



Framework issues: Independence and effectiveness in utility regulation

**Organisation of Caribbean
Utility Regulators
September 2004**

Bob Rowe
Chairman
Montana Public Service Commission
browe@state.mt.us

***A warm greeting from
Montana!***



Come visit us next January



Overview

- Overview of United States “cooperative federalist” approach
- Effective regulation baseline
- Forces encouraging regulatory change
- Joint service regulation as a form of cooperation
- ROC” An example of regional (state-to-state) cooperation on opening local telecoms market to competition

I. U.S. “cooperative federalist” telecoms policy



A Simplified U.S. story

- The **early 1990s**.
- The last major rewrite of national law was 60 years ago, and the biggest companies in the industry have been under the supervision of a judge for 10 years.
- **Bell Operating Companies** subject to anti-trust order, cannot provide in region long-distance without a court waiver, don't want large competitive entry into local, would like reduced retail regulation.
- **AT&T and MCI** interested in quick and low cost access to local market, and slowing BOC entry into long distance.
- **Facilities-based "CLECs"** want interconnection and good performance and prices from the incumbent.



A Simplified U.S. story

- **Rural telecom providers** concerned about universal service.
- **Policy experts**, academics, interested in various kinds of reform.
- **Consumer advocates** want low prices for residential service, affordable service for low income citizens, and service quality protection.
- **States** want to preserve their historically strong role in telecoms policy.
- **Other interests** include broadcasters, cable companies, wireless providers, print publishers, tech and equipment companies, schools and libraries and rural health care advocates, local governments.



1996 US Telecommunications Act goals

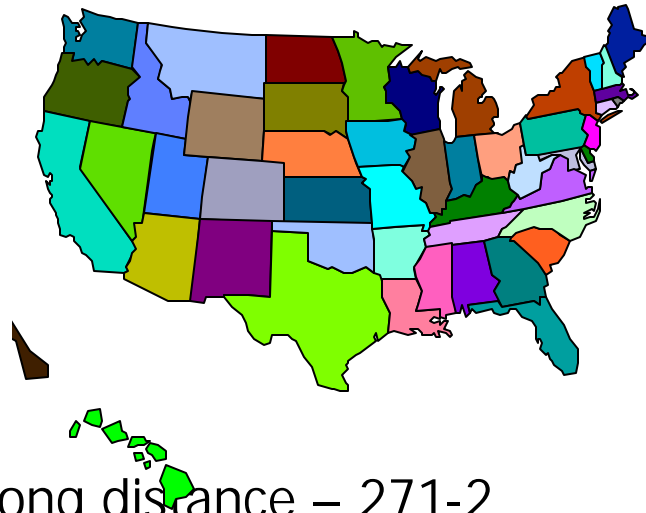
“To provide for a pro-competitive, de-regulatory national policy framework designed to accelerate rapidly private sector deployment of advanced telecommunications and information technologies and services to all Americans by opening all telecommunications markets to competition, and for other purposes.” *Conference Report*

- Open markets
- Support introduction of advanced services
- Maintain universal service - and - *let's not forget* -
- Consumer protection

Telecom Act of 1996

- State commission duties

- Interconnection - Sections 251-2
 - Prices
 - Terms
 - Facilities
 - Enforcement – Sec. 271
- Advanced services Sec. 706
- Promoting competition, local and long distance – 271-2
- Maintaining and advancing universal service – Sec. 254
 - Antithesis of competition, or basis for some competition?
 - ED/CD opportunities and approaches
- Prohibiting barriers to competitive entry – Sec. 253
- Protecting customers of monopoly and competitive services – Sec 253
 - Traditional methods still useful
 - New methods required





Market Structure Effects (telecom)

- Prohibits local exchange monopolies
- Prohibits franchising authorities from restricting cable company provision of telecommunications services
- Differentiates Incumbent Local Exchange Carriers (ILECs) from Competitive Local Exchange Carriers (CLECs)
- Special rules for Regional Bell Operating Companies (RBOCs)
- Special rules for rural LECs
- Creates “information services” category, distinct from telecommunications service



Federalism - US states as vehicles of national policy in 1996 Telecoms Act

- Old – “dual federalism”
 - Section 2(b) reservation of intrastate rate and service authority
 - Jurisdictional separations
- New – “cooperative federalism”
 - 253 preemption of state/local barriers to entry
 - (d)(3) allows consistent state/local policies
 - 2(b) retained
 - States revise statutes to grant authority consistent with Telecom Act
- Not - “preemptive federalism”
 - National government assumes entire policy and implementation responsibility
- Note *USTA v. FCC* (DC Circuit) prohibiting certain “subdelegations” from FCC to state commissions



U S federalism and European “subsidiarity” compared

Deciding the appropriate level for action - EC or member nation.

