulation is that we must truly have expertise. I think this is where organizations like SAFIR become extremely important, because if we are doing regulation and we do not have the competence, there is no rationale for our existence. So I think it is extremely important particularly in infrastructure sectors that knowledgeable people are running affairs, that the economic and costing principles adopted by us are sound. This however is not adequate by itself.

I cannot think of a single instance where you can have a perfectly objective formula that can be applied to a regulatory problem that will be acceptable to all the stakeholders. However, we must reinforce our expertise and build upon it. One of the things

that we worked on in Sri Lanka was training. There must be continual updating of our knowledge, but even more important is that we must communicate our achievements in this respect. Whenever we had training programmes in Colombo or an expert who had come to do some consultancy for us was making a presentation, we tried to invite people from the operators and some relevant government organizations. One benefit is that this exposure increases the level of competence in the entire sector. For example, your operators get acquainted with how to file a properly documented tariff request. The other, less obvious, benefit is that when your staff responds to some questions from the consultants or from the expert trainers it is an effective mechanism to communicate the development of staff expertise.

Openness, I would emphasize, is one of the most important things that we have to achieve. Along with expertise, what we have to do is to demonstrate that we are looking at different viewpoints and different forms of expertise. In fact, expertise is not a guarantee of unanimity when there are different kind of experts. A workshop with experts of divergent views is useful for a more balanced portrayal of ideas even at the stage of framing the issues. Openness allows us a cost-efficient way of testing the quality of information that is put before us. One of the most difficult things we have to do as regulators is to get information from experts. The other problem is that when you do get information, you are not quite sure of its accuracy. One of the ways of getting some assurance of the quality of the information is to let the other side look at it, and criticize it. In the process the data that is not disputed can be ferreted out. So that is one of the values of the principle of openness.

Document the whole process if you want to show that you have allowed people opportunity to comment. Organize the material and make it retrievable, so that at a later time, two years down the road, when somebody questions the outcome of the proceedings, you can go back and say, 'Look, you are now questioning us, but you had been given an opportunity to comment on these things earlier; we gave you enough time and enough information, but you did not comment.' Or, in fact, 'You agreed with us at an earlier time. So do not speak now.' It's a part of credibility in the sense that you can actually get something implemented without being appealed. And, of course, openness is the best disinfectant against corruption.

I think it is equally important to understand the public interest and distinguish it from the consumer interest. One can define the interest of the consumer simply in terms of lower prices, higher quality of service, and more choices. In some cases, it is in the public interest to increase prices, to create the conditions for network expansion and adequate levels of investment. We have to, in many cases, balance the consumer interests with incentives for further investments. Sometime the short-term interest of the consumer of today has to be sacrificed for the consumers of tomorrow. Public interest is, therefore, a much larger concept than simply the interest of the consumer in lower prices. This is also a balancing factor to the principle of openness. While openness is a very good principle, and is needed to balance some of the problems of the expertise, it can have the unintended results of essentially making regulation a little clubby exercise, where a small number of parties interact with each other regularly. This is called regulatory capture. I think the public-interest focus is important to safeguard or to pull away from this tendency. On the other hand, if you go too far towards the consumer interest side you will be trapped in a phenomenon known as consumer capture. The balancing of these two interests is critical. So you should always be scrutinizing your decisions and also converting them into public-interest language so that the public realizes your actions are in its interests. I can remember at the news conferences that we held I used to get irritated at journalists always asking me about what each technical decision means for the general public. It is actually a profound question to which we must always give thought to. If you are a regulator, it is very important for you to explain yourself to people and remain open to criticism.

Let me now talk about tariff rebalancing. I know from various colleagues in the Indian state commissions that they have very serious problems of rate rebalancing in the electricity sector, where there are flat-rates or subsidized electricity rates for farmers and other groups are being charged higher prices to pay for that. The challenge in Sri Lanka was similar to this, but not as serious. In the beginning of the rebalancing process, one-third of the users of the main telephone company were paying less than \$5 total in rental and call charges, while most of the money was coming from the international segment of the market. This was a serious problem.



We did not have the ability at the regulatory commission to decide on the formula for rebalancing. We were committed to implementing a legal agreement that had been signed between the government and the investor, the NTT (Nippon Telegraph and Telephone) Corporation of Japan. It basically gave us a formula that said how inflation should be accounted for, what tariff elements were included and what were not, and yearly revenue requirements. Our job was to devise a tariff decision within this framework. We were requested to increase domestic revenue by 25% in the first year. When you increase revenue by 25% you may have to increase a particular tariff by even more. We even increased the monthly subscription (the rental) by 80% in the first year. As you can imagine, a lot of complaints appeared in the newspapers.

People have high expectations of the reform process. They also felt that they had been getting very bad services and also paying a lot for it. I think most people in Sri Lanka believed they were overcharged for telephone service anyway because they have got very little billing information, just a meter reading, and do not know what the calls they are being charged for. When the immediate result of the reforms is that telephone bills go up, this naturally disappoints people. The regulator has to deal with the reality of expectations on one side and the outcome of the rebalancing on the other side. In Sri Lanka, we had a particular problem. Just months before I came on the scene in December 1997 the household cooking gas industry sector was privatized with no regulatory mechanism at all. There were several increases amounting to may be 20% within the first few months and as a result there was a big negative impression of privatization and its effects.

We had the tariff request, a very simple document that the company had given us, saying that they want to basically increase the charges to all the low users. They wanted to increase some charges excessively, and they expected to get a lot of money. They wanted to get even more than the guaranteed 25% increase in the first year, as government had said at least 25% for the first year. I officially started in my job on 1 January. Since I wanted to communicate something new, I worked over Christmas and got 19 interrogatory questions prepared. It is nicer to say information requests than interrogatories, which is a legal term. And I had it delivered on 1 January to the company. Symbolically, I wanted to convey that something new was happening. It took them 19 days

to answer these 19 questions. After getting answers, we asked for more clarifications. They gave additional information. We said we wanted to see the basis of their calculations, that we wanted to see the algorithm. And I got my young staff to work on this. So they understood that we would be going deep into the structure of the tariff proposal. We tried to simplify the highly complex tariff structure and provided a basic rate design on which future changes could be built. Earlier we had an arbitrary type of formula. We released the decision in the first news conference that had been held by the commission and by its predecessor – the Office of the Director General of Telecom. We provided a detailed news release with a colourful get-up, since we wanted to project the sophisticated activity that was behind this tariff decision. After a day or two I went to talk on radio live: just taking questions without screening and answering any question anybody had on this subject. As you know an 80% increase in rentals affects everybody. This was a nasty decision. But I think we survived it well; we actually got only one slightly negative editorial.

Before the decision was announced at the news conference, I briefed the incumbent operator against the advice of my staff. My thinking was that they should not be caught off-guard by the first real major regulatory decision issued by the commission on my watch. I found that my staff was right; the incumbent rushed to the minister and exerted a tremendous amount of pressure. I told the minister, 'Sir, you have been consulted on this decision. The draft decision had to be shown to you, and we have shown it to you. You made some suggestions. We accommodated all these suggestions. The point where you could intervene is now over.' I continued, 'Your life is going to be very difficult, because every time we do something, everybody in the country will be calling on you. Do you really want to look at all these decisions? Don't you prefer to say it is an unpleasant decision that has been taken by regulator, why don't you go to talk to him? It is not me but the commission that took the decision.' He agreed. All he did was to ask the senior people at the incumbent to talk to me. I listened to them and explained what we were trying to do. There were leaks to the newspapers and so on, but everything died down after the news conference was held.

When we were working on the tariff, we knew in our hearts that we were doing something that was going to create a lot of pain for some people. So we kept pondering over how to

moderate the tariff increase and I came up with the idea of low-use tariffs, a tariff which reduced the burden for people who do not use the telephone frequently. As a result, the elderly, the pensioners, and other such people had some way of actually containing the effect of this increase by changing their behaviour. I was happy to see later that the same approach had been adopted in the UK.

We tried to link the tariff increase to service-quality improvements. For example, we said that we are giving you 80% rental increase but if a fault is not repaired within seven days, the customer had to get the money back for the time without service. So there were certain service quality improvement directly built into the tariff.

We had provisions in our Act dealing with individual complaints. Although these powers had been in existence since 1991, they had never been exercised. Shortly after the main tariff decision was announced, we also announced the first decision on an individual customer complaint—a complaint about a fault that had not been repaired for 48 days. It was an insignificant decision, but it got a lot of publicity – second story in the national television news – because for the first time the regulator was ordering the incumbent to refund the rental for the time period the fault was not repaired.

The other issues I highlight for your attention are as follows. We had many dealings with the finance ministry and the telecom ministry. There is a perennial tension between these two ministries, between any line ministry and the finance ministry, because they have different interests in relation to privatization. Finance wants to optimize the value of privatization and protect the interest of those particular investors, while the line ministry wants to ensure the success of the sector as a whole. Regulators have to be very careful in managing these relationships. In Sri Lanka, competition and consumer authorities are quite weak and the process of introducing new legislation to strengthen them is going on. But we kept good relations with them too. We spent a lot of time working with the top officials in different parts of government including the President's Office. People always appeal to the Prime Minister, to the President, and to different power centres to overturn the decision of the regulators, which is something we are all familiar with. To prevent that from happening, we have to

build good relationships and keep them informed. In fact, try to educate them as to what you are doing and why you are doing it.

In Sri Lanka, the legislature was not very active, at least when I was there. And I can honestly admit to the fact that I didn't spend a lot of time in educating the legislative committees on what we were doing. Though I would say that it is something that needs to be paid attention to.

We also had to try to educate the judiciary. And we did that, very carefully following protocol. We talked to the Chief Justice and with the judicial institute. We invited one of our consultants, the former Deputy Director General of Telecommunications in the UK, Mr Wigglesworth, to make some presentations to the judges. We had a separate session for the Court of Appeals and for the Supreme Court and a separate session for high court and district court judges. This had to be done extremely carefully because one should not be seen as trying to influence the judiciary. Even the invitations to these events were sent out by the Judicial Institute, and not by us.

In building up the legitimacy of the regulatory agency, some media involvement is essential. You should be aware of, keep track of, and be prepared for the issues that are going to hit you. We have to monitor the media, have a systematic clipping service in the organization where you have people marking out the stories of relevance to the regulatory process in various newspapers, photo copying them, and sending them to senior officers so that you see not only the individual stories but also the pattern of their development. The first point is about finding what the potential issues are and the things that we ought to be paying attention to. The second issue is about communicating, about telling our story. One of the important issues that we had during my tenure was a major consumer issue. This turned out to be an actual violation of licence condition by the incumbent operator, who was collecting large amounts of money, more than \$200 per subscriber, but giving connections only after several months. It was also a case where the connection fee was not refundable. So by taking the money before they were ready to give connections, they were also preventing the customers from going to their competitors. So there are all these kinds of complex issues involved. Sometimes you have to frame the issues in certain ways through the media to try to get people to think about them. In this case, I framed the

problem as one of interest-free loans from the people of the country to the incumbent phone company in an early interview on television. It was very effective.

Within the government, my policy was always to try not to surprise powerful colleagues and powerful organizations; to the extent possible, try to give indications as to where we are going, for example to the finance ministry. I talked about the question of educating all the relevant parties, not just those in the regulated sector but also other members of the government and the judiciary. The question of stakeholders appealing to say the President's Office or the Prime Minister's Office is an important issue. If you can educate the people in those offices about what you are doing and the procedures that you are following, and so on, there is a tendency for them to at least to call you before they take a position. Once they take a public position, then it is a question of prestige and they cannot back down and neither can you, and there might be unpleasant conflicts. Doing all this will not guarantee against conflicts, but at least one should attempt to do that.

