CREATING REGULATORS IS NOT THE END KEY IS REGULATORY PROCESS

- A Research Report

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CUTS International

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Acronyms

BoZ	Bank of Zambia
BRTI	*Badan Regulasi Telekomunikasi Indonesia*
CAZ	Communications Authority of Zambia
CBK	Central Bank of Kenya
CERC	Central Electricity Regulatory Commission (India)
CMA	Capital Market Authority (Kenya)
CPV	Communist Party of Vietnam
DGPT	Directorate General of Posts & Telecommunications (Indonesia)
DOT	Department of Telecom (India)
EAC	Electricity Authority of Cambodia
ERAV	Electricity Regulatory Authority of Vietnam
ERB	Electricity Regulatory Board (Kenya); Energy Regulation Board (Zambia)
FSB	Financial Services Board (South Africa)
IBA	Independent Broadcasting Authority (South Africa)
ICASA	Independent Communications Authority of South Africa
IPP	Independent Power Producer
IRDA	Insurance Regulatory and Development Authority (India)
IRSA	Insurance and Reinsurance Supervisory Authority (Vietnam)
ITU	International Telecommunications Union
JWSRB	Jakarta Water Supply Regulatory Body (Indonesia)
KCAA	Kenya Civil Aviation Authority
KMA	Kenya Maritime Authority
KPPU	*Komisi Pengawas Persaingan Usaha* (Indonesia)
MIME	Ministry of Industry, Mines and Energy (Cambodia)
MPC	Monopolies and Prices Commission (Kenya)
MPT	Ministry of Post and Telematics (Vietnam)
MPTC	Ministry of Post and Telecommunication (Cambodia)
NBC	National Bank of Cambodia
NER	National Electricity Regulator (South Africa)
NERSA	National Energy Regulator of South Africa
NWASCO	National Water Supply and Sanitation Council (Zambia)
PFRDA	Pension Fund Regulatory and Development Authority (India)
PIA	Pensions and Insurance Authority (Zambia)
PIP	*Pengawas Independen Pelaksanaan* (Indonesia)
PNGRB	Petroleum & Natural Gas Regulatory Board (India)
QOS	Quality of Service
RBA	Retirement Benefits Authority (Kenya)

RBI	Reserve Bank of India
SAP	Structural Adjustment Programme
SARB	South African Reserve Bank
SATRA	South African Telecommunications Regulatory Authority
SBV	State Bank of Vietnam
SEB	State Electricity Board (India)
SEBI	Securities and Exchange Board of India
SEC	Securities and Exchange Commission (Zambia)
SERC	State Electricity Regulatory Commission (India)
SNO	Second National Operator
SOE	State-owned Enterprise
TAMP	Tariff Authority for Major Ports (India)
TDSAT	Telecom Disputes Settlement and Appellate Tribunal (India)
TKL	Telkom Kenya Ltd.
TLB	Transport Licensing Board (Kenya)
TRAI	Telecom Regulatory Authority of India
VNPT	Vietnam Post and Telecommunications
WSRB	Water Services Regulatory Board (Kenya)
WSS	Water Supply and Sanitation
ZAMTEL	Zambia Telecommunications Co.
ZCC	Zambia Competition Commission
ZPA	Zambia Privatisation Agency

Chapter I
Regulatory Environment in Developing Countries

1. Background

In the past most developing countries were characterised by significant government involvement in their economies marked by dominance of large state-owned enterprises. Economic liberalisation process started in several of these countries during 1980s and 1990s and most of them adopted policies of deregulation, privatisation and trade liberalisation.

The thrust of economic reforms has been to allow for more competition. The underlying rationale is that competitive markets ensure efficiency resulting in best possible choice of quality, lowest prices and adequate supplies to consumers. This outcome emerges because of the following three conditions:

- *Competition*: there are a large number of producers supplying same product, or close substitutes, and no single producer dominates the market place
- *Full information*: all consumers are fully informed about the options market offers them
- *Low switching costs*: the costs a consumer faces in switching from one option to another is not high enough to deter this switch

Anyhow, the real world contains a number of instances where markets do not satisfy any one or more of these conditions, and in such situations, competitive markets may not exist or yield desirable outcomes. This includes situations where:

1. Market players adopt unfair means to restrict competition and hurt other players and consumers
2. Markets fail due to externalities, imperfect or asymmetric information, and economies of scale and scope
3. Government policy that paved the way for greater market-orientation in the first place, might itself have elements that distort functioning of markets

The first two factors require some form of intervention in the market process. The third factor requires fine-tuning of government policy and its implementation to facilitate working of markets.

There is now a growing realisation that the shift towards market-oriented economy does not mean 'invisible hand' will work to allocate resources efficiently and produce competitive outcomes, as potential benefits are often thwarted by market-distortionary practices[1]. Distortions to the market process arise, when, firms, while competing with one another, adopt restrictive or unfair practices (factor one above). This relates to fixing prices with rivals, setting price which is lower than cost in order to throw out competitors from the market, taking advantage of a monopoly position and charging unreasonable price, refusal to buy or supply, and the like. In view of this, Competition Law is enacted to check such behaviour of market players. It lays down legal principles and institutions that govern behaviour of firms in markets including restrictive trade practices, mergers, provisions to deal with abuse of dominance, cartels etc.

[1] Brusick, P. et al. (eds.) (2004) Competition, Competitiveness and Development: Lessons from Developing Countries, UNCTAD, Geneva

Where, however, competitive markets may not exist or yield desired results – generally because the conditions for a natural monopoly apply – a case is made for some form of intervention to control price and quality of products and services[2]. Therefore, in such situations, regulation emerges to simulate competitive outcomes.

The rationale for regulation differs for financial markets from that of utilities (e.g. electricity, telecommunications, water) and also for transportation. Regulation of utilities is mainly justified because of natural monopoly or locational monopoly for transportation (airports and seaport). In case of financial markets, regulation is required due to information asymmetry, whilst in the case of public passenger transport the rationale for regulation is to prevent destructive competition.

An important factor that calls for regulatory intervention in infrastructure sectors that are opened up for other players is 'access to essential facilities'. Another reason for regulatory intervention is that while the market can be expected to bring about equilibrium between "demand" and "supply", it will not be able to ensure a balance between "need" and "supply". From a social point of view, it is desirable that all consumers, regardless of their income status, have access to certain services, for example, electricity. This requires regulatory intervention to promote equitable outcomes.

What emerges is that appropriate competition principles and rules (competition law and sector regulatory laws) need to be framed and implemented, and supporting institutional infrastructure put in place for a market-oriented economy to deliver goods.

Many developing economies have adopted competition laws as a follow up to their market oriented economic reforms. Additionally, most of these countries have adopted regulatory laws in several sectors as they were opened up for private players. This upsurge in interest in competition and regulatory laws in developing economies reflects substantial changes that have been taking place in their political and economic environment.

Be that as it may, mere adoption of a competition law and a regulatory law is a necessary but not a sufficient condition for it to be part of market reform agenda. Implementation is equally important. Developing countries pose unique challenges for competition and regulatory law enforcement. Their low level of economic development, which is often accompanied by institutional design problems and complex government regulation and bureaucracy, creates real-world challenges that have to be recognised before successful implementation of competition and regulatory regimes[3]. Instead, developing country governments have established or are establishing regulatory agencies for utilities, inspired mostly by industrial countries model rather than their peculiar national context. Arguably, however, the performance of new regulatory state remains under-researched, especially in the context of developing countries[4].

Given this paucity of research, CUTS Centre for Competition, Investment & Economic Regulation, a programme centre of CUTS International has undertaken the present research work to study sector regulatory environment in developing countries in Asia (India, Indonesia,

[2] Anant, TCA and S. Sundar, "Interface Between Regulation and Competition Law", in Pradeep S. Mehta (ed) (2005), Towards a Functional Competition Policy for India, CUTS and Academic Foundation, New Delhi

[3] Gal, Michal S., The Ecology of Antitrust: Preconditions for Competition Law Enforcement in Developing Countries in P. Brusick et al. (eds.) (2004) Competition, Competitiveness and Development: Lessons from Developing Countries.

[4] David Parker and Colin Kirkpatrick, Researching economic regulation in developing countries: developing a methodology for critical analysis, Paper No. 34, December 2002

Vietnam and Cambodia) and Africa (South Africa, Kenya and Zambia). The countries selected have undergone (are undergoing) transition from a regime characterised by public sector dominance in different segments of the economy to one marked by privatisation and liberalisation, and setting up of independent sector regulators. While in some countries in certain sectors, government continues to perform regulatory function, in others an independent regulator has been set up to perform regulatory functions. Further, in some countries there is presence of both forms of regulatory approaches. Thus, the countries selected offer an opportunity to study a variety of experiences in economic regulation and would help in drawing relevant learnings for regulatory institution design in developing countries.

There are many possible approaches to the comparison of regulatory systems. In this study, we explore the regulatory institutional framework that has been adopted in project developing countries. The focus is on following issues:

- Identify sectors where regulatory functions are performed either by the Government or a specialised agency
- Analyse how transition from a regime characterised by dominance of public sector to one marked by privatisation is being/has been managed
- Study regulatory environment with regard to institutional and governance aspects, such as regulatory objectives, mandate, independence, accountability, interface with other agencies, decision making process, capacity, selection and staffing.

The study covers sectors where regulatory intervention is typically required i.e. telecommunications, energy (electricity, oil & gas), transport (seaports, civil aviation, railways), water supply, and financial sector (banking).

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2. Political-economic Environment

The research study comprises countries that vary in size (in terms of their national income), are at various stages of development and have emerged from different political-economy situation.

At one end is India, which is the largest economy in terms of Purchasing Power Parity, among countries selected for this study, followed by South Africa, Indonesia, and Vietnam, all highly performing economies in recent years. At the other end are Kenya, Cambodia and Zambia. While Kenya is catching up in terms of its economic performance, Cambodia is still recovering from civil war, and Zambia's economy continues to be in poor state.

India and South Africa are considered economic powerhouses in Asia and Africa, and Cambodia and Zambia are amongst world's poorest nations. Kenya is considered most developed economy in East Africa and a regional hub for trade and finance. Vietnam has achieved remarkable results in macroeconomic development and is among the fastest growing economies in world. Indonesia is one of Southeast Asia's successful highly performing and newly industrialising economies.

Some of these countries have suffered economic and political crisis in the past and are in the process of recovery. Vietnam has had to recover from the ravages of war, 30 years ago and Asian financial crisis of 1997. Indonesia experienced considerable trouble after Asian financial crisis and political turmoil in 1998. The country is now emerging from its political and economic crisis and has undergone tremendous changes in its structural and political reforms since 2001.

Cambodia had been disrupted by civil war, and the political crisis in 1997 combined with the Asian financial crisis led to a sharp economic slowdown. Since 1998, Cambodia has initiated fundamental reforms and significant progress has been made in promoting economic recovery.

