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**ORGANISATION OF CARIBBEAN
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**The applicability of the Glas
Cymru Model to the reform of
the Water Sector in Trinidad
and Tobago, from
'government to governance.'**

presented by

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Structure of Presentation

- **Introduction.**
- **Examination of the key reasons for the failure of the public sector model as a provider of utility services.**
- **Examination of the key conditions that foster good performance.**
- **Characteristics of the Glas Cymru Model and the ingredients for its success.**
- **Transferability of the model given local conditions.**
- **Conclusion.**

1. Introduction

- Water has two features which distinguish it from other infrastructure sectors:
 - Geography makes its supply limited and location specific.
 - Safe water is crucial to health.
Consequently, it is deemed an essential service and its provision is of great concern to governments. However, this concern has not always been translated into efficient state service.

1. Introduction (continued)

- Given the general failure of the public sector or “clientist” model of service provision many countries sought to reform the sector. This reform generally involved a two-fold strategy: ownership reform and/or the introduction of competition and market reform (including regulatory reform).
- However, while Private Sector Participation (PSP) attracted substantial investment, at the close of the 1990s, only 14.8% of the urban population in Latin America received water from an operator under private sector control.

1. Introduction (continued)

- Given the general reluctance by governments to implement and traditional PSP projects some countries are seeking less radical options. One such alternative is the so-called “mutualisation” or “not for profit model” or “not for dividend model.”
- The Glas Model is one example of such a model.

2. Key Reasons for the Failure of the Public Sector Model

- According to Baietti et al (2006) successful public utilities (in the water sector) are still the exception.
- The performance of the Water and Sewerage Authority (WASA), the service provider in Trinidad and Tobago, follows a similarly dismal pattern (RIC 2005).

2. Key Reasons for the Failure of the Public Sector Model (continued)

- Even the Honourable Prime Minister of Trinidad and Tobago, is quoted in the Guardian Newspapers of Tuesday, July 11, 2006, pg 5, as follows:

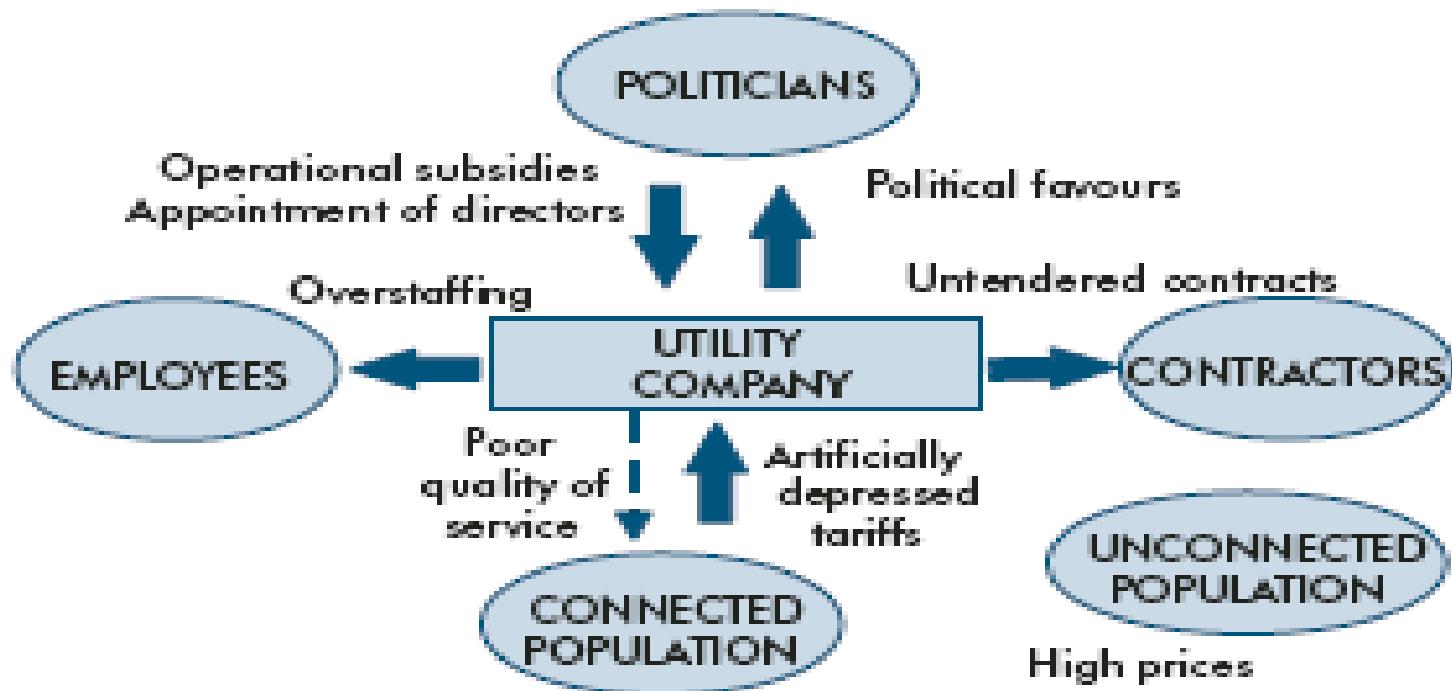
“WASA is a big challenge. It is a \$27 billion headache. WASA like almost all countries in the Caribbean, have the same problem.”