To demonstrate the value of building public support, I will talk about the public hearing we conducted. We had provisions for public hearings since 1991 but the first public hearing was held only in 1998. So for seven years, this was a dead letter. But even after additional resources were given to the commission, we had only two public hearings. The discretion as to whether to hold public hearings or not was left to the commission. A public hearing is a good mechanism in demonstrating support for a position. We had a situation where we had no itemized billing and lots of difficult-to-resolve billing complaints. These are again connected issues. When you are doing tariff rebalancing, you are increasing people's tariffs. Obviously they are going to want to get a lot more for what they are paying. Many consumers in Sri Lanka had a firm belief that they are paying not only for their calls but also for calls taken by telephone company employees that were fraudulently billed to them. There was a lot of distrust, and billing disputes were frequent and difficult to resolve. So we had to bring this issue out into the open and demonstrate that there is indeed a ground for the changes the commission wants, which actually cost the telephone company money and caused various difficulties for them. There was a division within the phone company on the question of itemized billing—some were willing to give it, but others strongly opposed it. So we conducted a

public hearing where we received close to 400 written submissions within two weeks. Of these we asked 40 people to make oral representations and some of them broke down because of all the harassment they had suffered in the course of trying to resolve their billing disputes. The effect of the hearing was that even before an order was given, the company voluntarily said that they would introduce itemized billing. The only issues remaining were the terms and conditions of itemized billing.

I would like to briefly take up the question of appeals. We are not trying to deal with appeals at a theoretical level, but also have gone through the experience of dealing with an appeal. I wrote a 50- or 60-page affidavit, in the course of dealing with this appeal. So let me say few things about this.

First, appeals are necessary. It is a discipline that we need, because we are exercising discretion. We need our decisions to be upheld. There are many people who told me that we do not need any appeals. I never agreed with that position. In the US, the appeal process has been abused. There it is used almost in a gaming sense. If the status quo benefits you, just continually use the legal system to block any change. This has been studied in the US and in Britain. The process of the appeal and the way the whole system can be damaged particularly when you are introducing competition are instructive. If the incumbent appeals, change is slowed down and new entrants are harmed. So there should be appeals, but it is necessary to prevent negative outcomes. I had discussions with respected and learned justices of our Supreme Court about the possibility of having a specialized court designated to deal with regulatory appeals on the grounds that specialized matter is involved. But Justice Amarasinghe of the Supreme Court disagreed with my idea. He believed that the judicial system should not replicate what we are doing. His view was that the regulatory agency should be responsible for the substantive matters that required expertise. The courts would only look at the procedural aspect; whether the principles of natural justice had been violated. In Justice Amarasinghe's view, this was something any court could do. If you created a specialized court, you would be practically inviting it to go into the substantive aspects, which would result in a duplication of effort. So there is a bit of disagreement on the way in which appeals should be handled. I am saying this because I now have a different view on this point, particularly after very long conversations with

Justice Amarasinghe. I have now come to this position and I can support it with my experience.

I believe we must look at two things in our actions. One is to apply our expertise and do the substantive work we are supposed to do. Then we must always keep in mind the procedural correctness of what we are doing. We must also keep a docket, keep records of all the procedures, and maintain the documentation properly because if and when there is an appeal you must be able to demonstrate to the court that you have followed the principles of natural justice and that you have been fair. You have given people an opportunity to participate and you have done all that could have been done to make it an open, transparent, and fair process. There could be some places where you have, for example, used a particular methodology that, according to your professional judgement, is the most appropriate. The tactic is to prevent the judges from going into the methodology itself. This requires you to say how you arrived at this methodology, which other countries are using it, what kind of claims you can make that this is a legitimate methodology, and try to stop the questioning at that. In a Sri Lankan court, if the sitting justices deem our selection of a particular method arbitrary, then it becomes amenable to judicial remedy. That is the problem we have to keep in mind.

Another problem with specialized appellate tribunals is whether that precludes the general writ jurisdiction being exercised. If not, there is a possibility of having a regulatory commission, and then a specialized appellate tribunal and the possibility of parties moving the courts under the general writ jurisdiction. So now you have a two-tier appeal instead of one-tier appeal. It is also possible to have an appeal to the commission for review and then a formal appeal to the prescribed authority. Thus, there are interesting issues involved in the legal appeal procedure.

Conceding that we need appeals, the question is how we can contain it so that it is timely. One critical issue we have to think about in this respect is stay orders. We have to make great efforts to prevent stay orders against regulatory decisions. I cannot give some kind of formula that we can apply uniformly to prevent stay orders on regulatory decisions. The people who benefit from the status quo continually use the appeal process to prevent change. Preventing courts from issuing stay orders against the commission is not possible, since justices are authorized to issue such

orders under writ jurisdiction and they will not give up the judicial right to decide whether the stay order should be given or not. But there can be some guiding language in the statute; and you should have some arguments placed before the justices as to why the stay order should not be granted. So we should be able to speak on the question of irreparable harm, which is the basis for issuing stay orders.

The other, more serious, problem is that of non-legal appeals. When somebody goes to the President's Office or to the Prime Minister's Office or to the Chief Minister's Office, and says the regulatory commission is doing wrong things and they should be overruled, there is no documentation. All that happens is that a phone call comes from some place in government, and some activity happens, which results in the decision being changed. This is in fact the worst kind of appeal because it affects the practice of independent regulation in the worst possible way. So when I look back at the one and half year's time in Sri Lanka, I think one of our biggest achievements was that instead of the earlier practice of all appeals going through back channels, we created a situation when an appeal was submitted to the court of appeals. And that appeal process is still continuing. A stay order was not granted against the order of the commission. And we were worried whether our decision would be suspended. The company was refusing to implement it. But now I am told that the company is fully implementing the decision, which was the interconnection decision issued in November 1998. And even before the company implemented it, the competitors did, in effect implement it by making their payments on the basis of estimation according to the new decision rather than on the basis of the old decisions.

The last point I wanted to make is that when I say 'appeal proofing', I do not mean preventing appeals but increasing the possibility of surviving appeals. And I will end this with one anecdote to illustrate this point. The UK telecom regulator, Oftel, is the model for many of our countries. Oftel had taken a particular decision on interconnection in the 1980s. Interconnection in the telecom sector is the most controversial problem. Oftel decided to give no reasons for its determination. And it has been documented by people who research these subjects that they took this course of action under legal advice. They did it to prevent or reduce the chances of an appeal. In Sri Lanka, the



interconnection decision was the most controversial thing that we did. In 1998 there was a lot of internal discussion both among my staff and among the commissioners as to what we should do. So while my position was of openness and of providing the reasons I was actually persuaded by the claims and the arguments of fellow commissioners and staff about the negative aspects. So the solution that we adopted was a compromise. And I completely accepted the compromise and I am not going to say differently now.

We employed the 'iceberg strategy', which gave a relatively short decision and provided a simple, short reason. We had an enormous amount of paper that was collected to provide all the reasoning and the work that went into the decision. As soon as the appeal came we were able to provide a huge pile of documents. This was very thick and we purposely made it look frightfully big with all the attachments to show how much effort we had put in to find the proper methodology and how we had looked at different views and conducted various proceedings to get different viewpoints. The documents showed how reasonable our procedure was and that we had developed all our reasoning before the decision was issued. It was not that the decision was just issued and when we were appealed we went back to figure out what the reasoning was. We were able to say we had all the reasoning in internal documents, that we will now provide to the court because our determination has been challenged. So I think that kind of compromise solution balances proper decision-making and openness on one side and the specific legal and administrative cultures of a particular country should be adopted.

## Session 2

### Review and appeal of regulators' decisions in the South Asian context

*Kamal Hossain\**

This invitation to be amid so many regulators and those involved with regulation in this region provides a valuable opportunity to compare notes on development of regulatory policy in this region. Sri Lanka is a pioneer of the regulatory process in the telecommunication sector starting from 1991. This was followed by the Pakistan Regulatory Authority Act of 1996, the Indian Telecom Regulatory Authority Act of 1997, and the Nepal Regulatory Act of 1997. The Bangladesh Regulatory Act is in the offing. We have drafted legislation and have had a round table meeting with potential investors and various government agencies involved. A draft law is ready. Those from Bangladesh will find this meeting particularly useful because they will be able to reflect and draw on the lessons to be learnt from all your experiences with regulations.

All of us are involved in this process of economic reforms that entails deregulation and privatization of a number of sectors that were earlier reserved for the public sector and have been progressively opened up to the private sector. This involves a redefinition of the role of the government. Earlier the government was the owner of most utilities; in our case it was the BTTB (Bangladesh Telegraph and Telephone Body) which ran the telecom sector or the Petroleum Corporation or Petrobangla which ran the oil and gas sector. These sectors are in the process of being opened up for investment (domestic and foreign). The critical need for a regulatory agency arises because once you are moving away from state-owned monopolies to a situation where private entities are also entering the field, one must maintain an environment in which the private investors and corporate entities are not placed at a competitive disadvantage vis-à-vis the state-owned services. The whole point of deregulation and privatization is the promotion of

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competition and allowing market forces to operate both for allocation of resources and for providing, in principle, the best services at the least cost. That is the ideal, but there are many intermediate stages between that ideal and what is achieved in the process of transition. There is inherent complexity in the process and the need to understand the regulatory functions of government is something new for all of us. Whether we have the Westminster form or any other form, the point is that the government did not have a framework that could allow a market economy to operate without undue constraints. What is the essential role of the regulator when you are trying to move from a controlled economy in which there is a large public sector in the field of infrastructure to a new situation where there are many competing actors? The aim of establishing regulatory authorities is to protect consumers from abuse by firms with substantial market power, to support investment by protecting the investors from arbitrary action by government, and to promote economic efficiency.

Regulatory reforms permit and encourage market forces to enhance competition with lower cost of entry and expansion and produce a more competitive and efficient industry structure. Among the principal benefits of reforms to consumers and producers are low prices and higher output in the form of higher quality, better service, and new products. The ultimate success of reforms will depend on consumers getting benefits of more competitive markets even while consumer protection is provided for. While there is growing recognition that competition can reduce the need for regulation in the utility industry, in most industries there exist some areas of monopoly where the benefits of regulation potentially outweigh the cost. Regulation of a utility is complicated by three related considerations. First, prices for utility services are fixed on political considerations. Second, investors are aware of the political pressure to keep the prices at the lowest possible levels and of the vulnerability of their large long-term immovable investment. Third, the long-term nature of most infrastructure investment makes creating a credible and sustained commitment to policy/rules difficult for governments. Highly specific rules, if considered sustainable, can provide assurance to investors and lower the costs of capital. In designing regulatory systems, policy makers need to resolve the following challenges: how much discretion should a regulatory system

contain and how should that discretion be managed to reduce misuse and create a healthy environment both for the operators and the consumers.

My topic today is 'appeals' against regulators' decisions. What Dr Samarajiva has brought out is the distinct quality of regulatory function. The normal functions of government with which we are familiar are policy functions, administrative functions, and judicial functions. The policy makers are accountable to Parliament, or whosoever the government is accountable to under the Constitution. This is the system prevailing today in this region, which can broadly be called the parliamentary system. I do not think we should criticize the Westminster system as good or bad. India has worked with a parliamentary system for over 50 years, and the system can justifiably be called the Delhi model, and not the Westminster model. In this system, the administrator is accountable to his ministers and the minister is accountable to Parliament. The judicial function deals with the application of law to facts that are established through evidence. What is a regulatory decision? It is neither a policy decision nor an administrative decision. Under regulatory balancing, different interests have to be balanced, in a manner different from taking policy decisions. While making policy decisions, the ministers are responsible to implement promises made to the electorate. There are 'public interest' concerns in policy making. However, the mental process, which you go through while making policy, is distinct from that when you are carrying out regulatory functions. It has elements of judicial functions because it involves competing balancing interests in a fair manner. The consumers may want something at the lowest price while the producer will certainly want adequate returns on investment. If the producer is out to make quick profits, long-term investments that require a certain rate of return and certain stability will not be assured. It is a part of regulatory function to maintain and nurture an environment in which the stability of conditions is maintained. So the regulatory function is one where you have to make tariff determination or regulate the terms of licensing. It also aims to protect the consumer interests. It therefore aims to protect the legitimate concerns of the consumers and the producers. The legitimate expectations of all the different actors have to be taken into account while setting tariffs. The proposed tariff structure cannot be mechanically arrived at.