Economic reform is an evolving process and needs commitment from those who are at the helm of affairs. Herein lies the role played by political governance system of a country. In this context it is observed that except Vietnam, which is a one-party communist state, all other project countries have a multi-party democratic set-up. This political governance system has implications for the way reforms are adopted and implemented in these countries. Thus, for instance, in case of Vietnam, the Communist Party of Vietnam (CPV) has committed to gradually liberalising the economy. Accordingly, reforms have been prudently implemented with the aim to allow for long-term, sustainable growth. In case of other countries, any major economic reform requires a consensus among major political outfits to ensure effective implementation. This factor is particularly important in the context of regulatory reforms that leads to a change in the economic governance system of a country and covers issues that are politically sensitive.

In brief, political-economy scenario in countries under study has now stabilised. By adopting policies of economic reforms and liberalisation, they are looking forward to moving along a high growth path.

Table 1.1 Key Economic Profiles of Project Countries

	GDP (PPP) (USD billion)[1]	Per-capita income (USD) (at PPP)[2]	Contribution of Sectors to GDP			Kea Feature of country's economy
			Agriculture	Industry	Services	
Kenya	48.33	1,445	16.2%	18.8%	65%[3]	• Regional hub for trade & finance in East Africa • Economy on recovery path
Zambia	10.79	931	22%	29%	49%[4]	• Among world's poorest nations • Depends on external grants
South Africa	570.19	12,160	2.5%	30.3%	67.2%[5]	• Focus on growth with equity • Economic powerhouse in sub-Saharan Africa
India	3,633.44	3,344	18.6%	27.6%	53.8%[6]	• 4th largest economy in terms of PPP • Among fastest growing major economy
Indonesia	977.42	4,458	13.4%	45.8%	40.8%[7]	• Highly performing, newly industrialising economy • Emerging from political and economic crisis
Vietnam	251.61	3,025	20.9%	41%	38.1%[8]	• Among world's fastest growing economy • Industrialising economy, recovered from ravages of war
Cambodia	34.67	2,399	35%	30%	35%[9]	• Among world's poorest nations • Recovering from civil war

1) http://en.wikipedia.org/wiki/List_of_countries_by_GDP_%28PPP%29 (estimates are as of 2005)

2) http://en.wikipedia.org/wiki/List_of_countries_by_GDP_%28PPP%29_per_capita (estimates are as of 2005)
Primary Source for 1) & 2): International Monetary Fund, World Economic Outlook Database, April 2006
3) CIA World Factbook (estimates are as of 2004)
4) CIA World Factbook (estimates are as of 2005)
5) CIA World Factbook (estimates are as of 2005)
6) CIA World Factbook (estimates are as of 2005)
7) CIA World Factbook (estimates are as of 2005)
8) CIA World Factbook (estimates are as of 2005)
9) CIA World Factbook (estimates are as of 2004)

3. Evolution of Economic Policy Regime

The countries selected for study are at different stages of development and are adjusting their policies to the varied market structures that have evolved as a consequence of their history. Cambodia and Vietnam started with complete state control of their economies, while others adopted a State led development. However, all of them have initiated economic reforms during the past decade with the objective of liberalising economic decision-making, encouraging private participation and reducing tariff and non-tariff barriers and quantitative restrictions on imports.

Reasons for Dominance by SOE

All project countries tried to accelerate economic development through industrialisation. To achieve this they followed a policy of import substitution supported by controls on trade and industry in the private sector. In all project countries there was a heavy reliance on state-owned-enterprises (SOEs) to meet the needs of the economy. Most SOEs were monopolies and this status was supported by governments in the hope that they would benefit from economies of scale. However, SOEs were found, on average, to be inefficient and loss making, which put a severe strain on governments' budgets to provide subsidies and additional resources for investment.

Imperatives for Reform

Most of the countries got on the path of economic reforms following economic crises. India (1991), Kenya (1992), Zambia (1991) initiated reforms around the same time following macro-economic disturbances characterised by huge external debt, mounting government deficits, and poor performance of SOEs that imposed further strain on government budget. Vietnam (1986), Cambodia (1987) and Indonesia (1988) undertook reform measures in late 1980s to move towards market-oriented economy and pushed up their reform efforts following the Asian financial crisis in 1997. South Africa adopted the Growth, Employment and Redistribution strategy in 1996 following the end of Apartheid regime and the adoption of a new constitution. The country was characterised by poor performance of SOEs and low penetration rate for utilities, which was also racially skewed.

While India, South Africa, and Vietnam, initiated reforms autonomously, economic reforms in Zambia, Kenya, Indonesia, and Cambodia were initiated under pressure from international donors as part of Structural Adjustment Programs.

Key elements of reforms

Economic reforms undertaken by project countries included measures relating to trade liberalisation, opening up of economy, promoting FDI, and facilitating private sector participation. There has however been a difference in the nature of reforms undertaken with respect to state owned enterprises. The poor performance of SOEs and consequent pressure on budgets forced governments to reduce support to SOEs and move towards either privatising them or restructuring them, and this is where the difference lies.

Most countries began with a program of privatisation of SOEs; some autonomously and some as part of conditionality required by donor community. However, the experience with privatisation has brought about significant changes in approaches followed in some countries. While Kenya and Cambodia continue to move along the path of privatising their SOEs; in South Africa, India, Zambia, and Indonesia the process has slowed down or abandoned due to protests from various stakeholders. For instance, in Zambia, which passed a privatisation act and established a privatisation agency, the process has virtually stopped due to large-scale labour retrenchment following privatisation. South Africa, India and Vietnam are putting more emphasis on restructuring of SOEs (i.e. corporatisation and commercialization) rather than their privatisation. In Indonesia, privatisation has involved greater involvement of private sector in economic activities that were earlier dominated by SOEs, without much state enterprise divestment.

Effects of Economic Reforms

In spite of the slow down of the process of privatisation, effect of other reform measures has led to a reduction of domestic controls and liberalisation of trade. All countries, including Zambia, which is grappling with poverty reduction strategies, are now experiencing a steady improvement in their economic growth in recent years (see Chart 1).

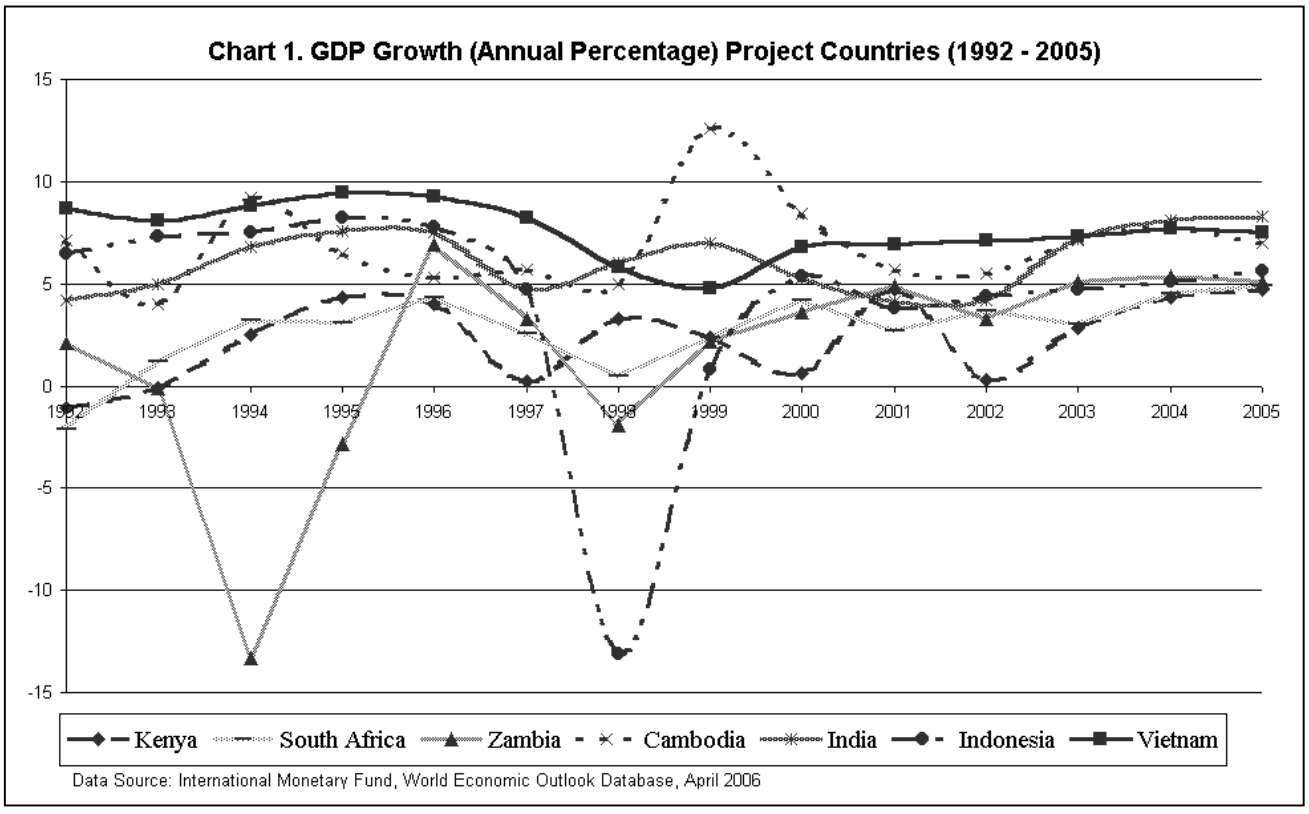


Table 1.2 Evolution of Economic Policy Regime in Project Countries

	Feature of earlier economic policy regime	Year when economic reforms initiated and trigger	Feature of new economic policy since economic reforms
Kenya	• Centralised economic planning • Import substitution strategy • Reliance on SOEs, monopoly status in several activities	• 1992: economic reforms initiated in response to internal pressure (mounting government deficits, debt ridden SOEs providing poor services) and as part of Structural Adjustment Programme supported by donor agencies	• Market-oriented economy • Liberalisation of economy, privatisation of SOEs, de-linking government from market, tariff reduction and removal of trade barriers • Privatisation bill to provide legal framework for privatisation program
Zambia	• Import substitution • Dominance of SOEs • National development planning	• 1991: economic liberalisation and SAP adopted following continued macro-economic disturbances (huge external debt, 3-digit inflation, mounting government deficits); SAP supported by IMF and World Bank	• Transforming into a market driven economy • Removal of exchange controls, increasing participation of private sector, privatisation of SOEs, streamlining government's role • Privatisation Act enacted, Zambia Privatisation Agency established in 1992
South Africa	• Import substituting industrialisation • Dominance of SOEs • Extensive government intervention in economy	• 1996: Growth, Employment and Redistribution strategy introduced following poor performance of SOEs, low penetration rate for utilities, which were racially-skewed as well	• Mixed economy with SOEs given a role to ensure fairness & equity • Trade liberalisation, tariff reduction, promoting private sector participation • Emphasis on restructuring of SOEs than on privatisation
India	• Centrally planned economic development model • Dominance of SOEs, restrictions on private sector • Government intervention through licensing and quota • Inward-looking import substituting growth strategy	• 1991: economic reforms following macro-economic disturbances (BoP crisis, mounting government deficits, low competitiveness of Indian industry)	• Outward-looking export-led growth strategy • Trade liberalisation, promoting FDI, facilitating private sector participation, government's role as facilitator rather than controller • Initially privatisation of SOEs, now focusing on their restructuring
Indonesia	• Concentration of wealth amongst certain families • Import substitution strategy • Structural weaknesses: weak legal system, non-tariff barriers, rent seeking by SOEs, export restrictions, barriers to domestic trade	• 1988: regulatory obstacles to external and financial sectors eliminated; private investment encouraged, move towards market-oriented economy • 1997: economic reforms initiated in consultation with IMF following Asian financial crisis, and macro-economic disturbances	• Market-based economy in which government plays a significant role • Elimination of economic policies favouring certain families, greater private sector participation in economic activities • Privatisation of SOEs as a condition for assistance from IMF, but remains low