- Generally, as close to the citizen as possible
- Maastricht Treaty - in areas not within the EU's exclusive competence, will act only if objectives cannot be achieved by Member States, and due to scale or effect of the proposed action, can better be achieved by the Community
- Amsterdam Treaty - Community action should not exceed what is necessary to achieve the objectives (“proportionality principle”)

Old word: Dual federalism.

**“One big company,”
two regulators, and a
“horse high fence.”**

**New world: Broken fences,
lots of “borders” – technology, layers,
jurisdictions, etc., but nobody can find
the property lines.
Many issues happen on the borders.**

**Alternative 1: Preemptive federalism. Efficiency,
consistency, scope of markets require national action.
 (“Withering away of the states.” Strongly top down.**

Alternative 2: Subsidiarity. “Bottoms up.” EU/Articles of confederation.

**Alternative 3: Cooperative federalism. Both federal
and state authorities charged with implementing
federal law within a federal structure. Less top down.**



II. Effective regulation baseline



Baseline requirements

- Sufficient independence from government and regulated sectors
 - “Bounded independence”
- Sufficient resources
 - Legal and political authority
 - Staff and commissioner training
 - Other resources
- Sound processes
 - Predictable
 - Efficient
- Stakeholder and public understanding
- Transparent decisions
- Outcomes
 - Investment and deployment
 - Rates
 - Service quality
 - Service choices
 - Efficiency
 - Equity
 - Procedural outcomes - perceived fairness and effectiveness



Elements of effective regulation

- Transparency of process and reasons for decision
 - Does multi-member board help?
- Neutrality between parties
- Professionalism
 - Understand technology and economics
- Independence from utility management
- Independence from rest of government
 - Employment processes
 - Budgeting
- Judicial review
- Understanding of informed public and decision leaders
- *Can various forms of cooperation help strengthen these elements?*



Barriers to effective regulation

- Limited legal authority
 - Mismatch with markets
 - Access to information
 - Ability to structure remedies
- Limited resources
 - Budgetary
 - Personnel
 - Investigative
 - Technical and economic analysis
- Limited political legitimacy
- *Can various forms of cooperation help address these barriers?*

III. Forces encouraging change in regulatory bodies



The image features a large outdoor sculpture in a snowy mountain setting. The central focus is a tall, weathered tree trunk. A figure of a lumberjack, dressed in a light-colored jacket, blue pants, and a hat, is climbing the trunk. To the right of the tree, a large, brown, textured sculpture of a bear's paw is shown gripping the tree trunk. The background consists of snow-covered mountains under a blue sky with light clouds. In the foreground, there are snow-covered rocks and a black metal railing. The title 'The Regulator's Dilemma' is overlaid in red, italicized text on the right side of the image.

***The
Regulator's
Dilemma***

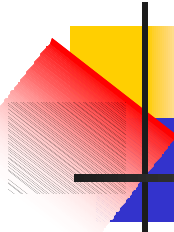


Continuous change in each industry sector.

Continuous change in policy.

Continuous change in regulatory structure.

*Continuous change in demands on
and opportunities for agency staff.*



*How do we know when
it's time to change?*

How do we initiate change?

How do we implement change?

How do we respond to change?



Asymmetries and borders

- **Nation to nation** – treaties, settlements.
- **Federation to member state** – subsidiarity, federalism.
- **State to state** – regional coordination, consultation, shared proceedings, regional authorities (electric RTOs).
- **Nation or state to firm** – law, regulation, or “ether” (implicit consensus)
- **Firm to firm** – business practices, standards, law, regulation.
- **Firm to customer** – consumer protection, privacy.
- *Can various forms of cooperation help address these barriers?*



Asymmetries and borders

- Networks, firms and markets cross international and other boundaries
- Providers offer multiple products, some are substitutable, either now or over time
- How to coordinate policy across jurisdictions, across markets, across products?
- How to share resources, including information and skills?
- Growing interest in regional coordination on regulatory issues

Forces driving change in utility policy/economic regulation.

- 
- **Technology** – more scalable, flexible, and powerful.
 - Affects regulated sectors.
 - Affects regulatory decision-making tools.
 - **Economics**
 - Greater interest in market models.
 - Now “sadder but wiser”?
 - Increasing mismatches between scope of regulatory authority and scope of firm or market.
 - **Law** –
 - Challenges to formalism.
 - New decision making models.