Statutorily identified criterion set by the regulator must take note of the relevant factors and give them due consideration while appraising proposed tariff structure.

There are four steps involved in the process of setting up the tariff structure. There are projections about future prices, costs, and market conditions about which judgements have to be made. These judgements have to be made not by any reference to any law but by drawing on the regulator's professional technical expertise and experience. This is the unique dimension of regulatory function. You must bring to it the mind of a judge in your aim to be fair and free from biases. You may have served all your life in the industry but you should be able to divest yourselves of a pro-industry bias. Is that possible? Or if you have been in the government you had a certain kind of attitude and approach. When you are functioning as a regulator can you divest yourself of that attitude? You probably cannot. I am saying this because unless one understands the distinct nature of regulatory decisions, one will not be able to appreciate the necessity of an efficient and effective appeal mechanism. The regulatory function has to balance competing interests, the legitimate concern of the consumers, the producer, investor, and the government in a fair manner while ensuring effective provisions of services to the community. Infrastructure facility has to deal with the essential services that are recognized by the community and are traditionally called public utilities. These are expectations whether it is in the telecom, power, or water sector.

So there is continuing government concern to see that the legitimate expectations of the consumers are taken into account. Regulators must have the sensitivity to comprehend legitimate expectations, and they should set the limits on what is legitimate. If someone expects to have telephone calls at absurdly low prices or if the government suddenly promises in the election that it will make telephone calls available at 2 paise per call, all regulators will say that these are not legitimate expectations either by the government or by the consumer. If, according to the regulator's calculations, the investment needed to allow a reasonable return on an investment in an efficient telecom system cannot possibly be provided, this would imply subsidization, which will undermine efficiency.

The issue of cross-subsidization is one with which all the governments are confronted. In the transition through which all

governments and societies are passing, this will be a very sensitive and difficult area since people consider subsidies to be legitimate and are not willing to give them up to meet the claim of other legitimate expectations of greater efficiency, modernization, and improvement of utilities. This is an unenviable task that regulators have to take up. This is why we talk of independent regulators. Insulate them as far as possible from extraneous influences so that they can draw on their expertise and apply statutory criteria with a sense of fairness. Judges work with a sense of justice. Regulators would have to work on a sense of fairness in balancing different competing interests. However, it is not the same exercise as that of a judge. A judge applies law to fact. The regulator has to make his own judgement drawing upon his technical expertise and experience and also upon his judgements on various forecasts and projections. Now it is necessary to provide for an appeal because regulators are human beings and can go wrong in their judgements. Therefore, there will always be decisions that one can question. There will always be decisions that will aggrieve some party. Any of the competing parties may well take the view that the regulator has not come out with the correct decision. Therefore, on grounds of efficiency and rationality and fairness in any system of governance, one should recognize human fallibility or the very human characteristic of any institutional set up. People can also take a view different from that of the regulator. So an appeal is something you might call an inherent aspect of sound governance. No one would like to accept something where some one takes decisions with absolute finality. Now having said that, with regulatory functions you get into a problem, because quick decisions are required if someone puts up an investment proposal. First regulators are expected not to sit on proposals like many of our courts or statutory tribunals. We have administrative tribunals, income tax tribunals, and others that take a long time to take decisions, which the regulatory authorities can ill afford. If an investor puts up some proposals, he cannot wait long for decisions on his proposal. Our judicial organs and administrative tribunals most often give decisions in not less than six months. This is not acceptable for the regulatory determination and it would be much less acceptable for an appeal. In our region, we are still groping with the problem of appeals. I have just taken illustrations from the telecom sector. The Indian Telecom Regulatory Authority Act of 1997 had in fact provided

for appeals against regulatory decisions to the judiciary. Very quickly it was realized that this is unworkable. So the Ordinance of 2000 has introduced a Telecom Dispute Settlement and Appellate Tribunal. Significantly, the tribunal was given the power to adjudicate on a wide range of disputes including those between licensor and licensee, between two or more service providers, and between service providers and a group of consumers. The Ordinance stipulates that the Appellate Tribunal will dispose of appeals as expeditiously as possible, and most certainly within 90 days. The 90-day limit is innovation in the context of the dispute or decision-making procedure in our region.

I would have liked to hear the Indian experience with the Appellate Tribunal. After its introduction in 2000, a few appeals must have been dealt with. Have any of the appeals been decided within 90 days, and, if so, how has this been done? This will encourage us to make a similar provision in our legislation. In Pakistan, the jurisdiction on appeals has been left to the High Court. The only ground on which a regulator's decision can be challenged in the High Court is non-compliance with the Pakistan Regulatory Act of 1996. I am not sure that the High Court would be able to do justice to such appeals. If you challenge the regulator's decision saying that it is not in accordance with the Act, the inclination for the judges is to apply their jurisdiction according to their interpretation of the law. The judges are good and competent people, but an appeal on a regulatory decision is something that is outside the normal area of their experience. The judge is not normally expected to have full appreciation of technical aspects due to a number of reasons. We have in an Income Tax Appellate Tribunal, a judicial member, and an accounting member who is supposed to understand the accounting dimension of a tax problem.

The regulator's function includes economic aspects of tariff determination, which involve understanding cash flow analysis, and other technical matters. These are things our High Court judges are not familiar with. Yet our telecom legislation has proposed a first draft which envisages an appeal to the High Court on questions of law where the determination is obviously made on the basis of no evidence or in breach of natural justice, when the parties affected have not been heard or given an opportunity to present their case. These are the cases on which it provides an appeal to the High Court. At least there should be one appeal, I

think, that is the basic thing we all share in the region. But in Pakistan we see that an alternative is provided for by way of an application for revision to be lodged with the Ministry of Communication. Instead of appeal you can resort to an administrative review or revision. And thus you do get a wider range of choices.

Sri Lanka has a public hearing procedure. Any representation on matters relating to the proposed exercise of regulator's power can call for detailed investigations or determination under section 12 of the Sri Lanka Telecommunication Act. This calls for public hearing. I would like to hear about Sri Lanka's 10 years' experience of public hearing. Openness is an important factor for ensuring fairness. A public hearing process reduces the need for an appeal, since there is an open procedure where the party affected can spell out its problems which can then be taken into consideration while framing the policies. But I still believe in the necessity of an appeal to some forum, and after that for an appeal on a question of law. In Pakistan, the court decides whether the Act has been applied properly or not. The Court of Appeal in Sri Lanka decides on a question of law. In Nepal appeals are made to an appellate body, which is presumed as a specialized body consisting of legal experts, economists and financial experts, and engineering and technical experts. We in Bangladesh are keen for an alternative to an appeal to the High Court. That alternative could be a tribunal, with a clear directive that appeals should be disposed of in 90 days in most cases. The competence of the personnel and the qualifications of the appellate body should be such that they should be able to understand regulatory decisions as distinct from judicial and administrative decisions.

Therefore there should be persons with a degree of independent functioning as regulators and as members of the appellate body. If these functionaries are not independent and can be easily removed by government then there would be an inevitable tendency for the government to influence their decision. The emoluments of the regulators should be such that there will be less temptation or vulnerability of being influenced by either government or other powerful influential quarters. Independent regulators must function effectively and efficiently. The same would be true for an independent appellate body. They should be protected from arbitrary removal from office and they should be given emoluments to keep them above temptations and also to secure the necessary level of expertise. I think that the level of expertise



for our regulators should be higher than that in any other department of the government.

The scope for review must be very limited. At least three of the countries in this region have provided for judicial review to correct acts which are held to be ultra vires, to determine gross errors of law or breaches of a statutory mandate or natural justice, or a constitutionally protected fundamental right. This is what we call 'writ' jurisdiction. In Pakistan, India, and Bangladesh, and, to an extent, in both Sri Lanka and Nepal, we do have judicial review. So even if there is no appeal procedure provided, it would always be subject to judicial review. The difficulties faced by regulators once their decisions are subject to judicial review is of delay and lack of appreciation by judges of technical matters. If there is an adequate appeal provided, judicial review may only be sought or entertained in rare cases. This is another strong argument in favour of a sound appellate mechanism.

## Session 3

### Managing the introduction of competition

*MHAu\**

I noticed that I am the only regulator coming from outside the SAARC (South Asian Association for Regional Cooperation) region. I hope what I am going to present to you this afternoon would be of some use and interest to you.

I think one major difference between Hong Kong and the other countries represented here is that Hong Kong is not a country. Since 1997 Hong Kong became a part of the People's Republic of China and has got the status of a special administrative region of China, implying that policies in Hong Kong are separate from those in the rest of China. So in the telecom sector in Hong Kong, we actually have different legislation and different policies from the rest of mainland China. The telecom laws of China do not apply to Hong Kong. There is a high degree of autonomy in formulating the law and policies within the area of autonomy in the special administrative region of Hong Kong.

Secondly, there is difference in size between Hong Kong and your countries. We have a population of 7 million. In spite of differences between my territory and your countries, we would have similar problems on the issue of regulation. We too have been grappling with many of the issues that were discussed this morning. In the earlier part of this year, we amended our telecommunication law. The telecommunication market in Hong Kong is very competitive with a large number of operators. The operators are complaining about too many players in the market. We did start with a monopoly. For example, in our local fixed telecom service and in the international communication we had a monopoly. There had been a transition from monopoly to a competitive market. In some sections of our market, we haven't seen full competition. In some cases, there are locally fixed markets, but still there are incumbent operators who control more than 90% of the market. That is why there is a need for a regulator.

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We have a fully privatized industry. The government does not operate in the telecom sector. Perhaps this is a legacy of history. The Far Eastern Telecommunication Company brought in telegraph cable in the country. We do have some utilities operated by the government. Postal service, water supply, and electricity are operated by the private sector. The government does not operate the telecom service although it has to provide and maintain an environment conducive to attracting investment for the development and operation of the telecom infrastructure. Hong Kong provides a level playing field to the investors so that they can come in to operate infrastructure and expect returns commensurate with the risks of their investment. The Office of the Telecom Regulatory Authority is a government department. Like the FCC (Federal Communication Commission) or Oftel (Office of Telecommunication), it is not appointed by or accountable to the legislature, but it is a part of the civil service. Its independence is created and maintained by law. The Telecom Ordinances enacted by the legislative council in Hong Kong have vested certain discretionary powers for making regulations with the Telecom Authority. The independence of the regulatory authority is enshrined by the law, giving power to the regulatory decision. In Hong Kong, there is no restriction on foreign ownership in the telecom industry. So a foreign telecom operator – even the operator of basic infrastructure – could own 100% share of a company. Our policies are pro-competition and pro-consumers, and one of the heartening fact is that although the regulator is mandated to protect the competition in the market, he is not to protect the competitors in the market. So the policy in Hong Kong is to further the interest of the consumers because it can be argued that the interest of players and interest of the consumers are linked, because if players are not willing to invest in the market and develop infrastructure, then the interest of the consumers cannot be safeguarded. The policy is to have the right kind of regulation, that is, regulation should be used as a surrogate for competition only. We rely on market forces to the maximum to determine the number of players, prices, technology, and quality standards. It is only when the market has not developed that we will have to use regulations to protect the interests of the consumers. In Hong Kong, we regulate tariffs of monopoly operators or the dominant operators because the customers do not have sufficient choices in the market, but we never regulate prices for

the mobile phone services. In the early 1980s, when mobile phones were introduced, they were not considered to be essential items. So there was no reason for the government to regulate the prices. Now in 1990s when the market has fully developed and there is sufficient competition, there is no reason at all to regulate the mobile phone service. In fact the market forces will bring the prices down, and therefore we never regulated the prices for mobile phone.