	Feature of earlier economic policy regime	Year when economic reforms initiated and trigger	Feature of new economic policy since economic reforms
Vietnam	• Centrally planned economic development model • Dominance of SOEs, Private participation limited • Administratively decided industrialisation policy	• 1986: *Doi Moi* (reform) process initiated following huge public sector and trade deficits, high inflation, and slowing growth • 1997: Asian Financial crisis and other structural deficiencies pushed up economic reforms	• Socialist-oriented market economy • Trade liberalisation, foreign investment encouraged, state intervention confined to regulatory role of the market, attracting private participation • Restructuring of SOEs for improving performance, to operate on commercial principles
Cambodia	• Centrally planned economic system totally controlled by state • Land considered as public property	• 1987: opening of economy, elimination of state monopoly for foreign trade due to external pressure and linked to evolution of political situation • 1993: Constitution sets forth market economy system • 1998: Fundamental reforms initiated following fundamental reforms and political crisis	• Private ownership of economic activity recognised • Trade liberalisation, privatisation of SOEs • Control over exports through licenses and permits

4. Evolution of Sectoral Regulation

Developing countries are in general characterised with low per capita income and consumer welfare levels. Economic development policies in these countries have the objective of reducing poverty and improving the well being of masses. Therefore, in developing countries regulation is likely to be not simply concerned with the pursuit of economic efficiency but with wider social welfare goals.

In view of these factors, traditionally, state has played a primary role in provision of infrastructure services in developing countries. Moreover, private sector was perceived as not having the wherewithal to invest in such long gestation activities. Accordingly, governments pursued their economic philosophy to accelerate development by establishing and encouraging state-owned enterprises (SOEs). The expectation was that combination of political control and accountability, and administrative *diktat* could best meet regulatory goals.

However, the performance with regard to provision of infrastructure services has been quite poor in most developing countries including the project countries. Large fractions of populations continue to be deprived of access to these services. Technical performance has been low, with generally low levels of productivity. Availability and pricing of infrastructure services has been highly politicised. Most SOEs incurred deficits and became an additional burden on the state. The poor performance of these infrastructure sectors became a drag on economic growth.

This led to a policy shift involving restructuring/privatisation of SOEs and encouragement to private participation. It has been realised that the manner in which governments intervened in

providing these infrastructure services proved to be ineffective. Moreover, the apparent successes of privatisation and market liberalisation programmes in developed economies prompted a shift in public policy from direct state ownership to private ownership with state regulation.

Technological advances also created opportunities by making possible the entry of other operators even in industries that were traditionally regarded as natural monopolies. For instance, in the electricity sector, new technology has enabled competitive generation and distribution industries to develop, even where the network remains a monopoly. Similarly, in telecommunications, new technologies are challenging predominance of a single national network and are opening up the market to competition. In view of these reasons, it was realised that private participation could play a significant role and more investible resources could be expected to flow. This calls for putting in place effective regulatory institutions to provide credible commitments that investors will not be held up once their investments have been sunk, that consumers would be protected from excessive prices and poor-quality service, that other goals for the sector (universal service) would be achieved.

There are a number of decisions to be made regarding the structure of regulatory framework including single industry versus multi-industry regulatory agency, designation and powers of regulatory authorities, regulatory appointment procedures, financial autonomy, staffing, fora to arbitrate controversies, administrative procedures, and role of antitrust authority in competition issues in regulated industries.

In principle following three broad forms of regulation have emerged[5]:

(a) Regulatory authority is *integrated* into normal government machinery, notably where it is a section of ministry and controlled by minister;
(b) *Semi-independent agency*, which has some independence from ministry but where decisions can still be over-ruled by a superior government authority; and
(c) *Independent agency*, where there is no right of appeal to a superior government authority, though there usually is a right of appeal to the courts to ensure fairness and rationality in decision- making process.

An important policy reform relates to separation of policy-making, regulation and operation functions. The project countries have significantly progressed from a situation where all three functions were vested in same agency to a situation where in most countries, and in many sectors, operation function has been separated and in several cases, regulatory function has also been separated. Nevertheless, separation of the three functions has not been effected in true sense as they continue to be interlinked. The most prominent being cases where an independent regulator has been set up, but is made to report to a line ministry, which also manages SOE. Another case arises where regulatory body has been set up within line ministry that also manages SOE. These raise conflict of interest issues.

In this context, the regulatory framework adopted by Zambia in water supply and sanitation sector is a good example of separation of policy-making, regulation and operation functions.

> *In Zambia, responsibility for water supply and sanitation service provision is under Ministry of Local Government and Housing (MLGH). In order to follow the principle of separating policy making and regulation functions, the regulator, National Water Supply and Sanitation Council (NWASCO) is made to report to Government through the*

[5] ibid

Ministry of Energy and Water Development (MEWD), which is water sector's "line" ministry.

Sectoral regulation has not evolved at the same pace in project countries. Variations are observed in terms of setting of regulatory bodies and their relation with government.

In Vietnam, for instance, government policy emphasises on separating commercial operations from ministries; but creation of regulators, independent from government is not the preferred approach, and line ministries perform policy-making and regulatory functions. In Indonesia, setting up specialised regulatory bodies under direct control of ministry is a common practice. Cambodia, India, Zambia, and South Africa, on the other hand, have established independent regulatory bodies in some sectors (primarily telecom, electricity), while relevant ministry acts as policy-maker as well as regulator in some others (primarily transportation). Kenya seems to be the frontrunner among project countries in establishing independent regulatory bodies, with regulators established in most infrastructure services (telecom, electricity, water supply, road transport, and seaports).

In infrastructure services, on one extreme are telecommunications and electricity sectors where independent regulatory bodies have been established in almost all countries. On the other extreme is transportation, which continues to be largely under state control. Water supply and sanitation sector falls between the two extremes, as some countries have established independent regulatory bodies and in others, government continues to control the sector.

Interestingly, in telecommunications, electricity, and water supply and sanitation sectors, countries that have allowed private sector in service provision have also established an independent regulatory regime. However, the same principle does not seem to apply in case of transport sectors, where private operators have been allowed, but not much attempt has been made to establish an independent regulatory regime.

As part of regulatory reforms, most project countries have sought to preserve the monopoly of their incumbent state-owned service providers. For instance, South Africa and Kenya granted specified periods of exclusivity to their SOEs in both telecom and electricity sectors. Anyhow, in telecom, technology (in the form of mobile phones) came to the rescue of consumers and policies favouring incumbent SOEs did not have much impact. There was no such respite for consumers in other sectors.

Some countries replaced their public monopoly with a private monopoly in the process of regulatory reforms. Kenya, for instance, created a private monopoly in air transportation, and in railways, private sector monopoly is set for creation. In Zambia, private monopolies have been created in power, railways and seaports. The experience with regard to creating a private monopoly has not been good as welfare benefits of transferring ownership to a private investor have not been realised. In Kenya, for instance, there are complaints of excessive tariffs.

Coming to financial services, banking is one sector that is placed under independent regulation of central bank. In some project countries, central bank had been performing the functions of a commercial bank in addition to supervision of other banks. All such countries have now created a two-tier system, with central bank being divested of commercial operations and made responsible for monetary policy and regulation and supervision of commercial banks.

Capital market is another sector where independent regulatory regimes have been established in project countries, with the exception of Vietnam, where the capital market regulator (State

Securities Commission) has been established under Ministry of Finance. In both insurance and pensions sectors, India, South Africa and Kenya have established independent regulatory bodies, while others have established an agency within relevant ministry.

In brief, project countries have come quite far from a situation where government controlled all the sectors to a situation where independent regulatory regimes are being established. Considering the experience of project countries in regulatory reforms, they can be clubbed into two broad categories:

- One set comprises of Kenya, Zambia, South Africa, India, and Cambodia (to an extent) that have taken measures to separate policy-making, regulation and operation functions and created an independent agency to undertake regulatory functions in several (if not all) sectors
- Second set comprises of Vietnam and Indonesia where state continues to hold sway over policy and regulatory matters.

Regulatory reform is still at an evolutionary stage in these countries and there is a need for them to continuously probe their regulatory environment. This study is an attempt to do a review of the nature of regulatory regimes that has been established in project countries.

Table 1.3 Separation of Policy-making, Regulatory and Operation Functions: The Scenario in Project Countries

	Kenya	Zambia	South Africa	India	Indonesia	Vietnam	Cambodia
Telecom	All functions separated; Regulator and SOE report to line minister	All functions separated; Regulator and SOE report to line minister	All functions separated; Regulator and SOE report to line minister	All functions separated; Regulator and SOE report to line minister	All functions separated; Regulator under direct control of Ministry, SOE reports to line ministry	Only operation separated; line ministry: policy-maker regulator, and manages SOE	Only operation separated (separation of regulation under discussion); line ministry oversees functioning of SOE
Electricity	All functions separated; Regulator and SOE report to line minister	All functions separated; Regulator and SOE report to line minister	All functions separated; regulator reports to line ministry, and SOE reports to Ministry of Public Enterprises	All functions separated; Regulator and SOE report to line minister	Only operation separated; SOE reports to line ministry	All functions separated; regulator established as a unit within line ministry; SOE managed by line ministry	All functions separated; separation of powers between regulator and line ministry provided in law; SOE managed by line ministry
Oil & Gas	—			All functions separated; Regulator and SOE report to line minister	All functions separated; Regulator and SOE report to line minister	—	—
Water Supply & Sanitation	All functions separated	All functions separated; regulator reports to a ministry different from that responsible for WSS service provision; service provision by local governments	Only operation separated; service provision by local governments	Only operation separated; service provision by local governments	All functions separated (confined to Jakarta city); service provision by local governments; regulator reports to Governor	—	No separation (separation of regulation under discussion)
Road Transport (public passenger)	All functions separated; regulator reports to line ministry	Only operation separated	Only operation separated; SOE reports to Ministry of Public Enterprises	Only operation separated; SOE reports to state government dept concerned	All functions separated (confined to Jakarta city);	Only operation separated	Only operation separated
Airports	Regulation and operation by same entity	Regulation and operation by same entity	All functions separated; Regulator reports to line ministry	Regulation and operation by same entity (separation of regulation under discussion)	No separation	No separation	No separation

	Kenya	Zambia	South Africa	India	Indonesia	Vietnam	Cambodia
Seaports	All functions separated; regulator reports to line ministry; port authority(ies) report to line ministry	Only Operation separated	Only operation separated (separation of regulation under discussion)	All functions separated; regulator reports to line ministry; port authority(ies) to Central/State governments	No separation	No separation	No separation
Railways	Only operation separated	Only operation separated	Only operation separated; SOE reports to Ministry of Public Enterprises	No separation	Only operation separated; SOE reports to line ministry	Only operation separated; SOE managed by state government dept	Only operation separated (separation of regulation under discussion)

4.1 Communications

The past two decades have witnessed far-reaching reforms in the provision of telecommunications services. Before 1980s, telecommunications services were mainly provided by state-owned enterprises. The 1980s saw the role of state being increasingly changed from that of service provider to that of regulator and policymaker. These developments were a result of technological changes that enabled some segments of telecommunications to be subject to competition. Regulatory reform was also often undertaken by governments as a strategy to attract investment in the sector to enable increased telephone penetration. Pressure from Bretton Woods institutions and other international organisations to liberalise their markets was another factor that developing countries faced.