Forces driving change, cont.



■ **Politics**

- **Legislative and interest group pressure.**
- **Federalism – national policy directions affecting state policy.**
- **Internal** – staff and commissioner frustration and turnover, resource constraints.
- **“Regulatory bypass”**
 - Declining consent of the regulated.
 - Declining consent of some (mainly large) consumers.



Changing regulatory roles – regulatory restructuring

- Retargeting policy resources –
 - Less direct retail rate regulation.
 - More wholesale terms and enforcement.
 - Universal service.
 - Technology and ED/CD
 - Consumer protection.
 - Quality of service concerns recurring – but what approaches will work?
 - *Cooperation as a strategy to understand, respond to, and help guide change.*



A regulatory regime includes consideration of

The substance of regulation,

the form of regulation,

*and the forum
in which regulation occurs.*

“The pyramid of policy”

Retail Rates

- *Rate base/Rate of Return
- *AFORs *Price cap

- Level
- Federal
- Regional
- State
- Local

Customer

- Customer education
- Consumer protection
- Retail service quality

Forum

- Legislature
- Agency
- Court
- Standards body
- Private dispute resolution

Universal Service

- Customer support – Low Income
- Loop support – High Cost Fund
- E911 * Schools & libraries * Rural health care

Wholesale

- *Rates *Terms *Numbering
- *Interconnection/unbundling *Structural/non-structural safeguards

- General consumer law*Uniform Commercial Code*General contract law*
- *Anti-trust *Common law