2. Key Reasons for the Failure of the Public Sector Model (continued)

- From the available literature, there seems to be a consensus that the reasons for the poor performance of state owned enterprises are rooted in the failure of the political directorate to maintain an arms length relationship with these enterprises. See Nellis (2006), Irwin and Yamamoto (2004) and Foster (2005).

2. Key Reasons for the Failure of the Public Sector Model (continued)

Clientist Model



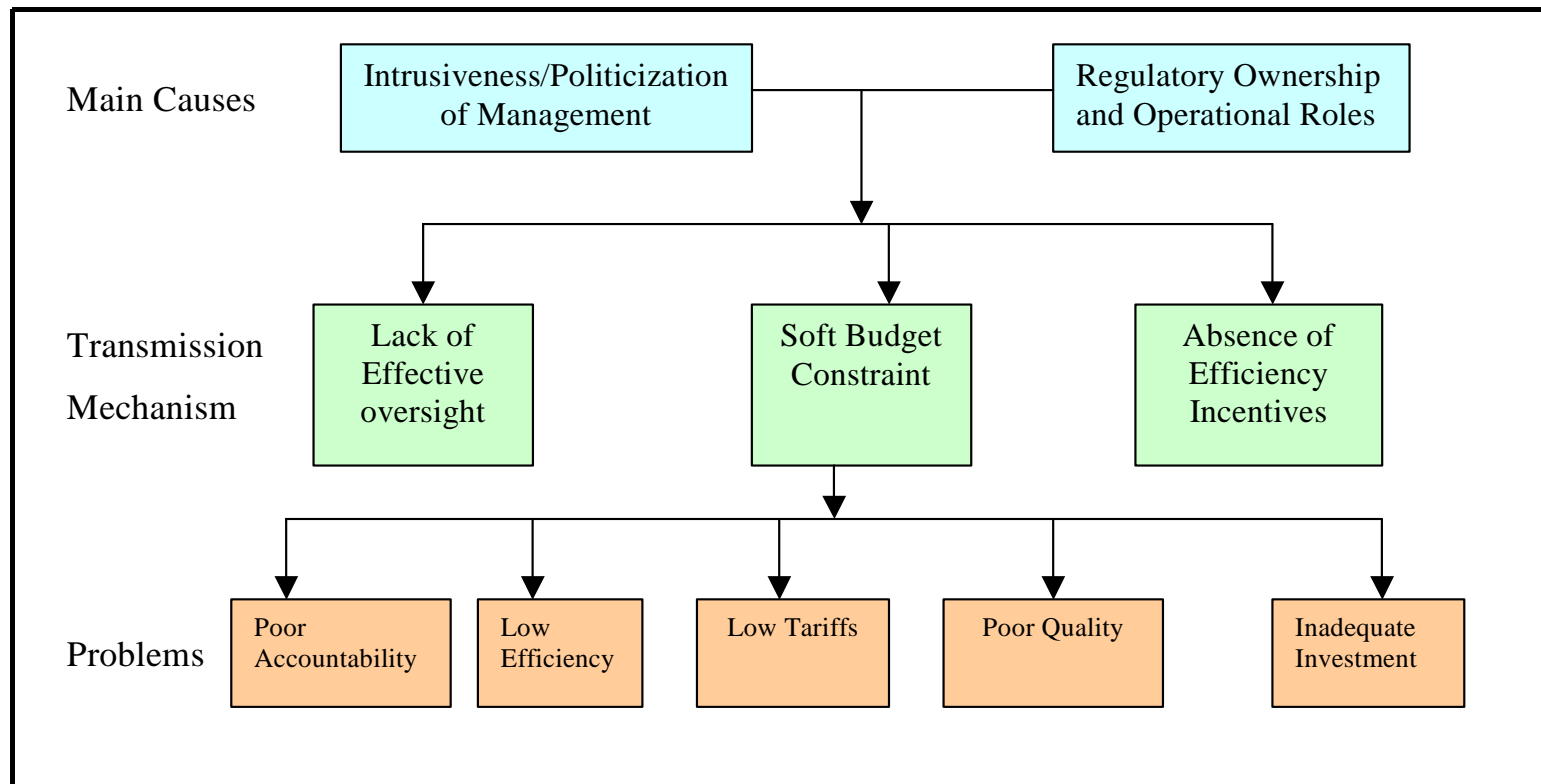
Source: Foster (2005)