All project countries were, at some point of time, in a situation where telecom was combined with postal operations. Among other things, this made the separation of cost between the two operations difficult and often resulted in cross-subsidisation. Indonesia separated the two operations in 1965; India separated in 1985, and South Africa in 1991. All these countries carried out the separation before onset of regulatory reforms. Kenya and Zambia separated postal and telecom operations after the reforms, and Vietnam and Cambodia are reportedly moving in this direction. Among the key reasons cited for separation of the two operations is to allow telecom and postal services to be commercially oriented and facilitate the process of telecom reforms.

Before the initiation of regulatory reforms, communication services were entirely under the control of government in project countries. For instance, in Vietnam, Cambodia, and India, policy-making, regulation and operation functions in post and telecom were vested in the same agency. In other countries (Kenya, Zambia, South Africa and Indonesia), operation function was separated from policy-making and regulatory functions and a state-owned enterprise set up as sole service provider. Line ministry performed policy-making and regulatory roles, besides state management function over SOEs.

In terms of service delivery, performance of SOE service providers in all project countries was poor, both in terms of coverage and quality. This situation put pressure on government to improve service delivery. Technological advances in telecommunications and increased domestic demand further augmented this pressure. All this compelled the governments to adopt reforms in order to improve service delivery. Donor conditionalities (in Kenya) and international commitments (in Vietnam) were other reasons that made governments adopt regulatory reforms.

Most project countries got on to the path of reforms during 1990s by issuing a policy statement and/or enacting an enabling legislation. Among the key elements of reforms was allowing entry to private players. Anyhow, all countries, except Cambodia[6], undertook explicit measures, which favoured their state-owned service providers over private operators. Kenya and South Africa granted limited period monopoly to their SOEs in select services, primarily fixed telephony. Indonesia made it incumbent upon other operators to enter into a mandatory cooperation with the SOEs. Vietnam encouraged domestic enterprises, mainly SOEs, to provide telecom services. Zambia imposed high entry costs for fixed line segment, thereby protecting the monopoly of Zamtel. India allowed private operators to provide only valued added services (which included mobile telephony). Thus, the reform process in telecom sector in these countries began with a relative disadvantage towards private operators.

[6] Cambodia did not take any such measure because of its special position – unlike most other countries, it does not have a dominant incumbent public sector operator due to the destruction of fixed line network in the civil war.

These restrictions, though, could not stem the march of technology, in the form of mobile telephony, which facilitated growth of telecom services. All countries have witnessed a spurt in mobile telephony, while performance of fixed line service, which is primarily dominated by SOE incumbent, continues to be poor.

A key element of regulatory reform relates to the setting up of a sector regulator. Kenya, Zambia, South Africa, and India have established an independent regulatory agency and in Cambodia establishment of a regulator is under discussion. Indonesia created a regulator with the Director General of Posts & Telecommunications, the earlier regulator (which was set-up within the Ministry of Communications) as its chairman. Thus, de facto, the new regulator continues to be under direct control of ministry. In Vietnam, line ministry performs regulatory functions.

In Indonesia and India, reforms were implemented in two phases, primarily because the first phase did not yield desired results, which was due to limitations inherent in regulatory law itself. In case of Indonesia, the law initially allowed entry to other operators, but made it conditional upon them to mandatorily cooperate with state-owned incumbents. Pursuant to economic crisis in 1997 and technological advances in telecommunications, government enacted a new law to facilitate introduction of competition and obligation to cooperate with SOEs was removed. The first phase in India witnessed turf war between the Department of Telecom (DoT, policy maker and service provider) and Telecom Regulatory Authority of India (TRAI), the regulator, raising doubts about regulator's powers. The worsening regulatory environment led to an amendment in the law that reconstituted the regulator giving further clarity to its powers. In this way, transition from first phase to second phase led to significant restructuring of regulatory regime in both countries.

South Africa began the process of reforms with a focus on broadcasting sector to ensure smoother transition from Apartheid to democracy and prohibit political control over broadcasters. The transformation of telecommunications regulation took a few years longer than broadcasting. Later, broadcasting and telecom regulators were merged and ICASA, the new regulator was formed in 2000 to accommodate convergence of technologies. Now, the postal regulator, which was established in 1998, is also set to merge with ICASA.

One common feature observed in regulatory reforms undertaken by project countries is that all have separated operation functions. There continues to be variation with respect to separation of policy-making and regulatory functions. Kenya, Zambia, South Africa, and India have separated all three functions. While Cambodia is considering separation of regulatory function, Vietnam has stuck to the policy of vesting policy-making and regulatory functions in the same agency i.e. line ministry. Indonesia has established a separate regulator, but as noted above, it is under the direct control of Ministry; hence separation has not taken place in true sense.

There are differences across project countries with respect to the sectors covered by regulatory agency. In South Africa, the sector regulator is responsible for regulation of post, telecommunications and broadcasting. In Kenya, Indonesia, Vietnam and Cambodia, the same regulatory agency is entrusted with the task of regulating telecom and postal services. In India, the regulator, TRAI is responsible for telecom, and broadcasting and cable services. A point worth noting in this respect is that TRAI was given the responsibility of regulating the broadcasting sector not to accommodate convergence of technologies, as was the case in South Africa, but to tackle a crisis that had occurred in the sector. In Zambia, regulator's ambit is confined to regulating telecom sector.

4.2 Energy

Energy is the driving force for growth and development and power is the foremost economic activity in energy sector. The provision of electricity to the whole population is, in general, an important policy objective of governments in developing countries, but budget constraints have limited their ability to increase generation and transmission capacity. Consequently, governments have tried to attract private investment, including foreign direct investment in this sector.

At the time of initiating reforms, operation function was already separated from policy-making and regulatory functions in all project countries, with Vietnam and Cambodia joining this league in year 1995 and 1996, respectively.

A vertically integrated monopoly was created to generate and provide electricity. In general, performance of these state-owned vertically integrated monopolies was poor, with a huge gap in demand and supply. Realising the importance of power sector in economic development and recognising the limitation of incumbent SOEs to meet this objective, steps were initiated to allow entry of private sector in power sector. Donor conditionality (Kenya and Zambia) was another factor that prompted some countries on the path of reforms.

All project countries enacted an enabling legislation to facilitate the reform process in power sector. Among the key elements of reform has been opening up of generation segment to private sector, thereby ending the monopoly of SOE incumbent. This is not surprising, as a key reason for undertaking reforms was to meet the growing demand by enhancing generation capacity. Some countries (Kenya and India) are moving in the direction of opening distribution segment to private sector as well.

Despite liberalisation measures, power sector in project countries continues to be dominated by SOE incumbent. Further, unbundling of SOE incumbent has not been favoured in most project countries and has been met with resistance. The exceptions are Kenya and India. While Kenya has undertaken partial unbundling by separating generation segment, in India, the enabling legislation mandates unbundling. SOEs in other project countries continue to be vertically integrated and this coupled with their dominant status raises concern about discrimination and other anti-competitive behaviour in situations where other operators seek to access the network of incumbent SOE. Further, in most cases, private generating companies end up supplying to a single buyer, resulting in absence of competition.

One of the rationales for privatisation was to facilitate competition and eliminate monopolies. But this has hardly happened. In fact, the opposite situation has emerged, as is the case in Zambia, where foreign private monopolies have replaced state-owned monopoly structure.

A key feature of regulatory reform relates to the establishment of sector regulator. Kenya and Cambodia have established independent regulatory bodies for electricity sector. Zambia and South Africa have established single regulator for entire energy sector. India has established independent regulators for electricity as well as oil & gas sectors. In India, electricity sector is in the Concurrent List of the Constitution, and both federal and provincial governments are responsible for its development. Therefore, separate regulatory bodies have been set up at the federal as well as in the provinces. Vietnam has recently established a regulatory body for power sector, but as a unit of Ministry of Industry. In Indonesia, surprisingly, the law to create an independent regulator in electricity sector was dismissed by High Court on the ground that it would end the monopoly of state owned service provider. Instead, a supervisory body has been established under government department.

4.3 Water Supply & Sanitation

Traditionally government and/or local authorities have played multiple roles of service provider, regulator and policy maker in water supply and sanitation sector in project countries. In Kenya, and Cambodia ministry concerned had been performing these multiple roles. In India, and Zambia, Ministry concerned was policy maker and regulator, and local authorities provided water services. In South Africa, and Indonesia all functions had been entrusted to local authorities.

As is the case with other sectors, performance in delivering water services has been poor in project countries. Accordingly, Kenya, Zambia, South Africa, and Indonesia undertook reforms with a focus on commercialisation. All four countries have enacted enabling legislation to facilitate reforms.

Kenya, Zambia and Indonesia established separate regulatory bodies to regulate water service delivery function, and Cambodia is considering one. While regulatory bodies in Kenya and Zambia have a countrywide mandate, the mandate of water regulator in Indonesia is presently confined to Jakarta city. All three countries have facilitated entry of private sector in service delivery. Indonesia has opened up service delivery function to private sector operation in certain geographic areas, particularly Jakarta. Kenya has established water services boards for service delivery, and Zambia has allowed local authorities to establish commercial utilities for service delivery.

South Africa has established a Department of Water Affairs to ensure a coherent strategy to develop water resources and improve service delivery. This step was undertaken to address the erstwhile fragmented approach to service delivery, and poor availability of water supply in black-population areas. Accordingly, the focus is presently on expansion of services to meet universal provision of services and little attention is given to economic regulation of water sector.

4.4 Transportation

Transportation consists of various sub-sectors: railways, civil aviation and airports, road transport, and seaports.

In road transport, most project countries allow private operators to provide public passenger transport services. In several of these countries, related Ministry/government department is responsible for policy-making and regulation. The exceptions are Kenya and Indonesia that have established regulatory bodies to regulate public passenger transport. While the regulator in Kenya, Transport Licensing Board (TLB) has a country-wide remit, Indonesia's regulator's jurisdiction is confined to Jakarta city where most operators are private.