The regulatory framework in Hong Kong is based on the law of the Telecommunication Ordinance. This is very important because what can be done and what cannot be done is provided for by this legislation. Of course the law cannot be too specific on certain things and the regulator has to spell out norms, which are then published. They are also on the web site. This is one way to achieve transparency in a regulatory framework.

We have already fully honoured our commitments under the basic telecom agreement of the World Trade Organization and have fully implemented the regulatory principle in the so-called 'Reference paper on basic telecommunications'. As pointed out before, Hong Kong's market did not become competitive at one go. There was a process; there had never been any monopoly of the paging services; customer premises equipment like telephone instruments became fully competitive from the early 1980s. Therefore, from 1982, customers could purchase telephone instruments, fax terminals, public PBX, and automatic branch exchanges from the market, and connect these to the networks of the monopoly operator. Cell phone operation service became competitive since the introduction of mobile phone services in 1985.

We did have some monopolies; for example, the local fixed telephone service functioned as a monopoly until July 1995. In Hong Kong, even communication with mainland China is regarded as external services. For external services we have commitments to continue with monopoly services till January 1999. For external facilities we have commitments to continue with monopoly services till January 2000. The telecommunication facilities and services in Hong Kong are operated through two types of operators. A facility operator operates the circuits based on cables or satellites, and we have service providers who do not operate the circuits themselves but lease circuits from the operators. Competition in external services started in January 1999,

and for facilities it started in January 2000. Duties of regulator included the development of the telecommunication market in Hong Kong. The amount of competition will tend to depend on whether basic services have been attained. If there is much competition in the market then the players in the market might concentrate on the more lucrative and profitable areas. Perhaps the extent of competition in Hong Kong will not be applicable to the rest of China. One of the reasons that Hong Kong has a very competitive market is because we have well-developed telecommunication networks and services. For example, we have teledensity of 56 per 100 persons and also mobile carriers are in general quite high. We have six operators, and customers have a choice of six operators in the same areas. For service providers, we have allowed the market to determine the number of operators. In general, a large number of operators exist in the small territory of Hong Kong. Nearly 90% of the households in Hong Kong are covered by a broadband network; cable TV network covers 85% of the households; 60% of the household are connected by optical fibre cross-cable network and the other 40% covered by cross-cable microwave network; and Internet networks cover 25% of the population.

Let us turn now to the role of the regulator. Our role is to enforce fair competition. In Hong Kong, we don't have a general law governing competition. That has something to do with *laissez faire* philosophy in Hong Kong. It is the most capitalistic territory in the world. Of course there are some sections of the community that advocate the enactment of a general competition law. There are equally opposing voices in the community against a general competition law arguing that it is too costly for the business community. So this debate is going on as of today.

Another important role deals with networks emerging in the market: customers of one network must be able to communicate with customers connected to other networks and also access services provided by other networks. The philosophy in this respect is to allow the operators to negotiate the terms of interconnections. If they fail, the regulators have the powers under the law to determine the terms of connections. Redressing interconnection disputes is an area of responsibility of the regulator. Developing the common antenna size, or mobile services, or in some cases the action of one operator may affect the other operator. If one service provider migrates from one network to

another, then the operator may again feel aggrieved. The regulator therefore has to goad the operators to cooperate and resolve their conflicts.

Another major role in the sector deals with the problem of accessibility. For example, when a network is rolled out, it is necessary to give the operator access to land in order to install cables and the network facilities. Sometimes there are problems encountered in access of land for rolling out a network. For example, extending a mobile service into tunnels requires the operator to get into tunnels to install the transmitters. There are often disputes related to such plan access, for example, in determining the amount of access fee. There is often another role which may not be a function of other regulatory authority. We are also responsible for the management of radio spectrum. In some countries, this is the work of a separate authority responsible for managing operators' spectrum.

In cases of monopoly or the existence of a dominant operator in the market, it is necessary for the regulator to promote competition in areas where competition has not fully developed. But we feel regulation ought to commence right at the beginning of competition in the market so that, as the market becomes more and more competitive, the level of regulation can eventually be phased out. Apart from the general law applicable to all sectors like general competition law, there is a question of whether or not there should be a sector-specific regulator for different utilities. At least for the telecom sector, during the state of transition to true competition, it may not be entirely efficient to dispense with the sector-specific regulator, because the sector-specific regulator understands the issue of industry more and is able to dispense with those issues in a more efficient manner. A general competition authority might take longer time to redress the issues dealing with the telecom sector. Also the system alone may not be able to cope with the complexity of the sector-specific issues.

As far as the development of competitive markets in Hong Kong is concerned, we are in a state of transition to a competitive market. Major telecommunication networks and service operators work as a monopoly. For example, we had a monopoly for the operation of local fixed telephony service until July 1995 and there was also an exclusive licence for external communication till 1998. So in monopoly days we had to spend a lot of time to regulate the boundary between monopoly area and

areas outside it. At that time, one of our major concerns was to ensure that the monopoly would not extend to areas of new technologies. For example, we had monopoly for local fixed telephone service, we did not extend it to cellular services. Moreover, the monopoly operators operate some services outside the monopoly areas. We had to ensure that these monopoly operators of locally fixed telephone services do not give favourable treatment to clients supplying customer premises equipment. Otherwise competition in the customer premise equipment sector would be hampered. Mobile phone service operators in 1985 tried to argue that mobile phone service should form part of the monopoly service and opposed the introduction of competition in this utility. Our job in Hong Kong is to prevent this expansion of monopoly area; so we went to the extent of seeking an interpretation by arbitrator to interpret the law, norm, and rules and to ensure competition in operating mobile service in 1985 in the face of monopoly for local fixed telephone service.

We had an exclusive licence for external communication, which was not to expire until September 2006. Even when this exclusive licence was in place, we tried to restrict the scope of monopoly. So the policy at that time was liberal rather than expansive interpretation of the scope of exclusive licence. So, we introduced competition in areas like network services, call-back service, and self-professional service of external communications. Therefore it has been possible to introduce competition in these areas, which were interpreted outside the area of exclusive licence. Once we have decided to introduce competition there are two options. One can wait until the exclusive licence is to expire or you can negotiate early termination of the monopoly. In the local fixed telephone service we adopted the first option. We waited until the monopoly naturally expired at the end of June 1995. However, we introduced competition in the market for the external services and circuits, though monopoly would not end until September 2006, because we felt that Hong Kong will be left behind if we allow the exclusive licence to run until its natural expiry. We negotiated for early termination of the external licence.

In the transition to competition to determine market structure, one of the roles of the regulator is to decide how many operators are admitted into the market. In Hong Kong, we have

adopted a philosophy that unless there are technical constraints like availability of radio spectrum we allow the market forces to determine the number of operators. That is why there are a large number of operators for network services and for Internet access services. Another option for the regulator is to take part in the selection of players. The approach used in Hong Kong is competitive bidding in scarce resources, which is permitted by law. So far we have been using the bidding context approach, which evaluates application on merits. In the transition to competition, it is inevitable that the incumbent operators command the majority of the market shares or have a lot of market power. If this is not properly managed, entry of new operators into the market cannot be facilitated and competition cannot be developed. For example new operators cannot compete with the incumbent operator in their entry into the market in the original customer database. So we feel that it is necessary to introduce permanent operator regulation where the incumbent operator who has the market power is subjected to more stringent regulation compared to the new entrants into the market. The tariff of the dominant operator is subjected to regulatory approval but the tariff of the new incumbent need not be approved by the regulator. The new incumbent just needs to publish the tariff while the tariff of the dominant operator needs to be submitted before the regulator for approval. The dominant operator is not allowed to offer discount without approval so they have to charge the customer exactly the rates approved by the regulator. Also in the reporting of the accounts to the regulator, the dominant operator is subjected to a more detailed account separation requirement where the company's accounts are separated into specific segments. In the case of Hong Kong Telecom, the incumbent operators have to report the accounts for 24 different segments of the services they operate. We enforce fair competition law which is provided for in the Telecommunication Ordinance. In the transition to fully competitive market we have to determine the terms of interconnection and encourage the operator to commercially negotiate them. There will always be areas in which they fail to agree on terms of interconnections, on a commercial basis, and as regulator, help them to arrive at the terms. We also have to intervene in the case of extending facilities essential for the provision of services like local loops since it is rather difficult to duplicate loops to



consumers. Competitors may require access to the local loops of the incumbent operator to reach the customers, and if they cannot agree to the terms of the local access, the regulator will have to step in.

We have to ensure that access to the limited resource like telephone numbering will be fair as all operators have numbers from the same line of the same structure so that from the customer's point of view there is no difference in extent of convenience in switching to the different operators. So if a customer switches over to a new entrant, he still has the telephone numbers of the ATT links. Thus, there is no discrimination and this is very important to safeguard competition in the market.

In Hong Kong we have adopted the philosophy of not taking an active role in enforcing quality of service. If there is sufficient competition in the market, the customers have genuine choices and operators have incentives to improve the quality of service. Otherwise, they will upset the customers and customers will simply migrate to the other service providers or network operators. So our aim is to ensure that there is genuine choice in the market. We feel that the customers ought to be able to make an informal choice of operators, and the regulator enables an environment for reporting of the comparative performance of different operators, so that the customers can make their choice.

With more and more competition in the market, the question of whether or not the universal service can be achieved is significant, because new entrants may be more inclined to concentrate on areas that generate more profits and neglect areas which are less profitable. We feel that the regulator ought to set up a fair system to cover the cost of providing universal service. In Hong Kong, we have an incumbent operator who has the obligation to provide universal service but the cost of meeting this universal service obligation will have to be fairly borne by all operators in market. We apportion the cost of meeting universal service coverage based on the volume of international traffic or external traffic covered by the operators. So all operators of the external service will have to fairly pay the cost of meeting the universal service obligation.

In Hong Kong, there is a consumer protection body called the Consumer Council. This body has the power to require the operators to take certain actions to protect consumer interests.

Our philosophy is to encourage the consumers to approach the operators on a first line basis, and, if they feel that the operators cannot solve the complaints in a satisfactory manner, they can then turn to the Consumer Council to look at whether or not the services provided by the operator meet the licence conditions. And if not, what action should be taken to restore the service back according to the licence conditions.

Now I will quickly go through the consideration in determining the exclusive licence for the external services and circuits. Originally, the monopoly for exclusive licence was not to expire until September 2006. Our consideration in 1997 was that the licence – the contract between the government and the monopoly operator – should be fully honoured by the government. If the government cancelled the licence without negotiations and without compensating the monopoly operator, the confidence of the investors in Hong Kong would be undermined. The early termination of the exclusive licence was done in a perfectly cordial atmosphere. The amount of compensation offered to the monopoly operator had to be justified since the cost is borne by the public coffer. The compensation given was based on an estimation of the net present benefit of the company if the exclusive licence were to continue and the net present value of the company. We estimated the cash flow of the company until September 2006 and took into consideration the terminal value of the company until September 2006. The difference in the net values between the two scenarios was estimated as the fair compensation to be paid to the company. Eventually an agreement was concluded between the government and Hong Kong Telecom in January 1998 and the exclusive licence was terminated earlier on 30 March 1998. Under the framework of this agreement, although the exclusive licence was terminated, competition to external service was to commence from 1 January 1999 and competition to external facilities from 1 January 2000.

As part of that agreement, apart from compensation, there were some supplementary benefits to the company. First we agreed to the schedule of refinancing the local telecom tariffs so the local telecom tariffs were kept at below the cost. We agreed that the local telecom tariffs may be progressively raised to the cost level. We also agreed with the company on the ways of royalty payment to the government, which originally represented nine per cent of the gross revenue.