2. Key Reasons for the Failure of the Public Sector Model (continued)

- In Trinidad and Tobago, the Public Utilities Sub-Committee of the Vision 2020 Planning Committee, identify government intrusiveness and the governance structure of public ownership as the core reasons for the failure of the local utility sector.

2. Key Reasons for the Failure of the Public Sector Model (continued)

Failure of the Current State-Owned Enterprise Model



Source: Vision 2020 Draft Sub-Committee Report

3. Conditions that Foster Good Performance

- Baietti et al (2006) identify certain key characteristics or conditions that foster good performance, which are common to well run public water utilities. These include:
 - **A high degree of external autonomy.**
 - **A high degree of external accountability.**
 - **High internal accountability.**
 - **Highly market oriented.**
 - **Highly customer oriented.**
 - **Good Corporate Culture.**

3. Conditions that Foster Good Performance (continued)

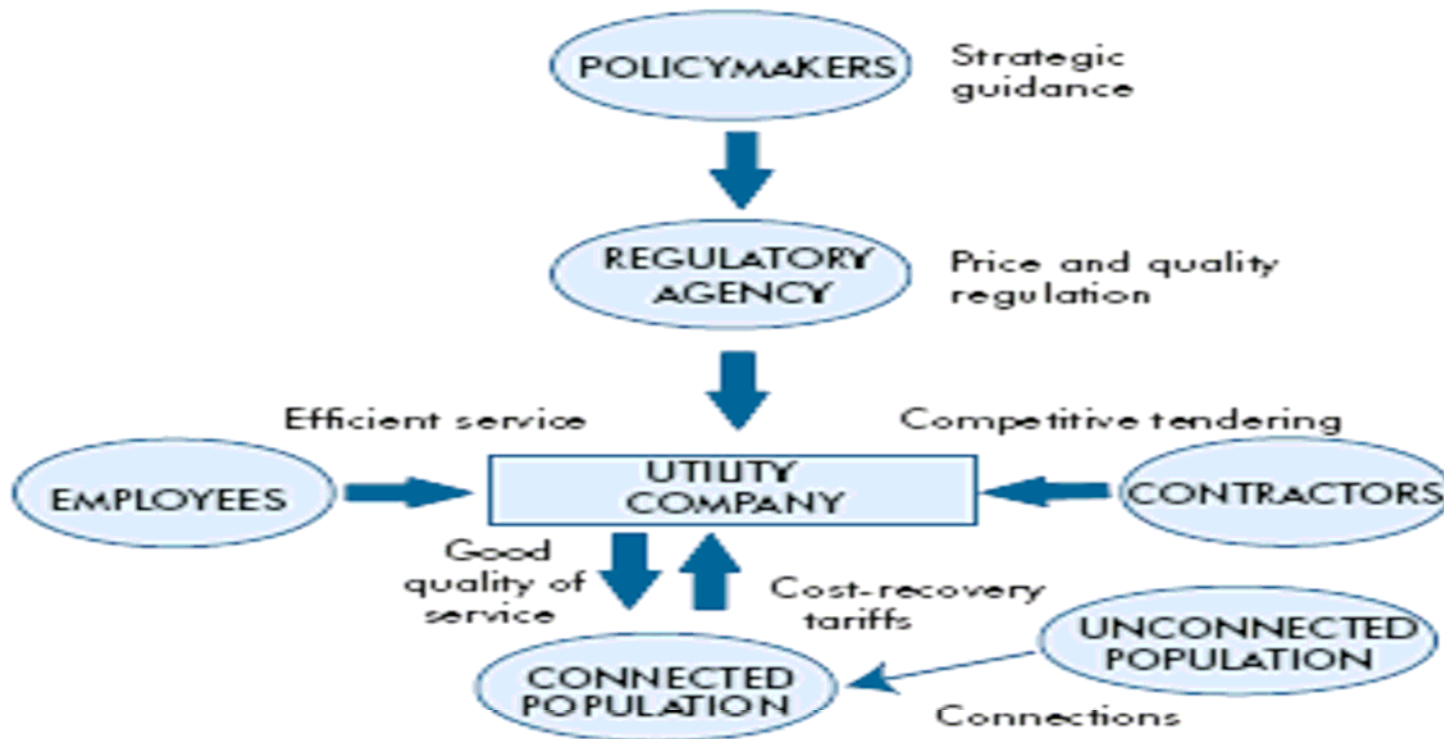
- Irwin and Yamamoto (2004) advocate that improving corporate governance can help the performance of state-owned businesses. However, this alone cannot be expected to solve the problems of government ownership.
- Foster (2005) believes corporatization strengthens the performance publicly owned enterprises, by making it increasingly self-sufficient financially and protecting directors and senior managers from being removed on political grounds. However, she also recognizes that water sector reform needs to include institutional reform.

3. Conditions that Foster Good Performance (continued)