Railway transport has traditionally been a state monopoly in all project countries. Several countries have taken measures in recent times to allow private sector in railway transport. For instance, Zambia has concessionaired its railway services to private sector and in Kenya privatisation of railways is under way. Indonesia and Cambodia are considering opening up the sector to private operators. Nevertheless, entry of private sector does not necessarily mean competition. For instance, with privatisation, Kenya railways is set to become a private monopoly. The entry of private sector calls for an independent regulatory regime and only Cambodia, among the project countries, is considering establishment of a regulatory body.

Services at seaports in project countries have traditionally been provided by government agencies. Most project countries allow private sector in port operations. For instance, Zambia has concessionaired its seaport to private sector as part of privatisation programme. The exceptions are Indonesia and Vietnam where port operations are controlled entirely by government or its agency. Of the countries that have allowed private entry, only Kenya and India have established separate regulatory bodies for seaports, and South Africa is considering one.

In civil aviation, most project countries allow private airlines to operate. While Kenya privatised its national carrier, other countries allowed entry to private sector airlines. In Kenya, Indonesia, Vietnam and South Africa, airports are managed by a government agency, whereas Zambia, Cambodia and recently India have allowed private participation in operation of airports. Anyhow, in all these countries regulatory functions continue to be performed by a government agency within relevant ministry.

In brief, all project countries have taken measures to facilitate entry of private sector in transportation sub-sectors, however, this does not necessarily imply emergence of competition. This is evident in the case of Zambia, which has created a private monopoly in Railways and seaports. Similarly, Kenya has created a regional monopoly in air transportation by privatising Kenya Airways, and is set to create a private monopoly in Railways. Further in transport sector there does not seem to be any connection between private participation and establishment of independent regulatory regime. For instance, Zambia has allowed private operators in all transport sub-sectors, but has not established independent regulator. In Kenya, South Africa, India, Indonesia, and Cambodia the approach towards establishing independent regulation is mixed. In some sectors where private operators have been allowed, independent regulators have been established, while in other sectors this is not the case.

4.5 Financial Services

The financial sector covers a broad category of services, namely, banking, capital markets insurance, pension and related services.

Central Bank is the oldest regulatory body in all project countries, entrusted with the responsibility of supervising the banking system. In Vietnam and Cambodia, central bank had earlier been involved in commercial banking operations, in addition to regulation and supervision of other commercial banks. Vietnam separated commercial banking function from central banking in 1988, and Cambodia adopted the system in 1996. This step was undertaken primarily to facilitate transformation of banking sector towards a liberalised regime and encourage participation of other players. In case of India, the central bank, Reserve Bank of India (RBI) continues to hold majority stake in State Bank of India, a leading nationalised commercial bank. This has raised concerns relating to conflict of interest arising from RBI being the regulator of monetary system and also owning a bank it is supposed to regulate. Anyhow, realising the issues at hand, RBI is said to divest its interest by end 2006.

Traditionally, financial sector in project countries has been strictly regulated and controlled by government. Credit, interest rates and exchange flows were controlled. Credit controls entailed direct or selective allocation of funds to certain sectors of the economy; in particular, SOEs. Interest rates were administratively set. Under this paradigm of administrative controls, financial system remained under-developed and repressed, and formed a key reason for undertaking

reforms. The Asian financial crisis of 1997 was another trigger for reforms, particularly in Asian countries.

Financial reforms entailed interest rate liberalisation, development of money and capital markets, removal of exchange rate controls, and entry of private sector in financial services. Besides, central banks have been given greater autonomy in carrying out banking regulation and supervision, as government rolled back its intervention. In Indonesia, however, which was most affected by the Asian Financial crisis among project countries, restructuring in banking sector led to most assets of banking system coming under the control of a government agency, as government took over failed banks to restore public confidence.

Most central banks are now tightening regulations to improve reliability of banking system and to conform to international prudential norms. Disclosure requirements, transparency and accountability mechanisms have now become key concepts in regulation.

In other financial sub-sectors, such as insurance, pensions, and capital market, traditionally some government department/agency performed regulatory function. This approach is now changing. In capital markets, for instance, most project countries have established a capital market regulator. The primary reasons being to facilitate raising of long-term credit and development of securities market. In insurance and pensions, the trend with respect to separation of policy-making and regulation is mixed, as some countries (India, South Africa, Kenya) have established independent regulators, and in others (Zambia, Cambodia, Vietnam, and Indonesia) regulatory function is performed by a government agency.

South Africa is following a policy of appointing a single regulator for broader sectors. Before 1980s, banks, insurance, and capital markets were regarded as separate sectors with little coordination between regulatory agencies in these sectors. Considering the areas of overlaps and potential conflicts in regulatory environment, South Africa established the Financial Services Board in 1990, to regulate all sub-sectors except banking. The country is now contemplating establishment of a single, mega-regulatory structure for the whole of financial services sector.

Table 1.4: Regulatory Institutional Frameworks in Project Countries

Sectors	Kenya	Zambia	South Africa	India	Indonesia	Vietnam	Cambodia
Communications	Communications Commission of Kenya (CCK) in 1999 (telecom, postal services)	Communications Authority of Zambia (CAZ) in 1994 (telecom)	Independent Communication Authority of South Africa (ICASA) in 2000 (formed after merger of broadcasting and telecom regulators; merger of postal regulator on cards)	Telecom Regulatory Authority of India (TRAI) in 1997 (reconstituted in 2000) (given the additional charge of broadcasting & cable services)	*Badan Regulasi Telekomunikasi Indonesia* (BRTI) in 2003 as advisory body within the line Ministry (telecom)	Ministry of Post and Telematics (telecom, postal services)	Ministry of Post and Telecommunication (establishment of regulator under discussion) (telecom, postal services)
Energy							
- Electricity	Electricity Regulatory Board (ERB) in 1998	Energy Regulation Board (ERB) in 1997	National Energy Regulator of South Africa (NERSA) in 2005 (earlier only National Electricity Regulator since 1995)	Central Electricity Regulatory Commission in 1998 (at Federal Level) State Electricity Regulatory Commissions (at Provincial Level)	*Pengawas Independen Pelaksanaan* (PIP) in 2003 as advisory body under the Department of Electricity and Energy	Electricity Regulatory Authority of Vietnam (ERAV) in 2005 as a unit under the Ministry of Industry	Electricity Authority of Cambodia in 2001
- Oil & Gas	-			Petroleum & Natural Gas Regulatory Board (about to be set up)	BPH Migas in 2003	-	-
Water Supply & Sanitation	Water Services Regulatory Board in 2003	National Water Supply and Sanitation Council in 2000	Department of Water Affairs and Forestry	Ministry of Water Resources	Jakarta Drinking Water Supply Regulatory Body in 2001	-	Ministry of Industry, Mines & Energy (establishment of regulator under discussion)
Transportation							
- Road Transport	Transport Licensing Board in 1962	Ministry of Communications and Transport	Department of Transport	Ministry of Shipping, Road Transport & Highways (Federal-level); Department of Transport (State level)	Transportation City Council in 2005 (jurisdiction confined to Jakarta) (advisor to Governor of Jakarta)	Vietnam Road Administration (under Ministry of Transportation)	Ministry of Public Works and Transport
- Sea ports	Kenya Maritime Authority in 2005		Department of Transport (Regulatory body on cards)	Tariff Authority for Major Ports in 1997	Central/ Provincial/Local governments	Vietnam Inland Waterway Administration and Vietnam National Maritime Bureau (under Ministry of Transportation)	

Sectors	Kenya	Zambia	South Africa	India	Indonesia	Vietnam	Cambodia
- Railways	Ministry of Transport		Department of Transport	Ministry of Railways	-	Vietnam Railway Administration (under Ministry of Transportation)	Ministry of Public Works and Transport (establishment of regulator under discussion)
- Civil Aviation	Kenya Civil Aviation Authority in 2002	Department of Civil Aviation (within the Ministry)	Ministry (on advise of 'Regulatory Committee')	Ministry of Civil Aviation (Aviation economic regulator being debated)	Central/ Provincial governments	Civil Aviation Administration (under Ministry of Transportation)	State Secretariat of Civil Aviation
Financial Services							
- Banking	Central Bank of Kenya in 1966	Bank of Zambia in 1964	South African Reserve Bank in 1921	Reserve Bank of India in 1935	Bank Indonesia in 1953	State Bank of Vietnam in 1951	National Bank of Cambodia in 1980
- Capital market	Capital Market Authority in 1990	Securities and Exchange Commission in 1993	Financial Services Board in 1990	Securities and Exchange Board of India in 1988	Capital Market Executive Agency (Bapepam) in 1976	State Securities Commission in 1996 (under the Ministry of Finance)	-
- Insurance	Commissioner of Insurance (under the Treasury) (establishment of autonomous regulator in process)	Pensions and Insurance Authority in 1997 (under Ministry of Finance and National Planning)		Insurance Regulatory and Development Authority in 2000	Directorate of Insurance (within Ministry of Finance)	Insurance and Reinsurance Supervisory Authority (within the Ministry of Finance)	Ministry of Economy & Finance
- Pension	Retirement Benefits Authority in 1997			Pension Fund Regulatory and Development Authority in 2005	Directorate of Pensions (within Ministry of Finance)	-	-

5. Evaluation of Sectoral Regulatory Framework

5.1 Regulatory Mandate

Independent regulatory bodies, where established in project countries, have been assigned similar mandate.

In communications, for instance, independent regulatory bodies established in Kenya, Zambia, South Africa and India are given the mandate of licensing, tariff regulation, interconnection, spectrum management, and quality of service (QoS) standards.

Variations are nevertheless observed in respect of whether regulator's role is advisory in nature or absolute. In case of licensing, both Indian and South African regulators perform an advisory role and line minister concerned takes the final decision. In South Africa, where a single regulator has been established for telecom and broadcasting services, the regulator, ICASA, is assigned different roles when it comes to licensing in telecom and broadcasting sectors. In telecom sector ICASA's role is advisory in nature, which is not so in the case of broadcasting sector. Dispute resolution is an area that puts the Indian telecom regulator, TRAI at disadvantageous position vis-à-vis regulatory bodies in other countries. As per law, TRAI is not entitled to handle disputes between stakeholders, which significantly limit its powers, as almost any issue can be presented as a 'dispute' between interested parties. In Indonesia, the telecom regulator, BRTI plays an advisory role to Ministry with the DGPT having final word on any decision. In both Vietnam and Cambodia, where line minister concerned performs regulatory function, their mandate includes licensing, tariff regulation, interconnection, spectrum management, quality of service standards, and dispute resolution.

In power sector, independent regulators have been assigned the mandate of licensing, tariff regulation, QoS standards, and dispute resolution. Difference arises in the case of Indonesia where an advisory body has been set up. Similarly in Kenya, the electricity regulator has been given an advisory role in respect of licensing. In Vietnam the separate regulatory body established as a unit within the ministry assists minister in regulatory matters i.e. licensing, tariff regulation, and dispute resolution.

In case of water supply and sanitation sector, independent water regulators established in Kenya, Zambia and Indonesia have been assigned the mandate of tariff regulation, QoS standards, and dispute resolution. However, there is variation with respect to licensing role: Kenya and Zambia's water regulators have an explicit mandate to license a water service provider, and Indonesia's water regulator for Jakarta city has no such role.