The agreed compensation to Hong Kong Telecom was 6.7 billion Hong Kong dollars (equivalent to 859 million US dollars) and the total benefits to the Hong Kong Telecom, from compensation and additional benefits accruing through refinancing of local tariffs and from waiving royalty, amounted to 13 billion Hong Kong dollars (1.7 billion US dollars). The benefits from early termination to the community was estimated to be 17 billion Hong Kong dollars. We estimated the benefits to the community by estimating the amount of consumer savings as a result of competition in the market. In estimating this, we considered the drop in costs of international calls. The amount of consumer savings for the remaining tenure of the exclusive licence is estimated to be 17 billion Hong Kong dollars. This exceeds the 13 billion Hong Kong dollars given to the company by way of compensation and other supplementary benefits. That is why we have been able to justify this determination to the legislature. And the legislature approved the payment of the 6.7 billion Hong Kong dollars as compensation to the Hong Kong Telecom.

As a result of the termination of the exclusive licence and the introduction of competition in January 1999, prices of international telephone services dropped dramatically. We estimate that up till now the consumers have saved more than 6 billion Hong Kong dollars, two years after introduction of competition.

I would like to conclude by saying that competition has led to improvements in the telecommunication industry in Hong Kong and consumers have benefited from competition in different sectors of the telecom industry. A regulator has an important role to play in guiding the market from a monopoly to a fully competitive one. But the intervention of regulator should be minimum, and government should implement a non-inclusive regulatory framework. The level of regulation should reduce as the market matures.

Session 4  
**Issues on regulation in infrastructure sectors**

*S Sundar\**

Until the late 1980s, infrastructure services were provided in most countries by governments and government-owned utilities. It is only in the 1990s that governments recognized the need to attract private investment in the delivery of infrastructure services. This recognition in most countries has cut across all political ideologies and has been dictated by certain non-ideological and pragmatic reasons such as the need to provide efficient and cost-effective services in order to compete globally, the need to attract additional investment from the private sectors in infrastructure as adequate funds were not available from the public investment programme, and the need to introduce competition in order to improve efficiencies and reduce costs. Technological changes in recent years also made it possible to unbundle services vertically and introduce competition horizontally.

With moves to attract private investment, there also came the recognition that an independent regulatory body had to be established outside government in order to provide a level playing field between large and powerful incumbents and new entrants. Even with the prospects of introducing competition, infrastructure sectors retained strong monopolistic elements. And since the service providers were mainly governments or their agencies, the regulatory body had to be outside government and an arm's length relationship with government. Infrastructure regulation is not new to countries in South Asia. But what we now need is a different regime that helps to attract investment by assuring the investor of fair returns on investment, a regime that ensures consumer protection and earns consumer trust.

Against this background, let us see how regulatory reform has evolved in India, and the lessons that countries in SAARC (South

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Asian Association for Regional Cooperation) can learn from the Indian experience. A look at regulatory reforms in India reveals that the initial emphasis in 1991/92, when the process of liberalisation started, was on the privatization and commercialization of infrastructure services. At that time, policy makers did not appreciate the need for regulatory reforms to facilitate the orderly entry of the private sector and create a level playing field between new entrants and incumbents. Regulatory reform was thus not contemplated as part of the initial reforms but was introduced later largely as a result of investors' demand. Take the port sector, for instance. When one particular container berth was being privatized in an Indian port, the bidders demanded that there should be an independent agency for tariff regulation, and tariff setting should not be left to the incumbent operator/government. In the power and the telecom sectors also, investors insisted on independent regulators to regulate tariffs and create a level playing field. There was also pressure from some multilateral agencies such as the World Bank to introduce independent regulation. In the telecom sector, private investment was invited in manufacturing telecom equipment in 1990. The value-added services were thrown open for private investment in 1992. In 1994, the National Telecom Policy announced broad guidelines for the entry of the private sector. Mobile telephones were introduced thereafter. The Telecom Regulatory Authority of India was constituted only in 1996, some six years after the sector was thrown open to private investment.

The experience in the power sector was similar. This sector was thrown open to private investment in 1991/92 with the setting up of generation facility through the MoU (memorandum of understanding) route. Eight fast track projects were identified, and the government agreed to issue counter guarantees without seeking the advice of an independent regulator. The first electricity regulator was set up in Orissa in 1996 and the Central Electricity Regulatory Commission came into being only in 1998.

These two examples show that in India the initial thrust was on attracting private investment, and the independent regulator came into being only when it was realized that private investment would not flow into a sector unless an independent regulator was in place to create a level playing field for new entrants, and assure them of a fair return on their investment.

## Requisites for sound regulation

Let us now look at the requisites for sound regulation. An independent regulator should have a well-defined and clearly laid down scope and powers. Regulatory independence is necessary to ensure that it is effective and that decisions such as tariff setting are insulated from political interference. An independent regulator has also to be accountable, and we have had considerable discussion on this issue earlier this morning. And, finally, there should be a healthy relationship between the government and the regulator and also between the regulated utility and the regulator.

In South Asia it is perhaps best that the independence of the regulator and the powers and the scope of regulation are clearly defined through legislation. In fact, the legislative route for setting up regulators and guaranteeing their independence has been adopted even in some of the developed countries of the west. In the United States, for instance, regulators have been set up through specific legislation, which defines the scope for regulation and guarantees the necessary independence and powers of the regulators.

A good test to determine the scope of independent regulation is to see whether an issue is best settled by political considerations or on the basis of technical expertise. In other words, who is best equipped to address an issue should be the deciding factor. The kind of respect or confidence the regulator enjoys with the government and public at large are some other factors that would determine the scope of regulation. One of the core functions of the regulator should be tariff setting. This calls for enormous expertise, which is always not within the reach of the government. There are also functions like the laying down of quality standards, monitoring standards, and interconnectivity in the telecom sector that are best addressed by the regulator. These are the kind of functions that should constitute the core functions of the regulatory agency.

An important question that has exercised most countries is whether licensing should be a regulatory function or not. There is no unanimity on the subject. There are many countries where licensing is not a regulatory function, and where the regulator's role is only to advise on issues such as privatization and licensing. In India, for example, the licensing function in most cases has not been assigned to regulators. Here the regulator's role is restricted

to advising the government on the policy matters necessary for the healthy growth of the sector.

### Scope of regulators in India

There are three regulators at the federal level in India: TRAI (Telecom Regulatory Authority of India), CERC (Central Electricity Regulatory Commission), and TAMP (Tariff Authority for Major Ports). All of them regulate tariffs. But only the CERC has been mandated by the Act to take measures necessary to promote competition in the sector. Interestingly, the TRAI Act of 1997, mandated the regulator to take measures to encourage competition. But when TRAI was reconstituted in 2000 through an ordinance, the mandate to encourage competition was abrogated and made an advisory function.

None of the regulatory authorities have any role in licensing new players in their sectors, although TRAI has the right to recommend or advise government on issuing new licences and on the timing of entry of new players. Both TRAI and CERC are mandated to laying down the standards of quality of service and monitoring them. On the other hand, TAMP is more a tariff setting body rather than a regulator in the true sense. However, in revising port tariff, TAMP has attempted to link tariff revision with efficiency improvements and has used tariff revision as a mechanism to improve the quality of service. Only the CERC has the powers to settle disputes. Under the 1997 Act, TRAI had the power to settle disputes, but the TRAI Act, 2000 has vested these powers in the Telecom Disputes Settlement and Appellate Tribunal.

Not all regulators in the world are independent authorities. In the UK, the regulators are not independent authorities set up by an Act of Parliament but are part of the ministries concerned. To be effective the regulator need not necessarily be set up by an independent Act nor does it have to be an independent authority. In fact, setting an independent authority through legislation could result in friction between the regulator and the government. However, given the fact that the concept of independent regulation is new to our countries, it is, perhaps, best that the regulator is set up in our countries by an Act of Parliament.

Setting up a regulator as an independent body through a legislation is by itself not enough unless the legislation addresses certain basic parameters to ensure that the regulator is truly

independent. There has to be clearly laid out qualification and disqualification criteria for the regulator to ensure that the choice of the regulator is not arbitrary. The process of selecting a regulator should be independent and transparent, because if the executive were to appoint the regulator at will, the institution will surely lack independence. In America for instance, the regulator has to be confirmed both by the executive and the Senate. In Argentina a similar approach has been adopted, and there is also a process of selection through a committee of regulators. The regulators should have a fixed tenure so that they are not at the mercy of the executive. The criteria and procedure for removing the regulator from his office before the expiry of his tenure has also to be clearly laid down. The regulator should have financial autonomy and freedom to hire expertise, since one of the basic reasons for setting up independent regulation is that the regulator can hire the best expertise available at salaries dictated by the market. The regulator should also be fortified with sufficient legal authority to exercise his functions. So unless legislation ensures that all these parameters are addressed, it cannot guarantee the autonomy of the regulator.

Let us look at how these parameters have been addressed in India. The regulators in TRAI and TAMP are chosen by the government, and there is no independent selection process. It is only the CERC Act that has stipulated that the chairman and members of the commission should be chosen from a panel drawn up by an independent selection committee. The qualification and disqualification criteria in all the three cases have been laid down by the relevant Acts. The tenure in all the three cases has been prescribed and the criteria for removal in all the three cases have been laid down, but the procedures for removal are different. The chairman and members of CERC cannot be removed without prior consultation with the Supreme Court of India. There was a similar provision in respect of TRAI in the 1997 Act, but that was removed in the 2000 Ordinance. The provision now is that the chairman and members of TRAI can be removed after they have been given an opportunity to be heard. This is a retrograde measure as it militates against the independence of the regulators. None of the three regulators have the powers to hire staff without government approval. Thus, one of the great advantages of independent regulation has been, to a great extent, lost. Again, it is only the CERC which has its



expenditure charged to the Consolidated Fund of India. The budgets of TRAI and TAMP have to be approved by the ministry concerned and funded out of the ministry's budget. Thus they lack financial autonomy, and cannot, therefore, be totally independent. All three of them have some legal powers to call for information and to ensure the presence of witnesses and to examine them. But none of the three have complete judicial powers under the Cr Pc (Code of Criminal Procedure), which some of the state electricity regulatory commissions enjoy. For example, the Orissa Electricity Regulatory Commission has full powers under the Chapter 26 of the Cr Pc, which none of the federal regulators have. In short, regulatory legislation in India has not satisfactorily addressed the parameters that determine regulatory autonomy, and there is a need for reviewing the legislation to correct the lacunae and inadequacies.

The regulator should no doubt be independent but he should also be accountable for his actions. We had considerable discussion earlier on whether provisions for appeal were adequate to ensure accountability. Accountability can be ensured by other measures as well. The decision-making process should be totally transparent and that, to a large extent, marks the difference between independent regulation and governmental decision-making, which continues to be opaque in our part of the world. Interestingly, federal regulatory legislation in India mandates the regulators to follow transparent procedures. The legislation also provides for an appeal to an independent body. In the case of CERC, the law provides for an appeal to the high court. The TRAI Act, 1997 also provided for an appeal to the high court, but the new Act of 2000 has set up the Telecom Dispute Settlement and Appellate Tribunal, consisting of a judge, as the chairman, and two other members chosen from different fields like engineering, economics, administration, or commerce to entertain appeals against the orders of TRAI. We have had some interesting discussion this morning as to whether in entertaining an appeal against a regulatory decision, the judiciary should look only at points of law or whether it could also go into the merits of the substantive decision. In the UK, the judiciary invariably follows the practice of deciding an appeal on the basis whether the decision is 'unreasonable'. To establish that a decision is 'unreasonable' is indeed very difficult and the judiciary in the UK has by and large refrained from going into the substantive merits of a

regulatory decision. But in India, in the few cases that went on appeal against the orders of TRAI – these were appeals on the question of the jurisdiction of the Authority – the courts have tended also to look into the merits of the regulatory decisions. It is ultimately for the courts to decide, when they entertain an appeal, as to whether an issue is a legal issue or not, whether the regulator has ignored points of law, and whether all facts have been reasonably considered. The judiciary can well choose to address substantive issues but the resolution of the issues involved may call for technical expertise which the judiciary does not possess. There is, therefore, merit in setting up, as Dr Kamal Hossain argued this morning, a dispute settlement or adjudication tribunal, which in addition to a judicial presence and a certain judicial approach that such presence can bring about, has the necessary technical expertise and competence to go into substantive issues and settle an appeal on merits. This is the course that has now been taken in the case of TRAI.