- In order for a poorly performing water utility to become a top performer, it is necessary to undertake:
 - corporate governance reform or “internal governance reform”; and
 - institutional reform or “external governance reform”.

3. Conditions that Foster Good Performance (continued)

Reformed Model



Source: Foster (2005)

4. Characteristics of the Glas Cymru Model and Ingredients for its Success

- In May 2001, Glas Cymru Cyfyngedig, a 'not for profit' company limited by guarantee, acquired Dwr Cymru (Welsh Water) from Western Power Distribution.
- Dwr Cymru is the sixth largest of the ten regulated water and wastewater companies in England and Wales and serves 1.2 million households in Wales and some adjoining parts in England.

4. Characteristics of the Glas Cymru Model and Ingredients for its Success (continued)

Main Characteristics

- Annett et al (2002) cite four main features that distinguish it from other water companies in England and Wales. These include:
 - First, is its commitment to being a single purpose business.

4. Characteristics of the Glas Cymru Model and Ingredients for its Success (continued)

- Second, it out-sources almost all of its operating and investment activities.
- Third, as a 'company limited by guarantee', Glas Cymru has 'members' rather than shareholders. Otherwise it is similar in all respects to any other company incorporated under the UK Companies Act 1985.
- Finally, it is a wholly debt-financed company.

4. Characteristics of the Glas Cymru Model and Ingredients for its Success(continued)

Summary of Glas Cymru Model

Members' Responsibilities – Corporate governance: AGM, Support company objectives, Scrutinise performance.