In road transport, only Kenya[7] has established an independent regulatory body, the Transport Licensing Board. However, the mandate given to it is grossly inadequate. The regulator's role is confined to only licensing, and it does not have the mandate to regulate tariffs, prepare road transport plans such as number of public vehicles plying on each route (required to ensure all routes are served), and is not empowered to specify service standards.

In seaports, only Kenya and India have established independent regulators. However, there are variations with respect to mandate given to these regulators. The Kenya Maritime Authority is required to formulate general guidelines, and coordinate the implementation of policies relating

[7] Indonesia has also established a regulator for road transport whose jurisdiction is confined to Jakarta city, but it is not independent and serves as an advisor to Governor of Jakarta

to maritime affairs. As observed, these are not related to economic regulation. On the other hand, India's Tariff Authority for Major Ports (TAMP) has been given the mandate of regulating tariffs in major ports. However, it has no jurisdiction over minor/private ports[8], and has no jurisdiction over access issues.

In financial services central bank in all project countries is generally given the mandate of formulating and executing monetary policy, and carrying out supervision and regulation of banks. However, in Zambia, after an amendment in the Act in 1996, the Bank of Zambia, country's central bank's functioning has been confined to ensuring price and financial system stability. Keeping aside these variations, central bank in all project countries set prudential regulations.

[8] Ports in India are divided into "major ports" (where the central government plays policy and regulatory functions) and "minor ports" (which are under the jurisdiction of state (provincial) governments).

Table 1.5 Mandate Assigned to Regulatory Agencies in Project Countries

Sectors	Kenya	Zambia	South Africa	India	Indonesia	Vietnam	Cambodia
Communications	• Licensing • Tariff regulation • Interconnection • Spectrum management • QoS Standards • Dispute resolution	• Licensing • Tariff Regulation • Interconnection • Spectrum management • QoS standards • Dispute resolution	• Licensing (advisory role in telecom) • Tariff regulation • Interconnection • Spectrum management • QoS standards • Dispute resolution	• Licensing (advisory) • Tariff regulation • Interconnection • Spectrum management (advisory) • QoS Standards	• Advisory role	• Licensing • Tariff regulation • Interconnection • Spectrum management • QoS standards • Dispute resolution	• Licensing • Interconnection
Energy							
- Electricity	• Licensing (advisory) • Tariff regulation • QoS Standards • Dispute resolution	• Licensing • Tariff regulation • QoS Standards • Dispute resolution	• Licensing • Tariff regulation • QoS Standards • Dispute resolution	• Licensing • Tariff regulation • QoS Standards • Dispute resolution	• Advisory role (regulator only for tariff matters)	• Licensing • Tariff regulation • Dispute resolution	• Licensing • Tariff regulation • QoS standards • Dispute resolution
- Oil & Gas				• Licensing • Tariff regulation • QoS Standards • Dispute resolution	• Licensing • Tariff regulation • QoS Standards • Dispute resolution		
Banking	• Monetary policy • Licensing • Supervision and regulation	• Monetary policy • Licensing • Supervision and regulation	• Monetary policy • Licensing • Supervision and regulation	• Monetary policy • Supervision and regulation	• Monetary policy • Supervision and regulation	• Monetary policy • Licensing • Supervision and regulation	• Monetary policy • Licensing • Supervision and regulation

5.2 Governance Issues (Appointment, Dismissal)

Regulation is recognised to be a business in which people make a difference[9] i.e. implementation of regulation is a human and not simply a technical function, so the quality of regulators is important. 'Quality' is generally implied to mean, people with relevant expertise. This requires having in place proper mechanisms to ensure appointment of experts as regulators.

Variations are observed in approaches followed for selection and appointment to regulatory agencies in project countries. Following approaches are observed:

i) Selection and appointment at the discretion of minister (primarily in Kenya)
ii) Selection by search committee and appointment at the discretion of line minister (as in India)
iii) Selection through a competitive process and appointment by line minister (telecom and water regulators in Indonesia)
iv) Nomination by line minister, ratified by Parliament (telecom regulator in Zambia)
v) Recommendation of suitable names by an expert panel, ratified by Parliament (oil & gas regulator in Indonesia)
vi) Nominations invited from public and ratified by departmental parliamentary committee (telecom sector in South Africa)

In the first three approaches, line minister plays a decisive role in appointment. The first approach is primarily prevalent in Kenya where line minister concerned has a great say in appointments in regulatory bodies. In second and third approaches, while line minister makes appointment, nomination of candidates is through different approaches. In India, a search committee comprising of representatives from judiciary/government officials makes nominations. There is lack of transparency in this approach and most often, retired bureaucrats/ judges get appointed. In contrast, *the process of selecting telecom and water regulators in Indonesia is transparent. Announcement of vacancies is made through media and candidates have to pass a vigorous test process prior to being considered for appointment as regulator.*

In the last three approaches, *Parliament plays a decisive role in ratifying candidates*. On one hand is Zambia, where line minister makes nominations for appointing telecom regulator. On the other hand is *South Africa* where *nominations for appointing telecom regulator are invited from public and public hearings are held in respect of each candidate.*

In order to ensure that right people are selected and are given enough freedom to work, both selection and dismissal provisions are required to be free from any ministerial discretion. Though there are good practices with respect to selection and appointment, most of these practices get nullified by bad provisions relating to dismissal. For instance, in Zambia, though line minister does not enjoy a great say in appointment of telecom regulator, it is empowered to remove a member of Communications Authority of Zambia (CAZ) at its own discretion.

Following approaches are observed with respect to dismissal and no one country follows a uniform approach:

i) Dismissal at the discretion of line minister (primarily in Kenya)
ii) Suspension of regulator by government, with either explanation provided to Parliament (in the case of central bank in India) or matter referred to a competent court for decision (in the case of electricity regulator in Cambodia).

[9] David Parker et al, op cit

iii) Removed when proven guilty in a finding, either through a judicial probe or through a finding of Parliament.

In the first approach, regulator's term is at the mercy of line minister. The first approach is primarily followed in Kenya, where for instance, country's minister of communications suspended the board of CCK without any reason. In South Africa, line minister can withdraw appointment of a member of energy regulator should it find a member incompetent or unfit to fulfill the duties. The telecom regulator in India enjoys no legal protection from dismissal, beyond a right of being heard, if government wishes to remove them. In Zambia too, line minister plays a decisive role in removal of regulators.

The second approach is an improvement over the first one, as there are possibilities of overturning government's decision. In case of central bank in India, government retains the power to suspend the Board of Reserve Bank of India in certain circumstances, and in such an event, it has to inform Parliament about the circumstances that led to such action. In Cambodia, in case of electricity regulator, Prime Minister can suspend members from duties, with the final decision taken by a competent court.

In the third approach regulator can be removed only when found guilty in a finding. *In South Africa, a member of telecom regulator may be removed only when proved guilty in a finding of National Assembly and Assembly adopts resolution thereof. In electricity sector in India, a regulator cannot be removed unless proven guilty in a judicial probe.*

Though there are good practices in dismissal as well, but these are nullified by bad practice in selection/appointment. For instance, in Zambia, line minister cannot remove any member of energy regulator for no reason. However, this provision has limited impact, as appointments to energy regulator, in the first place, is made at the discretion of line minister.

Considering selection/appointment as well as dismissal provisions, *telecom regulator of South Africa* scores well. In both cases, *Parliament plays a decisive role, and line minister has minimalist role.*

Some regulatory legislation provide for appointment of representative of stakeholders on the board of regulatory body. In Kenya, the enabling legislation provides for appointment of representatives of stakeholders on the board of the electricity regulator. In Zambia, boards of telecom and water regulators, include representatives of government institutions, private sector, consumer organisations and other agencies. This facilitates stakeholder involvement and ensures that risk of capture by one particular group is kept at a minimum.

Table 1.6 Selection Mechanisms for Regulatory Agencies in Project Countries

Sectors	Kenya	Zambia	South Africa	India	Indonesia	Vietnam	Cambodia
Communications	Chairman (appointed by President) Members (appointed by line Minister); board includes officials from related ministries	Nominated from identified stakeholder groups (ratified by Parliament)	Chairman and members (appointed by President based on advice of Parliamentary Committee and nominations from public); board includes officials from related ministries	Appointed by central government (represented by line Minister concerned) *Nomination by search committee comprising of government officials and (judiciary, in some cases)*	Chairman and members (appointed by line minister) Members (other than Chairman) selected based on a competitive process	–	–
Energy							
- Electricity	Chairman (appointed by President) Official from related ministry Members (appointed by line Minister)	Appointment by line minister	Appointed by line minister	Appointed by central government (represented by line Minister concerned) *Nomination by search committee comprising of government officials and (judiciary, in some cases)*	Appointed by line minister	–	Chairman and members (proposed by Prime Minister and appointed by King)
- Oil & Gas	–				University of Indonesia appointed as consultant to nominate right candidates (ratified by Parliament)	–	–
Water Supply & Sanitation	Chairman (appointed by President) Members (appointed by line Minister)	Nominated from identified stakeholder groups (ratified by line minister, different from the ministry responsible for WSS service provision)	–	–	Chairman and members (appointed by line minister) Members (other than Chairman) selected based on a competitive process	–	–
Financial Services							
- Banking	Governor and other members (appointed by President in consultation with line Minister); board includes officials from related ministries	Chairman (appointed by President) Directors (appointed by line Minister) Nomination by line minister	Chairman and other members (appointed by President) Directors elected to represent different sectors	Appointed by central government (represented by line Minister concerned) *Nomination by search committee comprising of government officials and (judiciary, in some cases)*	Parliament approves name for Governor (appointed by President); Nomination of Deputy Governors by Governor BI (appointed by President)	Governor and other members (appointed by Prime Minister); all are government officials	Governor and Deputy Governor (proposed by government and appointed by King); other members (appointed by government)

5.3 Resources (Financial, Human)

Resources, both financial and human, at the disposal of a regulator help in effective implementation of its mandate. It is important that a regulator is not dependent on discretionary allocation by line minister; otherwise this would provide an opportunity to line minister to intervene in its functioning. Similarly, there is need to ensure regulatory body is staffed with skilled human resources to carry out regulatory functions.

Following approaches are observed in project countries relating to funding mechanism for a regulatory body:

i) Funding part of line minister's budget
ii) Funding from Parliament appropriations, but money allocated as per line minister's discretion
iii) Regulator funded from resources independent of government's budget, but levy/fees, etc determined by line minister
iv) Regulator raises resources through levy, fees, etc, which is either determined by itself or is mentioned in the enabling legislation

Central bank in most project countries is observed to be the only regulatory agency that is given sufficient financial autonomy and has sufficient funds to implement its mandate. In most other cases, line minister plays a decisive role.

A problem with the first two approaches is that given the overall constraints on government's budget, the amount available to a regulator is not enough to help it implement its mandate effectively. Ideally, this should not be a problem in cases where funding is from sources independent of government, anyhow there are cases where even in this approach the amount available is not enough, as overall amount to be raised is determined by government. This is the case with communications regulator in Zambia. As a result, while telecom service providers have adopted more advanced technological equipment, CAZ has not got sufficient funds from government to procure a spectrum monitoring equipment to improve it's capacity to monitor service providers.