In all these Acts there is provision for the Parliament to scrutinize the annual report of the regulator. Standing committees, attached to the ministries can also scrutinize the administration reports of the regulators. However, the legislators must realize that while they have the powers to scrutinize the functioning of the regulators, they should refrain from entering into an assessment of the substantive decision that a regulator has made. Fortunately this is not yet a major issue in India. There is also external scrutiny in India by the CAG (Comptroller and Auditor General). The CAG extended his scrutiny of TRAI to substantive decisions of TRAI on the ground that they caused financial loss to the public utilities. This decision of the CAG was clearly untenable. The amended TRAI Act has taken care to restrict the CAG's supervisory role to scrutinizing the expenditure of TRAI. External scrutiny is necessary but there must be restraints, either adopted by the external agency itself or placed by law, to ensure that substantive regulatory decisions are not subjected to external scrutiny other than that of the appellate body.

Sound regulation also requires that the regulator should have the power to access information and the authority to issue directions and that these directions should be enforceable in the court. The regulator should have the authority to impose a fine for non-compliance and to prosecute the officials for contempt of orders. These issues again have not been treated uniformly in the

different Acts setting up the three different regulators in India. TRAI has the authority to access information and conduct investigation, while CERC does not have such powers. They can pass orders and impose fines for non-compliance, but each one has different quasi-judiciary powers, and the treatment is not uniform.

Independent regulators set up in India have to take great pains to demonstrate that just as there is no regulatory capture by the industry, there is also no regulatory capture by the government, that they maintain an arm's length relationship with the government and are not dictated to by the ministries. So far relationship between the government and the regulator is not an easy relationship and there is hardly any consultation between the two. In such a situation, legislative provisions that empower government to issue policy directives to the regulator assume importance.

The central regulatory legislation in India as also the Acts setting up the various state electricity regulatory commissions vest the government with the right to issue policy directives to the regulator. Some of the Acts stipulate that policy directives must be issued in consultation with the regulator, while some do not provide for any consultation before the issue of policy directives. However, policy directives issued by government have to conform to the objectives of the regulatory legislation and should not relate to administrative or technical matters. But what is a policy decision is ultimately something which the government decides. Policy directives issued by the government should also be subjected to the doctrine of legitimate expectations or promissory estoppel.

The reasons for the issue of policy directives must also be transparent. In the electricity sector in the UK, the policy directives issued by the Secretary of State concerning to the regulator, the reasons for the issue of directives, the process of consultations, or the substance of the consultations that went in before the issue of the directives have all to be made public. There is no such requirement in India.

Let's look at some of the trends in regulation in the Indian telecom sector. The regulators' jurisdiction has been repeatedly challenged by the regulated entities in the telecom sector. In fact, the first few challenges were on questions of jurisdiction and the Act had to be amended through an ordinance to resolve some of

these conflicts. There has been general reluctance on the part of the regulated entities to accept an independent regulator.

A more recent tendency on the part of the government has been to bypass the regulator on several major decisions relating to the introduction of competition. The national long-distance services have been thrown open to private sector participation and the timing for throwing open international long-distance services for private sector participation has been advanced. All these decisions have been taken by the government without consulting TRAI. TRAI itself was reconstituted in 2000 through an ordinance and the government demonstrated that through a stroke of pen, regulators can be dismantled and reconstituted. So whatever be the merits of the 2000 Ordinance, it sent out a signal that the regulator can be reconstituted and the powers and scope of the regulator can be altered through a legislative fiat. The 2000 Ordinance was promulgated without public consultation or without prior parliamentary approval. The appellate jurisdiction and the disputes settlement jurisdiction of TRAI were also taken away through this legislation.

In the power sector too, the progress of regulatory reform has been slow. Regulatory commissions have been set up in some 14 states but regulatory functions have been effectively exercised only in 2–3 states. The regulator has taken a series of decisions in Andhra Pradesh, Uttar Pradesh, and Karnataka, but in most other states there has been hardly any progress. State governments have introduced independent regulation but still do not seem to appreciate the need for proceeding with regulatory reforms. There are instances where the state governments have used the regulatory mechanism to make sure that there are no tariff rebalancing or tariff resetting exercises. The basic reform structure is being questioned at different levels. In government, there is great a deal of continuing cynicism on the role of independent regulation and the regulated entities have not yet fully accepted the need for regulatory reforms.

Many of the regulators do not have the necessary administrative infrastructure or other facilities to function effectively. Governments are not showing the necessary commitment to overcome these difficulties. Staffing continues to be a major problem with the regulatory authorities since it is not easy to get staff with necessary expertise. This is a major problem in the telecom

sector. It is also a problem in the electricity sector where the staff largely comes from the regulated entities and do not have the mindset to discharge regulatory functions. Regulators need a lot of assistance in formulating tariff policy. There are not too many agencies or consulting groups that are capable of providing such support to the regulatory authorities. TERI is providing such assistance to some of the state electricity regulatory commissions. There are also some private consulting groups that are providing assistance. However, this assistance is expensive and is not easily available. Besides continuing resistance from the regulated entities, there is lack of support and commitment from the government. The respective ministries are unhappy that they have lost power and patronage. They find the regulators no different from the species that they belong to and question their capability to deliver effective regulation. Regulators themselves are yet to establish legitimacy. Because of their bureaucratic background or their quasi-judicial status, the regulators in India have not reached out to the public to explain their role and how their effective functioning could benefit the sector by bringing in more investment, ensuring better protection of consumer interest, etc.

These are some lessons that other sectors in India and the states that have not so far set up regulatory agencies, and perhaps other countries in South Asia that are in the process of setting up regulators, should learn. The regulatory authority should be put into place before or at least along side the opening up of a sector. The experience of the telecom sector in India has demonstrated that the opening up a sector for private investment without a regulator in place could result in enormous complications and all kinds of problems on connectivity, revenue sharing, etc., which the regulator may later find almost impossible to resolve.

What the Indian experience has also demonstrated is that the design of the regulatory agency has been left largely to the genius of the concerned ministry, which has created the regulator. The power ministry had thought differently from the telecommunication authority, or from the ministry which deals with ports. As a result, the extent to which powers have been delegated to the regulators has been determined by the mindsets of the ministries concerned. There has been no central thinking on how regulatory reform process should be proceeded with. For example, in the case of the disinvestment in India, there is a group of secretaries that addresses all kinds of problems or issues relating to

disinvestment. But such a task force or central thinking process on regulation does not exist and, as a result, each regulatory legislation is different from the other.

Regulators must be given substantive start-up assistance by government in terms of provisions of staff, in terms of physical infrastructure, and in terms of provisions of all the concerned facilities so that they can start performing their functions speedily.

Staff training is another very important area where groups and organizations like SAFIR, World Bank, and TERI can all help. Staff training is not only on the particular sectoral issue but also on regulatory issues in general. I have already dealt with the need for consulting support in areas of policy formulations and setting up processes. But ultimately whatever be the colour of the legislation and substance that has gone into the legislation, the regulator can perform effectively only when the role of independent regulation is recognized by all the stakeholders specially by government, and government demonstrates its willingness to support regulatory reforms. Setting up a regulator based on legislation and expecting a regulator to function as a department of government may not work. The mindset has to change, and governments must come out with demonstrated willingness to support regulatory reforms. Finally, the regulator will have to earn legitimacy, and only then can the institution become effective.

Concluding session  
**Plenary discussion of group outputs:  
Presentation of Group I**

*Palitha Gunawardene\**

The group started by discussions on the importance of managing two kinds of relationships: inter-operator relation and operator-regulator relation. We felt that these relationships could change depending on the market conditions. At the early stages of liberalization and introducing competition, there will be one player with dominant market power and the others who are new entrants. The relationship between players in that kind of setting would be much different from relationships where all players have equitable market power. There could be hostility between the regulator and dominant operator in the early stages of introducing competition.

Then we looked into the process of appeal and the mechanism of resolving some of the disputes that are likely to emerge among operators. There are differences of opinion whether the disputes are best resolved through adjudication, arbitration, mediation, or judicial review. I now go through some of these points.

We felt it is important for the regulator to initially examine if there is any error in the process or if some other material crucial for the process has not been considered. Then, during process of arbitration, operators are brought together and their views are heard. Thereafter, an expert group or an appellate body, which consists of a senior judge and two experts, decides on the issue.

Another aspect that was discussed is 'mediation'. Here, there were two sets of opinion. One is that it is not appropriate for the regulator to participate in the mediation process. The other view is that mediation is an important process, because this may help in bringing about an understanding between the operators, which, in turn, could reduce the possibility of a formal appeal or formal process being held. In the process of mediation, and perhaps even in the process of adjudication, there are some areas

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that are presumed to be important such as how this process is going to be conducted according to guidelines agreed to by all the parties involved. There are open hearings or open-house consultation with all the parties before coming to any conclusion. Even in decisions by regulators or by the appellate bodies it was considered important to have what is called 'self-contained decisions', which give the reasoning behind the adjudication. It is necessary to provide a summary of the mediation since sometimes people would like to get the crux of mediation at a glance. Mediations should get wide publicity because all the stakeholders need to be aware of the reasons to make the process more credible and also help in its enforceability. In this regard, it was felt that it is important to provide for a review process. In case there are obvious mistakes that have been committed by the regulator, this process ensures that it can be rectified. It was suggested that this 'review' be conducted by an expert body rather than a judicial body, because judges may not be fully aware of the technical aspects involved in the regulatory process.

The necessity of regulators appearing before the judiciary or only sending a written communication to it was also discussed. The practicability of appearing before judicial bodies in several areas of the country was debated. Here the important factor to be considered is how effectively a regulator can present his case. It is important that judges are made aware of the reasoning of the regulators and the background of the proceedings. So even if the judges are called upon to make orders, they are aware of the technicalities and the background of the case.

Next, we moved into the area of universal access which differs in different sectors. For example, universal access in electricity is perhaps not the same as what is meant in the telecommunication sector. But, perhaps, there are similarities between telecommunication and water sectors. So, there was a need to define the universal access. But that again would depend on two factors, namely the country and the sector, because these will have an impact on how it is defined in a particular environment.

Then there was a discussion on the necessity of subsidies. Subsidies are considered necessary in certain instances, but the group agreed that these should be implemented through a transparent process. It should be implemented in a manner that everybody understands that it is targeted on a specific objective and is not open-ended. Also, it is important that subsidies are



competitively neutral and do not create a competitively inequitable position by having subsidy that favours one operator at the cost of the other. The group also felt that though subsidies are sometimes necessary, they might not be ideal because one does not know from where the funds would come. In this regard, the issue of subsidy funding came up. Is the funding generated through some form of taxation from the consumer or through a levy that is charged from the operators?

We then moved on to the process of tariff rebalancing. There was wide perception in the group that some of the existing studies on tariff balancing are not cost-based, and it is important to bring it on to cost basis. Here, we focused on the inadequacy of information, the need to procure information from the operator, the need to analyse the information to ensure that it is accurate, and the importance of benchmarking in the absence of this information. The need to compare the information that we get from the operators was also considered important. Managing the process of tariff rebalancing is important to ensure that its negative effects are controlled. It was stressed that tariff rebalancing should be carried out after giving adequate consideration to the existing realistic ground situations.