Board Responsibilities- Set policy, appoint executive, approve budgets, monitor performance, ensure delivery, finance strategy, compliance matters.

Management Responsibilities – Procurement, monitoring day to day performance, intervene in the event of serious underperformance, investment planning, financial management, tariff setting, customer policy, regulatory affairs.

Service provider responsibilities (contractors), day to day operations of assets, service delivery, investment programme, billing, customer contact.

National Government – Sets national policies for sector

Ofwat -Independent regulator sets price limits every five years and has step in rights to protect public interest if licensee becomes insolvent.

Glas Cymru

DWR Cymru /Welsh Water (Licensee)

Asset management/Operations Contractor

Bond Providers – Bond financiers take risk on revenues and costs

AAA rated institution provides credit enhancement for some bond holders.

4. Characteristics of the Glas Cymru Model and Ingredients for its Success (continued)

Success Factors

- A number of factors have contributed to the company's success. These include:
 - Strong incentives to perform optimally.
 - These incentives are provided by the benchmarking regime operated by the economic regulator and the detailed oversight by bondholders.

4. Characteristics of the Glas Cymru Model and Ingredients for its Success (continued)

- Both management and staff are rewarded directly on the basis of the company's operational and financial performance.
- There is a common objective among stakeholders to maintain and improve the credit quality of the company's bonds, because finance costs are minimized it affects all of them positively.

4. Characteristics of the Glas Cymru Model and Ingredients for its Success (continued)

- The company's procurement or out-sourcing strategy is designed to ensure that the potential pitfalls of third party service delivery is avoided. Specifically, Dwr Cymru's procurement strategy does not affect its liability for service provision. It also maintains "no notice step-in rights".
- These conditions were further reinforced by Ofwat, which modified Welsh Water's licence to oblige the company to retain sufficient management resources and systems of planning and control to ensure that its functions are properly carried out.

4. Characteristics of the Glas Cymru Model and Ingredients for its Success (continued)

- In short the ownership model of Glas Cymru as well as the regulatory framework within which the company operates has promoted “good” governance and this has contributed in no small way to the company’s overall success.

5. Transferability of the Model given Local Conditions

- In this Section we will examine the transferability of the Model to Trinidad and Tobago. Key issues here include whether the existing institutional framework can accommodate the model and whether the model needs to be modified given local conditions.

5. Transferability of the Model given Local Conditions

- However, it is important to remember that to be viable, a reform model for the water sector needs to:
 - address the key problems of the sector; and
 - be palatable to the major stakeholders i.e government, unions and the consumers.
- Additionally, government commitment is critical to the successful implementation of any reform programme.

5. Transferability of the Model given Local Conditions (continued)

- Core tenets of the model:
 - An asset holding entity whose sole purpose is to raise finance for the operating company.
 - A completely autonomous operating company.
 - An independent regulator utilising an incentive regulatory framework.

5. Transferability of the Model given Local Conditions (continued)

- Transferability will impact on the following aspects of the institutional framework:
 - The ownership and governance of the company/companies responsible for the provision of water and sewerage services;
 - The legal and regulatory framework applicable to those companies; and
 - The relationship between the regulated company/companies and those responsible for implementing the agreed investment programme.

5. Transferability of the Model given Local Conditions (continued)

- Legal Framework and Ownership issues
 - Like the UK, the Trinidad and Tobago Companies Act, Chapter 88:01, Section 307 allows for the creation of non-profit companies. Consequently, the asset holding company can be a company limited by guarantee i.e. “not for profit”.

Legal Framework and Ownership issues

- Further Section 308 states that before articles would be accepted for filing by the Company Registrar, the business of a non-profit Company must be restricted to one that is patriotic.... or the promotion of some other useful object. The Articles of the “asset company” can therefore be restricted to holding the assets of the current WASA on behalf of the people of Trinidad and Tobago and providing funding to the new “operating company”. Additionally, it can specify that any benefit it derives from such holding must be returned to customers of the operating company or used to fund investment.