The case in South Africa, presents a disturbing scenario with respect to telecom regulator. Earlier it was observed that selection/appointment and dismissal provisions followed for ICASA provides it enough freedom from discretionary actions of line minister. However, in case of funding, ICASA does not enjoy any independence and government allocates budget to ICASA at its discretion. This seriously compromises on ICASA's ability to implement its mandate effectively. This issue came out strongly in a case where ICASA had planned to challenge Telkom, the state-owned incumbent, in court. Though it demonstrated ICASA's willingness to take action against the SOE, the regulator had to request government for funding to fight the case against Telkom. ICASA further pleaded government to help it resolve the problem, being the majority shareholder in Telkom! Similar problem of limited resources is encountered by TRAI, the telecom regulator of India that had sought government's permission for an independent source of funding. However, the proposal was turned down by Ministry of Finance.

In India, there is a general apathy towards granting financial autonomy to regulatory agencies. In most cases, relevant provisions of law that seek to ensure financially autonomy are also not implemented. In cases where regulators are allowed to raise resources, they do not have the freedom to spend it. The insurance regulator, for instance, is currently having a dispute with Ministry of Finance in this regard.

Several regulatory agencies in project countries are funded from sources independent of government's budget, but government decides the allocation/quantum of money. For instance, in South Africa, Financial Services Board is allowed to raise funds through imposing fee/levy on companies it regulates, but it is the government that determines the quantum of levy/fee. Similar approach is observed in case of several other regulators. *The status of energy regulator in Zambia has improved* in this context, as *the government recently took measures to enhance its financial autonomy. Earlier, amount collected by Energy Regulatory Board (ERB) was deposited in general revenue account of government. Realising that this provision constrained ERB's financial independence, an amendment was made in the enabling Act to allow ERB to retain a certain percentage of amount collected from undertakings as license fees.*

The fourth approach does ensure financial autonomy. Anyhow, when regulator is empowered to determine levy/fees, a concern often cited is that it might misuse this power and over-charge consumers. There are, in fact, such complaints against the Communications Commission of Kenya (CCK).

Financing a regulatory body through imposition of levy/fee is considered prudent, given the budget constraints governments generally face, particularly in developing countries. At the same time, proper arrangements are required to be in place in cases where regulator is empowered to determine levy/fees, etc to ensure the autonomy is not misused.

Financial autonomy determines the ability to appoint skilled personnel. Regulatory authorities often compete for qualified personnel with private sector firms and other entities that tend to have access to greater financial resources and flexibility in their hiring processes. Weak financial autonomy can greatly damage an authority's ability to compete in this area. The problem could be further compounded if regulatory bodies do not have freedom to appoint staff and determine their salary. To fulfill its obligations effectively, an agency needs staff composed of individuals with qualifications necessary to support agency's regulatory responsibilities.

Following approaches are observed in project countries with respect to staffing power given to regulatory bodies:

i) Staff is employed on deputation from various government departments
ii) Regulator has power to appoint staff but terms and conditions of employment require minister's approval
iii) Regulator has power to appoint staff and also determine terms and conditions

In the first two approaches, appointment of experts as staff of regulatory bodies is difficult. In case of India, for instance, most of the staff in regulatory agencies is on deputation from various government departments. In general, Government of India prescribes salaries and other terms and conditions of service of regulator's staff. In several cases, the number, nature and categories of staff too is determined with the approval of federal government. In Indonesia too, regulatory agencies often rely on personnel of related ministry. Consultant can be hired for specific purposes however the processes are cumbersome, as it requires approval of several related departments/agencies in government. As a result, regulatory agencies are poorly equipped. *Regulators in Kenya, in contrast, have the powers to appoint their own staff. The capital market authority, for instance, maintains a policy of attracting and retaining a small multidimensional team of professionals and administrative staff.*

Another constraint faced by regulators relates to compensation offered to their staff, as against that offered in private sector. Lower compensation acts as a stumbling block for regulators to engage professionals. For instance, in South Africa, regulatory bodies are not empowered to offer remuneration to their staff better than that offered by the public sector. Regulators often

compete with private sector to attract and retain qualified and talented staff, in which they often do not succeed mainly for the reason that public sector salaries, which regulatory agencies offer, are way below market rates. Nevertheless, *in South Africa, training and development programmes offered to staff are projected as an incentive to attract right talent.*

Regulatory bodies in Zambia and Cambodia, on the other hand, are empowered to appoint their own staff and determine their terms and conditions. This allows them to offer staff market-based salary, already witnessed in the case of NWASCO, the water regulator in Zambia.

In larger context, ability of regulatory agencies to offer attractive emoluments and to invest in skill development of their staff is subject to the extent of autonomy (financial and functional) ensured by law. Regulatory agencies will find it difficult to attract and retain high quality staff unless they are allowed to raise required resources, and given the freedom to structure the pay scales to make it attractive for their staff.

Table 1.7 Funding Arrangements for Regulatory Agencies in Project Countries

Sectors	Kenya	Zambia	South Africa	India	Indonesia	Vietnam	Cambodia
Communications	Levy/fees; determined by CCK board	License fees and government grants	Grants appropriated by Parliament; Parliamentary Portfolio Committee on Communication controls fiscal transactions	Grants from government (though law provides for regulator to raise funds through imposing levy etc)	Government's budget		
Energy							
- Electricity	Levy; determined by Minister	Retains 80% of License fees collected, as per Act	Levy (determined by Minister); government's budget	Grants from government (though law provides for regulator to raise funds through imposing levy etc)	Government's budget		Levy/fees; proposed by EAC and approved by Government (fee is subject to maximum stipulated in government order)
- Oil & Gas				Grants, fees, etc; budgetary requirement to be determined by a Committee, appointed by the government	Levy imposed on service providers		
Water Supply & Sanitation	Parliament appropriations, money provided at Minister's discretion	Levy/fees (determined in the Act)			Charges, fees		
Financial Services							
- Banking	Profits of the bank	Profits of the bank	Profits of the bank	Profits of the bank	Surplus, as prescribed in the Act	State Budget	Income of the bank
- Capital market	Fees, etc; determined by CMA	License fees and government grants	Fees, levy; prescribed by government in Gazette	Levy/fees			

5.4 Decision-making Process

Developing countries have had a history of poor infrastructure performance and arbitrary government intervention into a sector. Given this past, transparent administrative procedures are likely to be especially important to investors, competitors who rely on access to network infrastructure to compete, and consumers who want to be sure that objectives of the statute are being realised.

Three main categories of procedural rules can be identified that are designed to encourage transparency and third-party involvement in regulatory decision-making[10]: notification i.e. one-way communication between regulator and public; consultation i.e. collecting of information relevant to decision; and participation i.e. use of public hearings to allow oral representations and discussion.

The conventional form of regulation where government performs regulatory role has been criticised for discretionary decision-making, lack of transparency, ambiguity in procedures, etc. On the other hand, the independent regulation that has now emerged is based on transparency, involvement of stakeholders, participatory mechanisms, etc.

Broadly, two approaches are observed in project countries with respect to the decision-making process. One, where independent regulatory agencies take decision in consultation with stakeholders, and second approach, where decisions are taken in consultation with minister. In some other cases, regulator forwards its recommendations to minister after consulting stakeholders on related issues, as is the case with Kenya Electricity Regulatory Board and Telecom Regulatory Authority of India.

Independent regulatory bodies in most project countries involve stakeholders in the regulatory process. This is generally done by providing a link on regulators' websites, holding public hearings and open house discussions. Efforts are also made to disseminate relevant information to public and media.

A good model followed in involving stakeholders in the decision making process is that by NWASCO, the water regulator in Zambia. It involves various stakeholders at all levels of decision-making. In fact, from the beginning of reform process in the sector, particular emphasis was put on stakeholder participation. Stakeholders and public were made aware of reforms and its principles. Media was regularly briefed to sensitise stakeholders. As a result water issues became high on national development, social and political agenda with politicians and other decision makers being well informed of the progress and developments in the sector. *In order to ensure consumer involvement in tariff setting process, NWASCO has made it mandatory for water commercial utilities to hold consultative meetings with consumer representatives before applying for tariff adjustments. Similarly, the Jakarta Water Supply Regulatory Body (JWSRB) in Indonesia has taken measures to facilitate consumer involvement in decision-making process.*

In cases where regulator chooses to bypass ministry, and takes decisions not amenable to the ministry, it could earn the wrath of minister, as experienced by Communications Commission of Kenya that led to the disbanding of CCK board by Minister of Communications.

[10] Anthony Ogus, Comparing regulatory systems: institutions, processes and legal forms in industrialised countries Paper No. 35, December 2002

In banking sector, not all central banks in project countries involve stakeholders, and the decision is most often taken in consultation with Minister concerned. This is true in Kenya, Zambia, Indonesia and India. There is a sense of realisation that a consultative co-ordination with government is desirable as the duties of a central bank are inseparable from national economic policy as a whole. In South Africa, on the other hand, the central bank seeks to involve stakeholders by organising monetary policy forums with business, labour, politicians and academics.

In Vietnam and Cambodia, in sectors where minister performs regulatory role, consultation with public and industry is absent. Decision-making is discretionary, and procedures ambiguous. For instance, in Cambodia in telecom sector, there is no legal provision governing licensing procedures, and in its absence, the decision of Ministry of Post and Telecommunication often gives rise to contracts with private operators that have restrictive provisions. In Indonesia, on the other hand, despite most regulatory agencies being sub-ordinate to their related line ministries a proper consultation process is followed to make decisions. Anyhow, though ministers generally do not interfere, certain processes are in-built that lead to politicisation of decisions. For instance, the practice of seeking Parliamentary endorsement of proposed telecom price changes inevitably involves politicisation of pricing.

Consultative process in decision-making would not be meaningful if interest groups do not have required capability to take advantage of it. It can be presumed that regulated entities, actual and potential competitors that rely on regulated firm's network, and large industrial and commercial customers will have resources and ability to represent their own interests before regulatory agency. This is not likely to be the case for consumers. In practice, under representation of consumers remains a concern in project countries as they lack in capacity and resources to represent their interests.

5.5 Interface with Competition Authority

Liberalisation of markets traditionally associated with natural monopolies has given rise to a dilemma of institutional policy. In some areas, regulation in the form of price controls has been regarded as a temporary phenomenon pending arrival of sufficient competition. Legislation then typically requires of regulatory agencies both to promote competition and, if the market is insufficiently competitive, to control prices. The dilemma arises because typically, within the jurisdiction, there is a competition authority to enforce the competition law. Despite a common goal, conflicts between sector regulators and competition authority could arise, the resolution of which will depend on which is judged to be more effective of the two authorities on the basis of specific problem under consideration.