During the tariff rebalancing process, it is necessary that all the stakeholders, particularly the consumers, are informed that tariff rebalancing necessarily means an increase of certain tariffs. There is often criticism of an increase in tariffs. Since nobody likes to pay more for anything, a simple message justifying the tariff rebalancing is important. Certainly there is theoretical background to tariff rebalancing but it is difficult to communicate that to people. So a simple message is often the best measure to defend increases during the process of tariff rebalancing and is possibly more effective in reducing the resistance rate. One of the ways of possibly reducing resistance is to attach conditions. While rebalancing tariff the regulator can also introduce service quality improvement requirements. For example, in telecommunication if you increase the rates and if the operator fails to provide the required service within a certain period, he should be liable to pay a compensation to the consumer.

The importance of enforceability was discussed at length. All the conditions attached to tariff rebalancing lose value if they are not implemented. The importance of competition in tariff fixing was also noted. Competition most often results in the reduction

of tariffs. There is also a wide perception that with the cost of technology coming down, the fixed telephone tariffs and the cellular telephone tariffs may converge, and most of the tariff rebalancing would affect the fixed telephones. But in that competitive environment the fixed operator may not want to go away or go ahead with increasing tariff, as the market conditions may be disadvantageous for him to go through to it. And, of course, with the reduction in cost of technology, that also acts as mode of encouragement for the operators to go ahead with tariff rebalancing. Given that tariff rebalancing has been historical across regions, there is a need for rebalancing, but the extent would depend on various circumstances in the country.

Tariff rebalancing has to go hand in hand with government policy. An increase in tariffs, is not a popular move and could affect the government politically and bring in pressure from the politicians on the regulators. So we have to take the government policy into consideration while implementing tariff rebalancing and managing these processes.

Next we discussed renegotiations of concessions. The group reflected upon the presentation last afternoon, where the need for a certain amount of flexibility while drafting statute contracts was stressed. This is particularly important in the telecommunication sector where with fast improvements in technology we may come to a situation where the commitment or concessions given few years ago may not be enforceable. In that situation it is best to withdraw those concessions which cannot be given as happened to some extent in Hong Kong. However, when regulators are attempting to pull back concessions, they have to ensure that the investors' confidence is not diminished. Therefore, there has to be certain amount of financial compensation if concessions are withdrawn or some other concessions can be granted to offset the withdrawal of the earlier concession. How much compensation is paid or what other concessions are given is another important aspect of managing public perception. Some people will question the payment of compensation on the grounds that such payments are to the detriment of national finances. In such cases it is important to highlight, as in Hong Kong, that the amount paid as compensation is far less than the benefits that will accrue to the consumer.

## Presentation of Group II

*D K Roy\**

Quality of service is the subject we have discussed in our group. This includes service conduct, consumer protection and education, and developing healthy relations with governmental agencies and other regulators. Quality of service involves the setting up of two types of standards: overall performance standards and guarantee standards.

Overall performance standards indicate the main standards of technical and non-technical performance against which the performance of the licensees shall be judged. Guaranteed standards are those which licensees are mandated to satisfy, failure to comply with them will result in penalties or compensation to consumers. Next we discussed the laws that cover the criterion on which standards are prescribed, monitored, and enforced. The regulators will have to lay down standards after consultations with the service providers and other stakeholders. While the law indicates the broad areas of standard of performance and consumer protection the details are to be set by the regulators. The regulators must set the standards through a consultative process, taking into account the opinion of the players.

Next we dealt with the laws of prescribed penalties and the procedure for imposing penalties. Unless the law gives a very specific mandate in this regard, imposition can be later challenged in courts. Therefore, the laws should at least specify the range of penalties that can be imposed. The procedure for imposing penalties should also be broadly prescribed. Laws should empower regulators to award compensation. The regulatory authorities should prescribe payment of compensation to consumers in case of infringement of prescribed standards to the operators. The service provider should be persuaded to

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voluntarily agree to payment of compensation in case of infringement of standards. In the UK, the standards have been provided in the law itself. Initially, the law did not prescribe the standards. So the operators were summoned and given standards for different areas of their operations. Fixing the standards reduced litigations in the UK since the companies suo motu offered compensation for every failure to comply with guaranteed standards.

The quality of service has to be monitored through scrutiny of regular report and returns prescribed by the commission, inspection and/or public hearing, as well as specific performance audits whenever there are many complaints.

The periodicity of monitoring of standards should be prescribed by the regulator and will depend on the particular type of service. All information on quality of service gathered from regular and periodic reports and independent monitoring should be publicized in whatever form is considered appropriate, and their copies should be made available.

Regulatory legislation should mandate consumer education and consumer protection. There has been lot of controversy about the extent to which a regulator should safeguard consumer interests. The question of individual consumer protection arose since some Acts do not have such provision. The regulatory authority should not be a consumer forum and the regulator should not substitute the consumer court. At the same time, the regulator should not plead total helplessness in consumer protection. So consumer protection should not be left entirely to the judiciary or consumer court. The regulatory authority has to be concerned about it. It should ensure the establishment of effective complaint handling procedure with the service providers.

The extent to which the regulatory commission should deal with individual consumer complaints was also discussed. While one view was that regulatory authority should not entertain any consumer complaint and that they should be taken to the consumer protection court, the other view was that in exceptional cases the regulatory authority should entertain consumer complaints on a last resort for the consumer in order to establish credibility and legitimacy of the regulator.

We also discussed consumer awareness. Consumer awareness programmes can be undertaken by the regulatory authority through approach papers or press reports. Although it is a quasi-judicial body, the commission should play the role of an educator.

The regulatory authority should also arrange to provide the consumer groups with expert advice. All this will enhance the transparency of the regulatory body.

The next item discussed was the relationship with government and other regulators. Here the pertinent question was the extent to which the regulatory authority should be independent of government. The consensus on this issue was that the regulatory authority has to be perceived as totally independent from the government. Independence implies that the authority should not be under the influence of the government and it should limit its interactions with the government. It was felt that the government should have the power to issue only policy directives consistent with the objectives of the act.

Next we discussed the appropriate process for issue of policy directives. We felt it should be mandatory for the government to consult the commission before issuing directives. However, we felt that the opinion of the regulatory authority should not be binding on the government. Should the directions and reasons behind the public policy be made public? We agreed that the government should make the policy transparent. It must explain the reasons and the circumstances behind the policy issues. The intention of the government should be clear. It was felt that consultations between the regulatory authority and the government may occur as and when there is a need for it. We do not want any institutional arrangements for the interactions between the regulatory authority and the government.

Should there be a law to define the jurisdiction of regulatory authority vis-à-vis other regulatory bodies like competition commission and environmental agency? What sort of relationship should be there of the regulatory authority with other regulators? It was felt that regulators of a particular sector need not refer to and coordinate with regulators and authorities of other sectors except where it is mandatory. However coordination to the extent possible is desirable.

We felt that the regulatory authority can review its decision but only if the law mandates it to do so. Either the general law or any other laws can describe this. However, we did not espouse something like a judicial review as in the US Commission. If the law mandates it and the general law permits, as in India the Civil Procedure Code permits, it can be done. The general law in India provides that there can be a review by quasi-judicial authority

under limited circumstances to rectify an error or in order to accommodate indispensable evidence that could not be produced earlier in spite of due diligence. A sector-specific apex special authority at all-India level is preferable to appeal to a number of high courts. It should be headed by a sitting or retired judge of the Supreme Court and should have as its members persons with special knowledge.

## Summary of question–answer sessions

### **Question-answer sessions 1 and 2**

*Jehangir Basher*

I was in New Zealand seven years ago and asked my hosts there about their methods of regulating the oil and gas sector. They replied that in New Zealand the industry regulates itself. I do not think that is feasible for us in Pakistan. One of the reasons for which we have set up regulatory bodies is that the positioning of an independent regulatory authority will bring in a degree of fairness. With sectoral reforms taking place in countries in South Asia along with privatization and deregulation, it is important that the regulator is independent of the government. There was a lot of reference to tariff setting in the presentation. As we deregulate and introduce competition, the market forces take over. I think in the medium to long term, tariff setting in most of the activities in the oil and gas sector will be phased out. The tariffs will be set by the markets except in cases like electricity where you need a physical carrier. Even in the electricity sector, you have alternative forms of energy. So even here tariff setting will slowly go out. In the future the regulators will regulate areas like safety standards and environmental standards, set quality standards, and prevent monopolies from setting high prices. There is a monopolies' commission in most countries for these things. Where there is a single carrier of a product, gas or oil, setting tariffs that permit easy access to everybody is required. Investors do not want anyone other than the market to set the prices. So down the road, there will be less and less need for the regulator to set the prices.

*Rohan Samarajiva*

I think you bring up an interesting issue. I am not sure whether we have completely agreed on this. I would agree that in a competitive market, the regulator should not be setting tariffs. The elimination of price regulation is a desirable objective.

The question is: When do we get to that stage? When do we have adequate competition, is the more interesting question. There is a regulatory response to this situation. It is the principle of forbearance, which was introduced in Canada and then in the US through the 1996 Act. After taking stock of the market, if the regulator finds that there is adequate competition, he can forbear or not exercise certain regulatory powers. If there was that mechanism, for example, in the cellular market in Sri Lanka, I really would have had no interest in regulating tariffs. But in Sri Lanka, the power of forbearance was not built into the Act. So we have to go through the motions of approving the tariffs. But generally speaking, during my stay as Director General, TRC (Telecommunication Regulatory Commission), Sri Lanka, I kept impressing on my staff that we have to be extremely light-handed in the way we respond to our tariffs. The TRC, Sri Lanka would need to be very quick and apply very minimal criteria in tariff setting. If tariff settings are likely to confuse the subscribers, the regulator should try to make some changes to that. We (namely the TRC) applied different kind of criteria to various types of market, but then, we couldn't apply the same criteria to the fixed access market. There were three suppliers, one of whom had 90% of the market share and enormous revenues from the international sector. In a situation like that, the licensees for the competitive investors would say they are not subject to tariff regulation for a certain number of years in Sri Lanka, five years I believe. So they (namely the TRC) did the classic thing that the economic textbook tells us: focus on just one company. Now at what point this condition of competitiveness is arrived at, I think, is an interesting question, and it is more important that determination is made through an open proceeding as to when this condition is raised, so that if by some chance the conditions later changed, you can come back and take back the power that you gave up. So there is always a possibility particularly given some recent development where all these mergers and acquisitions that are happening in Europe could result in the fact. Sri Lanka's cellular or mobile market now has four powerful independent players, which could suddenly become two, if M/s Hutchinson is taken over by somebody else. So in a situation like this it is important to think about before deciding when there is enough open competition.



*Jehangir Basher*

We are working on developing the oil and gas regulatory authority and enacting rules for that. We are being told to open the sector to the market process. And the market will take care of itself. So the view is that from tomorrow the government will not fix the prices or the regulatory authority will not set the prices. We are told to include the term ‘sunset clauses’ into our Act for a limited period. Thereafter, there will be no price setting. To predetermine these dates, one has to go through government rules and procedures and approval processes. All these are very difficult to achieve.

*S Sathyam*

If I may intervene here, you have come to the other end of the spectrum that we are talking about, namely that of establishing legitimacy, the induction problems and problems with the government, getting statutory powers, getting adequate staff, and so on. Both the presentations about establishing legitimacy and about appeals and reviews decision, taken together, relate to early stages of regulators. The ‘sunset clause’ will come much later.