Legal Framework and Ownership issues

- This will in turn help insulate the operating company from any undue influence from the asset holding company.

5. Transferability of the Model given Local Conditions (continued)

- An important matter that would also need to be resolved is the membership issue of the “asset company”.
- Keeping in mind that you what to have government support for the model it may be prudent for the “asset company” to be owned by the government.
- Section 310 of the Companies Act of Trinidad and Tobago provides for no fewer than three members. Consequently, membership could be comprised of a number of key ministers for example the Ministers of Finance, Public Utilities and Energy or Minister of Trade respectively.

5. Transferability of the Model given Local Conditions (continued)

- The operating company would be a wholly owned subsidiary of the asset company, incorporated as limited liability company under the Companies Act.

5. Transferability of the Model given Local Conditions (continued)

- Another major concern is the composition of the boards of both the asset holding and operating companies. The boards must be of high calibre and be held accountable for the efficient conduct of the business. One way to ensure this would be to allow for the removal of board members in the event of poor performance.

5. Transferability of the Model given Local Conditions (continued)

- Another critical area is to ensure that directors and managers face appropriate incentives for ensuring good performance. It is important, that there be an incentive scheme for managers that will attract and retain a high calibre management team and incentivise them to deliver efficiency in business operations.

5. Transferability of the Model given Local Conditions (continued)

- It has already been noted that there substantial out-sourcing in the original model. In this regard other water companies play an instrumental role in its asset management programme and general operations of the operating company.
- In Trinidad and Tobago there is no equivalent domestic pool of specialist firms. Thus such an approach may not be feasible. However, the possibility exists of outsourcing asset management and network operations to an experienced private sector company (possibly through a foreign and local partnership).

5. Transferability of the Model given Local Conditions (continued)

- Finally, the Water and Sewerage Authority of Trinidad and Tobago is a statutory authority, created by the WASA Act, No. 16 of 1965. While the Act makes provision for the establishment of the Authority it also includes regulatory and other provisions.
- In order to establish a new company the Act would need to be repealed and the provisions unrelated to the establishment and functioning of the Authority reviewed to see whether these responsibilities would better be served by another body or contained in a water sector act similar to the **UK Water Act of 1991**.

5. Transferability of the Model given Local Conditions (continued)

- Regulatory Framework.
 - The incentive framework operating in the UK has contributed substantially to the success of the Water and Wastewater sectors in that country. In Trinidad and Tobago, the RIC is responsible for the economic regulation of the water and wastewater sectors. However, while the UK system utilizes relies heavily on benchmarking, the RIC has no domestic pool of companies on which to draw.

