THE CHALLENGES OF REGULATING STATE UTILITIES FROM A LEGAL PERSPECTIVE

Dion M. Abdool
LL.B(Hons)(Lond), L.E.C. LL.M (Lond)
Attorney-at-Law
Deputy General Manager, Legal Services
Water and Sewerage Authority of Trinidad and Tobago

ABSTRACT

State Utilities by their very nature provide essential services which necessarily demonstrates natural monopoly characteristics.

In the Caribbean, the utilities inherited from the past Colonial regime have remained ostensibly under the governance of the State. The defined purpose of the utilities has been the provision of services and not the making of profit. In this context, the foundation of the utilities was embedded in legislation, not in Articles and Memoranda (as applies to incorporated companies). The utilities were incorporated as statutory bodies.

Regulation of the services provided by utilities have hitherto had their bases in one or more of the forms of quasi-judicial bodies such as the Public Utilities Commission. Subsequently however, contemporary development in regulation of state utilities have been ushered in by various factors including influences of the IMF and World Bank.

A necessary corollary for such development was the reform of the state utilities themselves. In these circumstances the birth of the modern day Regulator such as the Regulated Industries Commission (RIC) was hastened. The Regulator being hoisted on the Caribbean landscape is now no longer quasi-judicial but more in line with an administrative tribunal.

This paper in the context of the above, seeks to explore from a legal perspective, the challenges of regulating state utilities.

August 2003

INTRODUCTION

Utilities are established institutional requirements of civilized societies. They touch and concern in a very direct way, the public health and well being. Historically they were provided by the state for the public good and therefore demonstrated monopolistic characteristics.

In the more recent past, however, many states have taken the path towards demonopolisation of the utilities and privatization. The causative factors are many, but have been fuelled no doubt by the need to ensure greater efficiency in the utilities, the need for private sector capital injection and private sector management as a direct result of a tightening public purse.

In the Caribbean, these imperatives are easily recognized. What is also recognized is the need to establish a regulatory regime for the utilities prior to any form of privatization to ensure that the Regulator can supervise restructuring, pricing reforms and to offer consumer assurance that their interests will be protected and so reduce possible resistance to privatization. The vision is that increased efficiency of supply as a result of demonopolisation or privatization would be translated into lower rates and higher levels of services to the consumer.

The traditional legal under-pinning of the utilities have been statutes authorizing the provision of the services for "the public good". Regulation (where it existed), fell within the purview of certain institutions or commissions (the "Public Utilities Commission" as it was called in our jurisdiction). Consequently, such a situation presented the perfect setting for the absence of competition. Regulation was limited to the control of rates. Regulation was limited in law to the principle "that monopoly suppliers of essential services must charge no more than a reasonable price", **VECTOR LIMITED v. TRANSPOWER NEW ZEALAND LIMITED (1999) 3NZLR646**

Legal challenges to the regulation of a utility in terms of supply or rates charged were limited to judicial review.

LEGAL STRUCTURE OF A STATE UTILITY

Under the Act which established the Utility, a Minister was designated by the statute as being the personality to whom the utility is responsible. Wide ranging responsibility was then devolved onto this utility and included development, provision and control of water supply and sewerage facilities, matters of sanitation, promotion of conservation and proper use of water resources. Baselines for the charging of rates and debt recovery measures which include disconnection and sale of property were also provided.

In short then, the legal structure for a state or public utility provided the mechanism for distribution and control of the relevant service, by the state.

THE LEGAL FRAMEWORK OF REGULATION

Utilities have always been subject to some form of state control. The divesting of the regulatory function by the state was a necessary corollary to the privatization or semi-privatization of the utilities. Regulation was essential as the utilities were providing public services as a substitute for the State.

The UK and New Zealand were at the forefront of this withdrawal of direct government involvement in the utilities in the 1980's. Interestingly, two different framework for regulation were used. In the Caribbean, the model followed has been the UK model albeit on the basis of multisector regulation and therefore the discussion which follows will have a common thread.