### **Question-answer session 3**

*Question* You mentioned that you have introduced number portability in Hong Kong and that it was introduced by the regulator. Have you also been instrumental in deciding band co-location or other such issues by the mobile operators’.

*MHAu*

In co-location there are six operators in Hong Kong, and there should be competition among the operators in the quality of service. So we encourage the operators to develop their own network, and they choose the individual cell size. In effect, we have six different networks and six different operators with different cell size. So a few cells on the building rooftop are shared. Only when the operator needs to cover certain area, these are shielded. For example in tunnels, airport terminal buildings, passenger terminal buildings, railway stations, underground railway, and the land of those premises, we cannot afford too many operators and too many dependants within the premises. For these tunnels and shopping arcades, we require the operators

to have so-called ‘shared size’ or ‘co-location’. The role of a regulator is to resolve the operators’ disputes in the development of these commercial sites. The regulator will have to appoint one operator as the lead operator and the coordination operator. The regulators will undertake the project through to equipment acquisition stage and then send appeals to the operators and recover the cost from them. If there is no agreement on how much each operator should contribute towards the development of a particular government site, the regulator will have to decide how much each individual operator should pay towards installation cost.

*Question* In one of the slides, you said that one of the reasons for regulation is to protect and enhance consumers’ interest. But isn’t it the duty of regulator to balance the interest of various stakeholders? Consumers are one of the important stakeholders, but there are other stakeholders as well. Isn’t it the duty of the regulator to balance the differences and often resolve conflicting interests of different stakeholders?

*MHAu*

In this regard, some public debates were initiated in Hong Kong. So the question is how interests of different stakeholders can be balanced. The consumers are also stakeholders and the players in telecommunication services another class. In Hong Kong, we want our policy to be both pro-competition and pro-consumers. So it is not amended to advance interests of the players. But, as I said, the interests of the players and that of the consumers are not necessarily conflicting but are linked. The players are able to come to the market and make their investments or quit if market conditions are not profitable. Investors will not come into the market on their own. If no one invests in the telecom market, the consumers suffer. So we feel that our policy has to be pro-competition and pro-consumers. It is not actually incompatible with the protection of the interests of the players. As I mentioned earlier, we feel the role of the government is to provide, create, and maintain an environment conducive to investors in the development and operation of the telecommunication business in Hong Kong. When the regulator needs to take a decision on a conflict between the players and interests of the consumers, then, the interest of the consumers takes precedence.

*S Sathyam*

You had a situation of a monopoly contract and you negotiated for an early settlement or its closure. Similarly if there is over-competition there is no scope for regulator's entry. They are already there and in such a situation should the regulator attempt to negotiate for exit?

*MHAu*

Whether the operator should exit the market or not would also be determined by the market forces. There is a limit to the number of operators a market can accommodate. Some operators might chose to exit the market and some to consolidate. So it doesn't require the government or the regulator to negotiate with operators to consolidate or exit the market.

*Jehangir Basher*

I think Mr Au echoed one or two comments I made this morning. With the development of markets in our region the regulators will restrict themselves on standard pricing and common access. On pricing, I believe, one of the biggest boosts that competition can get is through deregulation of price. I thought you could have highlighted it a little more in your presentation. On the other hand, to have competition, the market needs more players. Deregulating prices and introducing more players in the market should go together. Deregulating price to promote competition in a limited or undeveloped market may not work. In fact, in Pakistan there are pressures on us to deregulate. If you take regulation away from the government it is expected that the regulator promotes competition and eventually in the medium to the long term, there will be more players and more competition and lower prices. But my question relates to the following: in Pakistan's oil and gas sector, the current regulatory authority is the government department. But we are told in our country that in oil and gas sector, one should get out of the government. How do you reconcile this?

*MHAu*

In Hong Kong, the regulator is the part of the civil service unlike in other countries where there is independent commission. This, I think, has its origin in the days when the regulator was part of the

post office. Because Hong Kong was a British colony, many laws here are similar to those in the UK. Probably in some other countries also there is a post master general dealing with the telecom matters. At that time the post master general appointed the telecommunication authority. This was the regulator of the telecom industry. The telecom authority is still a part of the civil service, but its independence is enshrined in the law. Although the director general of the telecom authority is also from the civil service, the discretionary power vested with the regulatory authority is sanctioned by law. The minister and the secretary responsible for telecom policy cannot direct or influence the regulator in exercising his regulatory powers. One of the functions of the regulator under the law is to issue licences. So the secretary in Hong Kong cannot tell the regulator whom to award the licences and how many licences should be awarded. Likewise, in terms of determining the trends of interconnections, the regulator cannot accept directions from the minister or the secretary. So I suppose independence is given to the regulator by law, although the regulator is a part of the civil services in Hong Kong.

*Question* In case of settling disputes, do you go in for public hearing? If so, can you give some details about the procedure of holding the public hearing.

*MHAu*

We have not set the procedures of public hearing. But the mandate of the regulatory authority is to give affected parties a fair opportunity to make representations, and such representation need not be given in a public hearing. They can be in the form of written submissions, and in such cases where submissions concerning commercial interest do not involve confidential information, they are published on web sites. After the representations are submitted, the authority considers the written submissions and issue decisions, giving reasons. So even if there is no public hearing in Hong Kong, we try to make the process more transparent and give the affected parties fair opportunities.

*Question* Who determines the tariffs of the universal services in Hong Kong?

*MHAu*

The regulator will have to determine the size and the cost of the universal service and then decide on the method of apportionment. We are using the volume of private international traffic to apportion the cost of the universal service.

#### **Question-answer session 4**

*Question* How did the Indian telecom industry react when the independence of TRAI was significantly curtailed?

*S Sundar*

There was no reaction; in fact, they were relieved. The fact is that the government has solved a legal problem that the earlier Act had created. It was said that the new legislation was intended to strengthen the TRAI. In fact, several parts of TRAI were taken away, and the scope of its functions was curtailed. But the government propagated all this as strengthening the TRAI, and the media and the industry accepted it. There are few lone voices, which said that in the process TRAI has been mutilated. But these voices went unheard.

*Question* Mr Au says the regulator has an important role to play in guiding the transition from monopoly to a fully competitive market. He said that the regulator checks for monopoly excess. But regulation is not a substitute for competition. Is there no conflict between two remarks?

*S Sundar*

If you have near perfect competition or a very competitive situation, there is no need for regulation. Regulation really cannot be a surrogate or substitute for competition and competition would deliver best that which regulation intends to deliver. But until such time is reached there is need for regulation. That is what I understand and that is what Mr Au was also saying.

*DK Roy*

Many of the questions that were raised is because of our different perceptions about regulation. But in Hong Kong the situation is entirely different from that in South Asia. Like the commissioner

in Missouri, USA, my role as regulator in Orissa's electricity sector should have been to extinguish my job. The regulator's job there (in USA) is to deregulate. But now to come to that stage in which we start deregulating, first of all there must be regulatory equilibrium. We are trying to start right from the bottom and when the cost has not been recovered. So our problem will be entirely different. We have to see regulation as a transitory stage until we come to deregulate. We are in the transition stage.

*S Sathyam*

Here what I would say is that we are having a US type of regulatory commission to do a regulation of the UK type in the India, Bangladesh, and Pakistan environment. So the issue is that the regulatory commission that we have adopted is the independent commission which is there only in the US. The UK does not have such a commission. We are not having the US type of regulation but the UK type of regulation, which Argentina and Chile have followed. So what happens there has to be examined. With all these problems, the questions that have arisen are: How do you establish your legitimacy? How do you react with the judges? How do you react with your legislature? How do you cater to all the aspirations of the people? We have said these are all critical areas of the regulatory commission. These are things which possibly are very common; we have to develop so as to make ourselves acceptable. People expect that we are going to make a revolution in order to go to cure the ills of state monopoly while bringing in market forces. In fact Mr Sundar and Dr Sarkar of TERI have been advocating a common set of drafts and a similar type of format for the regulatory commissions in all countries of South Asia so that they will have similar powers. The question that has not been raised by Mr Sundar is how the regulator in India, Pakistan, or Bangladesh brings in competition. How are the tariff rates to be rebalanced? How does the regulator make a congenial environment for private sector participation? The latter task is easy for the government, and the regulator possibly has to stand by the government decision. Those are the basic issues confronting the regulators today. Mr Sundar talked only of three central commissions in India, which do not have as much interactions with the consumers as the state commissions will have. The question is whether tariff setting power should be given to

regulatory commission along with other sector regulating functions. It has not been given in some sectors like ports in India. Will the regulator be able to deliver the goods as they regulate in such situations? Should they deliver efficiently without licensing power or without monitoring power? There are many such issues that have to be addressed according to the particular situation. This applies not just to any particular country or also to particular states. So the idea is possibly to explore the best practices in different countries and different sectors. Since our problems are different, we have to develop our own mechanisms to solve them.

Mr Roy, I have to disagree with you on a basic point. I however, agree with Mr Sundar that regulation cannot replace competition. I cannot agree with you that the competition replaces regulation. Given the propensity for manipulation of price and quality, there will always be a need for regulation. In theory, there is perfect competition, but in practice and in reality, there is nothing called perfect competition. All kinds of imperfections that lead to distortion of markets require some regulation. Of course, when competition picks up, regulation should change from intensive regulation and the regulator should pull back to resort to what has popularly been described as light-handed regulation. Otherwise, you will never be able to protect the consumer interests. That is why the regulator's job includes consumer protection and that is a requirement for perpetuity.

*DK Roy*

I am rigid about my view but I am just saying this conceptually because what happens with regulation depends on what the law has mandated the regulator with. The objectives of the regulatory legislation should be looked at. In India, the Acts talked only about curing the financial ills that has occurred to the public sector. So the regulators have been brought in place to take the utilities out of the government and make it attractive to the private sector investment. As I said, the Act does not talk about protecting consumer interests as their overall objectives. However, regulator wants to forget the consumers. That is possibly the basic job of the regulator because that concept has come from the US and other developed countries. Discussions on the issues of public interest and consumer interest will go on for a long time. Public interest is a far bigger concept than consumer interest. So what is bad for the immediate consumers can be good for the

overall public and for the government. The customer interest is to be definitely protected. But how much is it legally mandatory? And even if it is spelt out in the preamble of the legislation, if actual law has no provisions, then it is meaningless.

When we frame an Act, we should be clear about what we want, where to go, and where to start. If the law clearly spells out not only the objective but also the power or limitations it will serve the interests of regulation better. Since the protection of consumer interests has not been spelt out in India's legislation, regulators have a tough time unless objectives are clearly spelt out.

In South Asian countries the bulk of the private investments we are targeting comes from the West. As we also have to cater to the needs and wishes of these foreign investors it makes our job a little more difficult. I must now explain 'sunset clauses'. It is not clear anyway. The sun must set on certain things that we are developing today. Presently, we are highly revolutionary. Control on certain activities must come to an end.

It is useful to compare different commissions in relation to certain characteristics. It would be interesting to pursue larger set of issues, not only in terms of analysing the legislation but in terms of what particular agencies have done or functions that have been performed or kept on ice.

Mr Sundar has brought out the comparative strength and weakness of the different regulatory structures in India. Different criteria have to be developed for every region. There is a consensus that we have to evolve our own regulatory systems for the particular industry in a particular country. The regulator's job is to create an environment for deregulation.

I want to give my views on whether regulation should continue or be stopped and if it has to be stopped, then when. The time will come when regulation will have to be completely stopped. Before that, a true sense of competition has to emerge. Unless we have a true sense of competition, complete regulation has to continue. Second, the people/consumer, who are the main beneficiaries, should be well educated and their views should be taken into account. The consumers' association should be strong enough to judge the quality and the cost of services. Third, in our region we do not have anti-monopoly acts. If the monopoly comes in, then, the regulator has to step in as the US or in any European country. Unless we have these laws effectively implemented, regulation must continue.



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