5. Transferability of the Model given Local Conditions (continued)

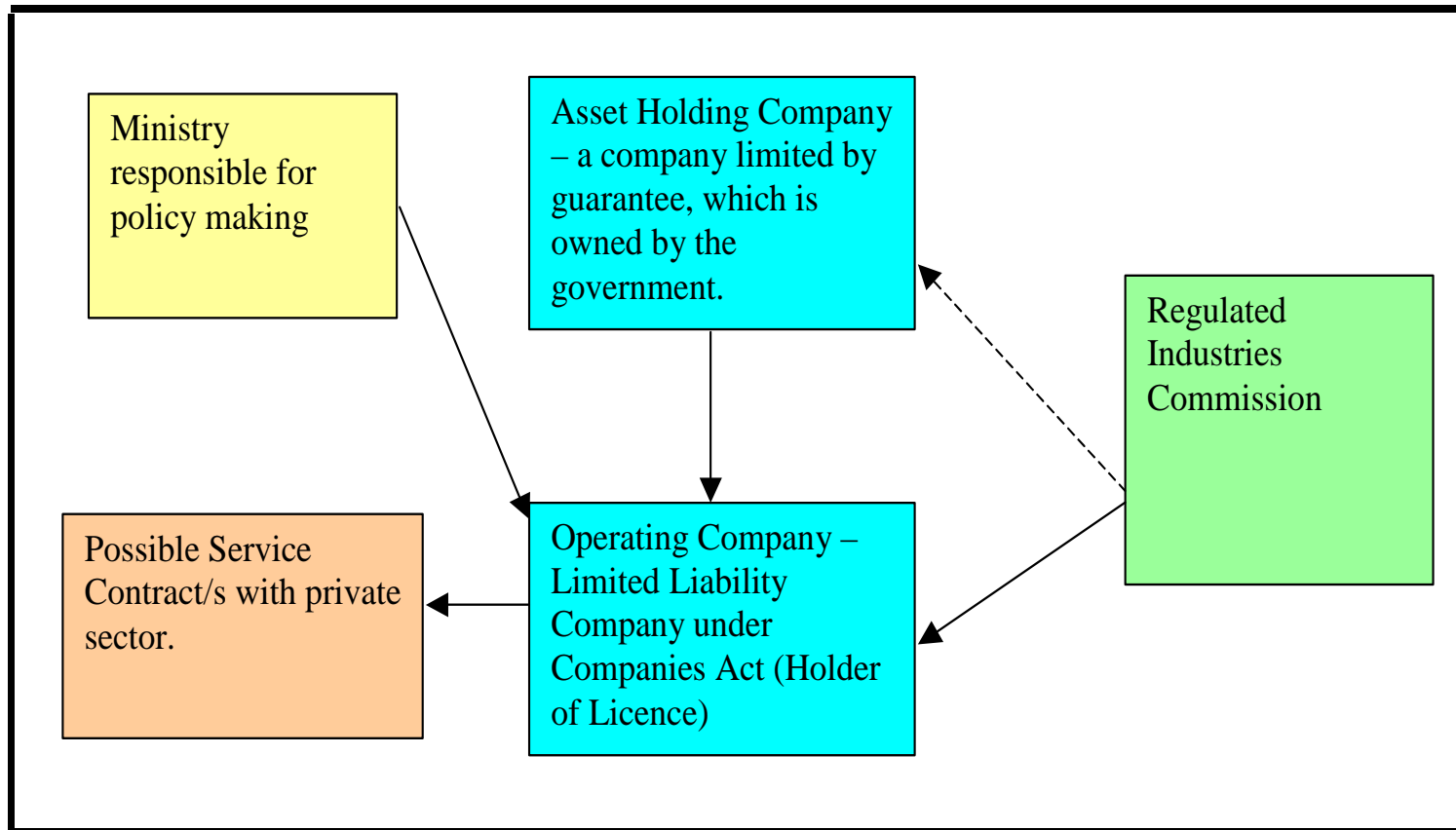
Fortunately, this does not preclude the RIC from utilizing performance indicators and other best practice indicators to inform its decisions. In its recently concluded price review of prices for the transmission and distribution electricity service provider, the RIC was able to combine various techniques to allow it to forecast efficient costs.

5. Transferability of the Model given Local Conditions (continued)

- Additionally, the UK has had a longer history of independent regulation. In essence external control of Glas is exercised by the regulator through its role as the licensing authority by imposing and enforcing licence conditions. This aspect of the model may prove to be challenging in Trinidad and Tobago as the RIC does not have concomitant powers but only makes recommendations and oversees its implementation.

5. Transferability of the Model given Local Conditions (continued)

Proposed Reform Model



6. Conclusion

- A key characteristic of any well performing utility is good governance structures. However, government ownership does not usually promote good governance. Under such ownership it is necessary to incorporate a number of best practice criteria, which will promote accountability and autonomy.

6. Conclusion

- The model proposed in this paper can improve the performance of the sector and is likely to be a more acceptable to both government and the public because:
 - The national patrimony is not being sold to the private sector.
 - Unlike in the conventional concession model, the private sector not being asked to provide capital funding and it is therefore likely to generate more interest, as there is less risk involved.

Conclusion

- The proposed model does not outsource as extensively as the original model and therefore it is more likely to be acceptable to workers.
- The asset company is a not for profit entity, any out-performance will be returned to the rate-paying public through rebates. Thus, there may be a greater willingness for customers to pay increased tariffs, as any profits will not be expropriated.

THE END