The Regulator (in our jurisdiction "the Regulated Industries Commission") was established by an Act of Parliament ("the Act"). Under the Act, the relevant Minister has the power to appoint the Commissioners who comprise the Regulator for a fixed term. The Act details the function of the Minister and the Regulator. The Regulator is required to issue a licence to companies to operate in the industry and to monitor and ensure compliance with the conditions in licenses. An administrative fee is charged on issue of the licence.

The Act spells out the objectives and typically they are to ensure that all reasonable demands for the services are satisfied, to ensure that licencees are able to finance their activities and to promote competition. The Minister and Regulator are also charged with the responsibility of protecting the interests of consumers (with respect to prices, continuity and quality of services), promoting efficiency and economy by companies, etc. The responsibility of the Regulator in the Act is laid down in the broad terms. It thus leaves considerable room for interpretation and a lot in the discretion of the Regulator.

The ability of the Regulator to control the relevant industry lies within the terms and conditions of the licence. These typically will contain clauses limiting the prices that companies can charge for their services (limited to three (3) – four (4) years). If privatization is taken to its limit in the Caribbean i.e. the establishment of utility companies, then challenges can be foreseen with regard to the enforcement of conditions in the licences e.g. where a subsidiary company of a group holds the licence.

Few statutory procedures govern the issue of licences and whilst there are provisions for the publication of notices of an intention to issue licences and for representations to be made, there is no statutory duty to give reasons for the award of licences nor to consult interested parties. There are broad guidelines on the content of the licences itself from which can lead to the Regulator ascribing onto itself either wide discretion or little discretion.

The Act also provides for variation of licenses. In the process of variation there are no statutory requirements for consultation with third parties such as consumer groups.

The licence seeks to set out the ambit of conduct of the regulated entity. It stipulates the conduct which may be engaged in and conduct which is prohibited.

The terms and conditions of the licence are derived from the Regulator acting in pursuance of statutory objectives. The Regulator can therefore enforce the terms and conditions where there is a breach and where such action is taken, the utility has redress in the High Court.

In essence, the licence protects the utility from arbitrary behaviour by the Regulator. The challenge then is for the Regulator to ensure that any action must be directed towards securing the public interest – as defined in the statute -- by the exercise of functions conferred on him by the statute.

LEGAL POSITION OF CONSUMERS

The withdrawal of state ownership from the utilities appears to have strengthened the position of the consumer. Where competition is possible within the utility service, it is promoted and even in a monopoly area such as water, one of the stated responsibilities is the promotion of consumer interest. To this end, consumer representative bodies are established, appointed, funded and staffed by the Regulator under the Act. It has been said that:

"The prime job of the regulatory office is to secure for the customer, a good product, properly delivered at a fair price, with proper redress for inadequate or poor service" and "The best way to please the Regulator is to please the customers".

While the intent is clear in the statute, its achievement appears to be a little difficult. An illustration of this is the fact that consumers are not a homogeneous group. Several different grouping lies within this area e.g. residential and industrial customers. There is also some difficulty in a large group of consumers like the residential or domestic grouping being organized to elect and appoint a representative(s). This leaves open the ability of the consumers to influence regulation by a Regulator who under the existing legislation is not accountable to or appointed by the electorate.

The challenge for the Regulator in this situation, is to strike a balance between the duty of the Regulator to avoid undue preference or discrimination in charges between consumers and ensuring that consumers can afford access to essential water and sewerage services.

JURISDICTION OF PARLIAMENT

On the face of it, Parliament is the ultimate forum for challenging, influencing and control of the Regulator and by extension, the Utility. Annual reports, budgets and

statement of objectives must be laid before Parliament. However, Parliament has no powers over the appointment of the Regulator (or its Commissioners) or over the exercise of their powers.

In our jurisdiction, it may be possible to channel the wishes of Parliament through the relevant Minister who has significant power such as the granting of licences, the appointment of consumer service committees and approval of the cess to be charged by the Regulator.

The power of the consumer at this forum is, therefore, restricted and it would seem that the challenge in this area would be for the Minister to effectively investigate and influence the Regulator to act within the consumer recommendations as articulated by appointed representatives in Parliament. In this way, the Minister can have a significant effect on whether the Regulator's actions are acceptable to the public.