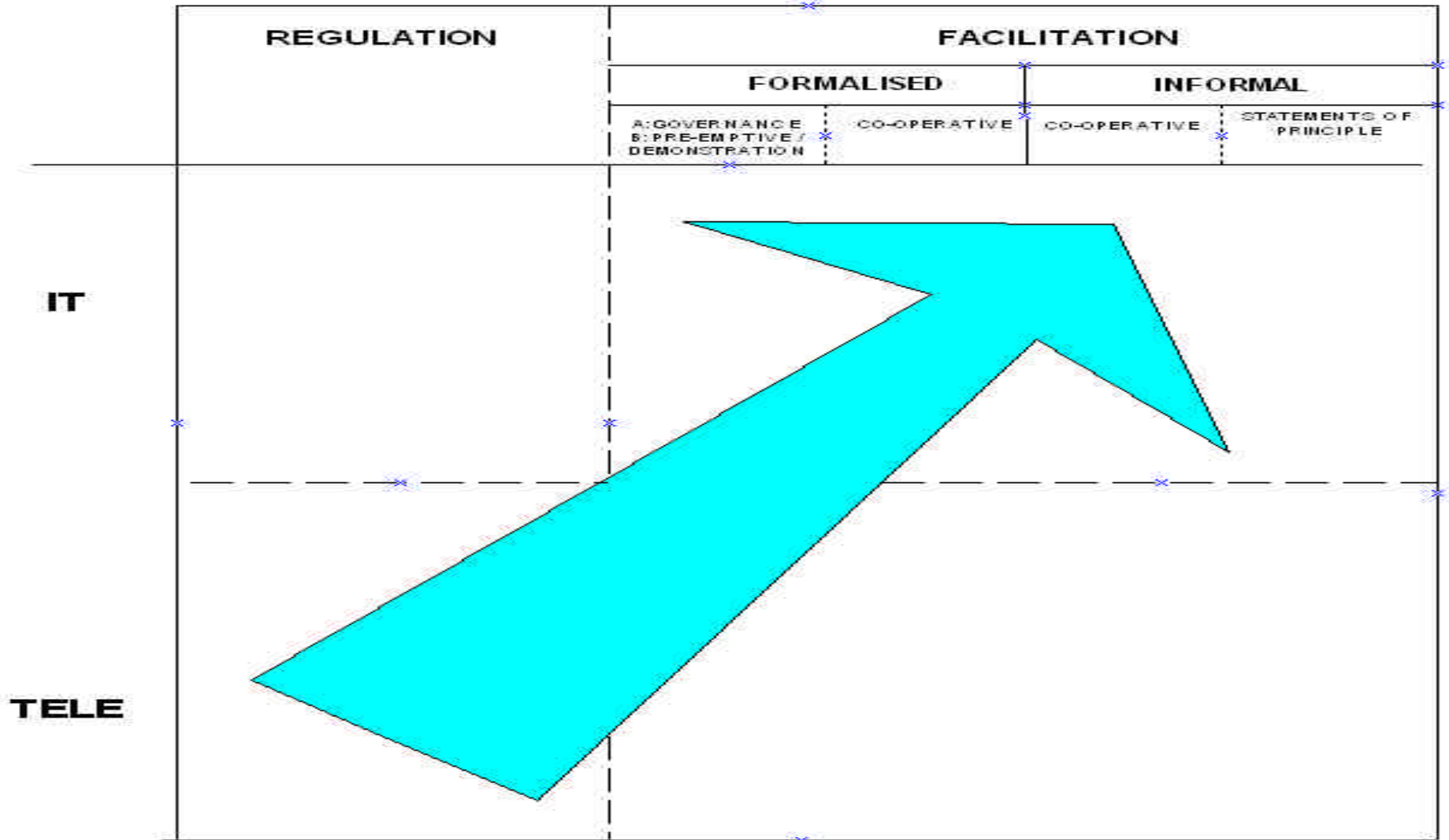
Form

- Contested case
- Tariff
- Rulemaking
- ADR
- Contract
- Implicit consensus

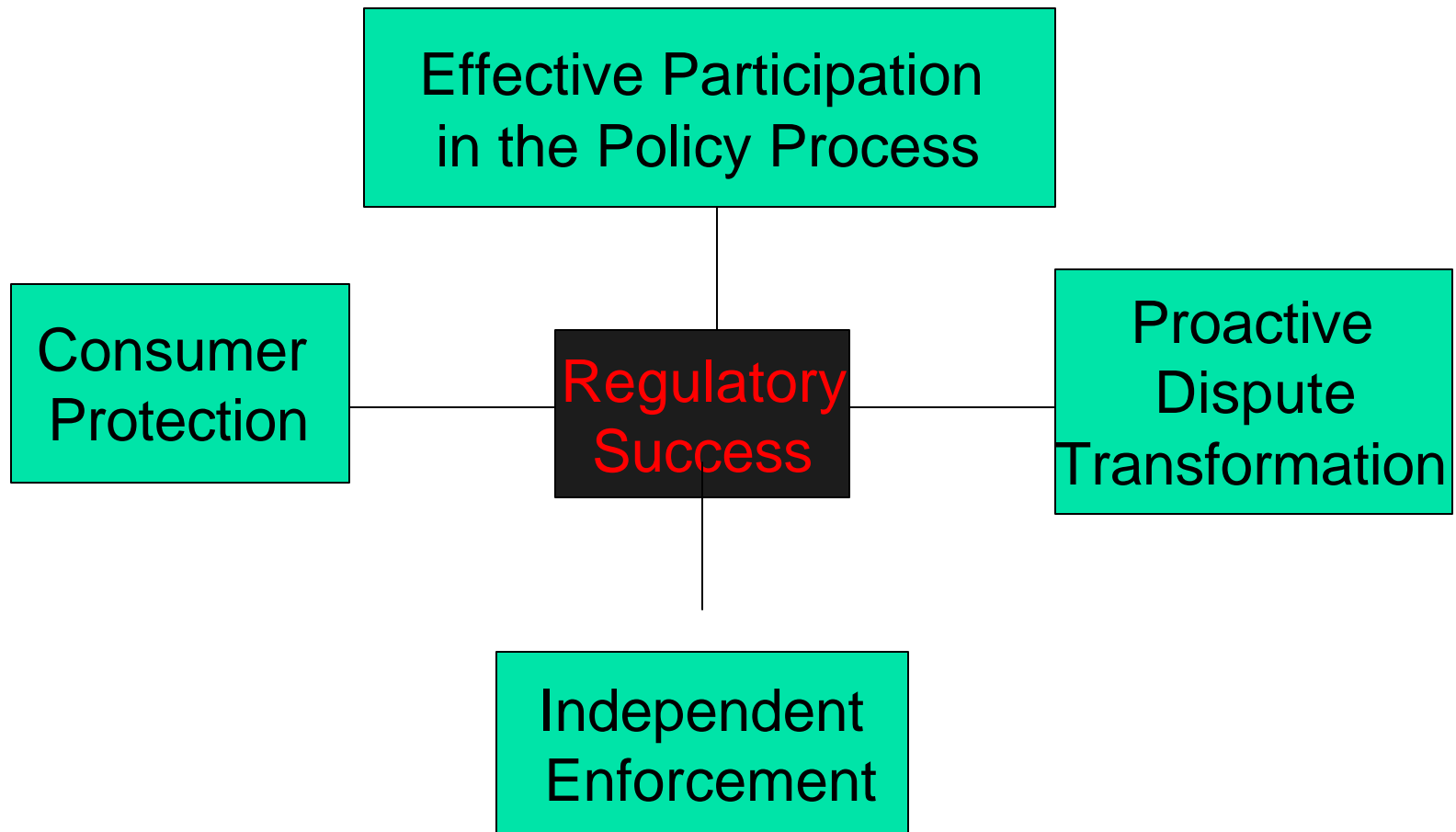
“State of nature” – Hobbes vs. Rousseau

How does the public role change?