THE JURISDICTION OF THE COURT

Any party aggrieved by a decision of the Regulator or Minister may appeal to a Fair Trading Tribunal. There is little learning emanating from this body which in fact seeks to replicate the Monopolies and Mergers Commission (MMC) in the UK (or its more recent surrogate). In any event, the option of the High Court is available. Any application to the Court to seek redress on a decision made by a public body (such as the Regulator) must be by Judicial Review and for example,

Director General of Water Services ex Parte Lancashier County Council & Ors. RV. EWHC Admin 213 (20th February 1998)

Six (6) applications for Judicial review were made by six (6) different local authorities in relation to certain decisions of the Director General of Water Services. The applicants sought orders of Certiorari to quash the Director's decisions.

In all cases of Judicial review, what is before the Court is the issue of whether or not proper procedures were followed by the public body exercising a public function in reaching a decision. Judicial review does not concern itself with the substance of the decision unless it can be shown that the decision is unreasonable given the procedures that should have been followed and the evidence presented.

Judicial review is the only forum available for ensuring that the right procedures are followed. A decision of the Regulator on a substantive matter can be overturned, but only if the decision is unreasonable. This criteria of reasonableness is a difficult hurdle to cross.

The challenge for the Regulator is to avoid Judicial review of its decision by adhering to transparent, auditable and proper procedures. Openness and transparency in the decision

making process is the key. The establishment and adoption of best practice procedures are essential.

THE REGULATOR'S FORUM

In our jurisdiction, the Public Utilities Commission functioned as a quasi-judicial body with regard to the setting of the rates. The PUC was constituted as a Tribunal and an application proceeded in a manner similar to that of Court. Objections to the application were heard and there was freedom of debate with the Tribunal deciding on the outcome. The process was an open one.

With the establishment of the Regulator however, the forum has changed, the application will now be submitted in the privacy of the Regulator's committee rooms. The objections or otherwise will also be heard in private. The openness of the quasi- judicial process and the freedom of debate will be lost.

The challenge for the Regulator will be to establish confidence in this new forum. Confidence on the part of the utility and confidence on the part of the consumer. Absence of confidence in the decision making process will no doubt lead to judicial review.

LOOKING FORWARD

In this area of privatization and regulation, the Caribbean has chosen to follow what is ostensibly the UK precedent. Fourteen years after privatization and regulation in the UK it is instructive to look at the consequences.

Articles in the Economist of 2003 May 31 and 2003 August 02 indicate that shortly after privatization of the Water Industry in England and Wales, rates went up until the Regulator realized that protecting consumers also meant protecting them from the profit motive. As a result prices were held down and rates went up only 22% since 1980. In Scotland however, where the Utility remained state-owned, rates have gone up 94% in real terms with the heaviest burden falling on business.

The challenge here is for the Regulator, acting within the legal framework to balance the competing issues of consumer interests and financial viability of the utility. Primary focus on consumer interests has necessarily led to cost cutting measures by the Utility companies and to challenging debate in the UK on sale of assets, mutualisation, mergers and ring fencing.

THE CHALLENGES IN SUMMARY

1. Purposeful and objective interpretation of the responsibility of the Regulator.

REFERENCES

1. Review of Utility Regulation – Submission by the Director General of Water Services, 25th September 1997.

2. Water Forum 2002 – Challenges of Water Supply and Sanitation Sector Regulation.

3. OFWAT Responds to Government's Review of Regulation, 11th June 1998.

4. Regulated Industries Commission Act (1998), (Trinidad & Tobago).

5. The Economist, 31st May 2003 & 2nd August 2003.

6. Director General's Address to the Centre for the Study of Regulated Industries, London School of Economics, 13th September 1999.

7. Utility Regulation in Barbados – Key Issues and Challenges OCUR, Kingston, Jamaica, 24th – 26th July 2002.

8. The Development of Regulatory Institutions for Public Utilities in Ghana and Jamaica, Philip D. Osei