HANDS ON → LIGHT TOUCH → HANDS OFF



Required functions in the new environment





Dynamic regulators' characteristics

Outwardly
focused

Constantly
learning

Outcome
oriented

Information-
based

Ecological

Multi-
dimensional

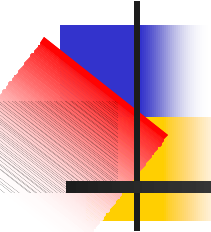
Collaborative

Vision
driven

Reform in a bounded world

- What are the **primary goals** in telecom reform?
- What are the **tools** through which it can be achieved?
- Who are the **stakeholders** and what are their **interests**?
 - Stakeholders currently have a set of “rights” that reform would modify or reallocate
- What other **constraints** are there on an “ideal” outcome?
- In this bounded world, what set of **strategies** are best employed to achieve the public interest?
 - Is there a “**public interest**”? How do we know it?

By standing behind the “veil of ignorance” about our own position, we can better determine what is in the public interest, rather than in our own narrower interest.



If you didn't know what was in your own interest, what would you consider in the public interest?

Paraphrasing John Rawls,
A Theory of Justice



Decision tree for designing a new structure

- What values underlie the work?
- What needs to be done (objectives)?
- How should it be done, most consistently with the underlying values?
- Who should do what needs to be done?
- Feedback - How will we know when we do not need to do something anymore, do less of it, or do it differently?



IV. Joint service regulatory bodies

A form of cooperation across
sectors



Joint service regulatory bodies

- Might combine some or all of telecoms (wireline, wireless, broadcast, cable), electric, natural gas, water, even transportation
- Economies of scale and scope
 - Eliminates duplication
 - Same skills - e.g., legal, accounting, economics, consumer protection.



Joint service regulatory bodies

- Dynamic efficiencies - learning from experience in another industry
- Recognize common evolution toward competition
- Recognizes convergence among industries



Evolution of joint services regulation - external

- Merging bodies
 - Potential and perceived challenges:
 - May be conflicting statutory roles or
 - May conflict with organizational cultures
 - May affect external support and acceptance, or alter balance between regulator and regulated
 - May withdraw resources or focus from one set of tasks
- Adding new functions to existing bodies
 - Challenges: Above, or may lack appropriate tools for new function



Evolution of joint services regulation - external

- Creating new bodies
 - Challenges:
 - May lose experience or legal precedent.
 - May be disruptive.
 - Change may be less than meets the eye (“old wine in new bottles”)



Evolution of joint services regulation - internal by sector

- Combine functions in one entity, but retain separate offices for each sector, e.g., telecoms and electricity
 - Common agency head, different staff
 - Allows specialization
 - Reduces efficiencies
 - Reduces shared learning



Evolution of joint services regulation - internal by function

- Recognizes industry convergence, common trajectory toward competition
- Organize by:
 - Economics - market analysis, competition policy
 - Consumer protection and education
 - Universal service/access
 - Accounting and auditing
 - Engineering – systems issues
 - Complaints and enforcement
- May/Should change as markets, technology, policy evolve



Discussion – What can we do together? Candidates

- Telecom
 - Spectrum
 - International transport – facilities and terms
 - Coordinating with multi-country firms
 - New services and VOIP
 - Reliability
 - Promoting buildout and access



Discussion – What can we do together? Candidates

- Energy
 - Supply adequacy
 - Infrastructure, including audits
 - Reliability
 - Buildout and access



Discussion – What can we do together? Candidates

- General
 - ADR
 - Consumer participation
 - Harmonization
 - “Best practices approaches”



Discussion – What can we do together? Candidates

- The issue of ADR and consumer protection needs to be explored more
- Issue of regulatory enforcement
- Law reform – ideas for improvement
- Comprehensive database of case laws and legislations of various nations
- Need comprehensive database so can benchmark
- Performance indicators
- Regulation for the future – VOIP, changes in technologies?



*Thank you for inviting us to joining you,
and sharing your
experiences and wisdom!*