Following approaches are observed across the project countries:

- Division of responsibility based on practice
    - Sector regulators and competition authority cooperate with each other (as in Kenya; telecom regulator in Zambia)
    - Competition authority negotiates agreements with sector regulators (as in South Africa)
- Formal relation between sector regulator and competition authority provided in the law (energy and water regulators in Zambia; telecom regulator in India).
- Competition authority given an upper hand (as in Indonesia and Vietnam)
- Relation is ambiguous and no cooperation mechanism exists (electricity regulator, central bank in case of India)

The South African competition law provides for concurrent jurisdiction on competition matters and *Competition Commission is required to negotiate agreements with each sector regulatory authority and co-ordinate the exercise of collective jurisdiction*. The Competition Commission has so far signed a Memorandum of Agreement only with the communications authority. A formal agreement with other regulators does not exist, which often leads to jurisdictional conflict. For instance, a merger proposal in the banking sector sometime back triggered a crisis concerning concurrent jurisdiction of Reserve Bank and Competition Commission.

In Vietnam, competition law states clearly that where there is any disparity between the provisions of Competition Law and those of other laws on competition restriction or unfair competition, the *provisions of Competition Law shall apply*.

In Zambia, there are *direct linkages between competition authority and sector regulators* in energy and water sectors. Executive Director of ZCC sits on the Water and Sanitation Council and energy regulator is obliged by statute to consult with ZCC over competition matters. Though such formal relation does not exist with other sector regulators, there are signs of *co-operation and information sharing between sector regulators and competition body*.

In Indonesia, division of responsibility between competition authority and sector regulators has not been defined clearly in the competition law. Be that as it may, KPPU, the *competition authority is empowered by law to give recommendation to sector regulators* on competition issue.

In Kenya, the laws creating sector regulators contain a portion dealing with competition in the sector with no deliberate harmonization of the role of competition authority and sector regulators. Nevertheless, there are *indications that sector regulators consult with the Monopolies and Prices Commission.*

In India, there is inconsistency and lack of clarity in related laws. On one hand, there is a very clear statement in the TRAI Act that telecom regulator would be subject to the rulings of competition authority. On the other hand, Electricity Act directs regulator to act in a manner so as to promote competition and efficiency. Further, the nature of competition authority's power vis-à-vis statutory regulators is ambiguous. The law implicitly recognises that sectoral regulators have a role to play in competition matters and says that statutory regulators may refer competition matters to competition authority but to what extent competition authority can influence regulators in the absence of such requests is not clear. This ambiguity runs the risk of creating either gaps or conflicts in functioning of respective agencies.

Institutional structures are still evolving in several of these countries. The above discussion highlights the need for developing cooperation frameworks between competition authority and sector regulators. This could be done through establishing a regular information exchange with all sector regulators. For instance, in South Africa a Regulators Forum has been established as an informal body through which sector regulators envisage maintaining a consistent and coherent approach while dealing with competition matters.

5.6 Accountability Mechanism

Appropriate mechanisms are required to make independent regulatory agencies accountable.

Accountability could be political and legal in form[11]. Political accountability includes submitting reports to legislature which may have a special committee to scrutinise and debate its contents. Legal accountability enables those aggrieved by a decision to issue a formal complaint or appeal. Here one observes a divergence between countries which establish specialist commissions or tribunals, having powers to determine disputes only within a sector, or a related sector, and those which rely exclusively on institutions such as judiciary having competence over general administrative matters.

Broadly speaking, following two approaches are followed in project countries to make independent regulatory bodies accountable:

- Annual reporting to legislature
- Provision of appeals against orders of regulatory authority

All independent regulatory bodies in project countries are required to submit their annual reports and/or audited accounts to legislature. In most such cases, regulatory bodies are made accountable to legislature through line minister. Legislative oversight over regulators' performance does not seem to be effective, as annual reports submitted by regulator are not always discussed with any seriousness. Regulator's actions are questioned only when there is an impending crisis or a serious debate in a country. In fact, in most such cases it is the line minister that is questioned, and not regulator. This practice makes line minister assume performing functions that are otherwise delegated to a regulator by law. This assumption makes line minister interfere in the functioning of regulatory body.

The practice followed by South Africa shows the way forward in such cases. In case of ICASA, the communications regulator, there is a Parliamentary Portfolio Committee on Communications that maintains an oversight over regulator's performance. Similar practice is observed with respect to central bank of Cambodia. The National Assembly or its standing committee may ask National Bank of Cambodia to explain its policies or to comment on proposed legislation.

There are very few instances in project countries where stakeholders are involved in evaluating the performance of a regulator. One such is the case in Kenya, where Capital Markets Authority, the *capital markets regulator has an institutionalised annual review forum, which allows stakeholders to review its progress as well as raise any issues or suggestions to help stimulate domestic capital markets*.

Another mechanism to oversee the actions of a regulator is by having appeals provision, which allows review of regulator's decisions. Following approaches are observed in this regard:

- Separate appellate body is created to hear appeals against decisions of regulator or appeals lie in the judiciary
- Line minister act as the appellate body

A concern with the review process is if gates of review are opened too widely, the administrative costs of regulation may escalate and private interests might have an incentive to exploit the process for tactical purposes. It is important to ensure that the review process does not create a second layer of regulation, as is currently experienced in the telecom sector in India. In India's telecom sector the role of appellate tribunal, Telecom Disputes Settlement and Appellate Tribunal (TDSAT), is quite wide. The telecom regulator, TRAI is not empowered to settle disputes; rather TDSAT has been assigned with the responsibility. This division of labour has adversely affected the performance of telecom regulator, as any issue can be presented as a 'dispute'. Nevertheless, judicial review is important in guarding against decisions by a regulatory

[11] ibid

agency that fall outside of its statutory mandate or that fail to follow established administrative procedures. Taking the example of telecom sector in India again, TDSAT is found to have taken decisions in certain cases where TRAI was observed to have not followed due process. The point is that review jurisdiction should ensure that regulatory decisions conform to principles of natural justice rather than give appellate court the right to substitute itself in place of regulator, which could lead to regulatory lag.

In cases where appellate power lies with the minister, it could make regulatory decision-making process discretionary and undermine credibility of regulatory regime. In Zambia, for instance, in case of capital market regulator, parties aggrieved by a regulator's decision in specific circumstances, could appeal to line minister concerned. In Kenya, till recently, electricity regulator's decisions could be challenged by seeking recourse from Minister for Energy. The new energy bill is a key step forward, as it removes review power with minister and allows for public inquiry to enable review of decisions made by ERB. Similarly, in South Africa, appeals against energy regulator's decisions now lie in the judiciary. Earlier Minister was made appellate authority for National Electricity Regulator.

Table 1.8 Accountability Mechanisms for Regulatory Agencies in Project Countries

Sectors	Kenya	Zambia	South Africa	India	Indonesia	Vietnam	Cambodia
Communications	Annual report of activities submitted to Minister, *who tables it before Parliament*; Appeal can be made to Communications Appeals Tribunal	Annual report of activities submitted to Minister, *who tables it before Parliament*	Annual report of activities submitted to Minister, *who tables it before Parliament*; Appeal can be made to minister (on licensing matters)	Annual report of activities submitted to Minister, *who tables it before Parliament*; Appeal can be made to TDSAT	Quarterly report of activities submitted to Minister	–	–
Energy							
- Electricity	Annual report of activities submitted to Minister, *who tables it before Parliament*; Appeal can be made to the line Minister	Annual report of activities submitted to Minister, *who tables it before Parliament*	Annual report of activities submitted to Minister, *who tables it before Parliament* Appeal can be made to the Minister	Annual report of activities submitted to Minister, *who tables it before parliament (CERC)/ legislative assembly (SERCs)*; Appeal can be made to Appellate Tribunal for Electricity	–	–	Annual reports submitted to the Prime Minister
- Oil & Gas	–			Annual report of activities submitted to Minister, *who tables it before parliament*; Appeal can be made to Appellate Tribunal for Electricity	Half-yearly report submitted to the President	–	–
Water Supply & Sanitation	Annual report of activities submitted to Minister, *who tables it before Parliament*; Appeal can be made to Water Appeals Board	Annual report of activities submitted to Minister, *who tables it before Parliament*; Appeal can be made to minister (on licensing matters)	–	–	Annual report of activities submitted to Governor of Jakarta; Appeals can be made to an appellate body	–	–
Financial Services							
- Banking	Annual report of activities submitted to Minister, *who tables it before Parliament*	Annual report of activities submitted to Minister, *who tables it before Parliament*	Annual report of activities submitted to *Parliament*	Annual report of activities submitted to Minister	Quarterly report of activities submitted to *Parliament*	Report of activities submitted to government and National Assembly	Report of activities submitted to government and National Assembly

Sectors	Kenya	Zambia	South Africa	India	Indonesia	Vietnam	Cambodia
- Capital market	Audited report submitted to Minister, *who tables it before Parliament*; Appeal can be made to Capital Markets Tribunal	Annual report of activities submitted to Minister, *who tables it before Parliament*; Appeal can be made to Minister (when SEC gives direction to a Security Exchange)		Annual report of activities submitted to Minister; Appeal can be made to Securities Appellate Tribunal			

5.7 Enforcement of Regulatory Mandate

The standard arrangement post-regulatory reform is to leave the development of policy framework in the hands of Ministry, whilst implementation becomes the function of regulatory agency. The relationship between Ministry and regulator should thus be supportive, as the two are governed by a common vision.

The discussion in previous sections highlights various ways in which government intervenes in the functioning of regulatory bodies in project countries. This includes influencing selection process, enjoying powers to remove regulators, determining financial resources at the disposal of regulators, intervening in decision making process, etc. There are of course variations across project countries with good practices existing in some countries. In this section we review the extent of functional autonomy regulatory bodies enjoy in implementing their mandate and role of minister in this regard.

In most cases, line ministry is empowered by law to issue policy directives to regulator. While this should not be a matter of concern, as government has the sovereignty to formulate policies and set regulatory objectives. However, concern arises in cases where government intervenes in operational aspects of regulation in the name of issuing policy directives and affects independent functioning of regulators. For instance, the Bank of Zambia Act provides that "the Minister may convey to the Governor such general or particular Government policies as may affect the conduct of the affairs of the Bank and the Bank shall implement or give effect to such policies". The mandatory tenor in which this provision is couched leaves little doubt of the overriding influence that minister may wield over central bank on some policy matters.

Confusion prevails over what is a policy matter and what is a regulation matter, and government departments seek to deal with typical regulatory issues under the garb of 'policy' matters. This severely undermines the ability of a regulator to function independently. In this context, *the practice with respect to the Electricity Authority of Cambodia (EAC) is quite revealing. The enabling Act specifies clear separation of EAC's function as regulator from that of the ministry, and interaction between EAC and the ministry is clearly stated in the Law*. This ensures clarity in respective roles of Minister and regulator.

In several cases, legislation empowers line ministry to take final decision and regulator's role is advisory in nature. For instance, electricity regulatory board in Kenya acts as an advisor to the line minister with regard to licensing. Zambia's Energy Regulatory Board is required to seek minister's consent prior to revocation of a license or refusal to renew a licence. Certain provisions in Water Supply & Sanitation Act of Zambia give overriding powers to Minister. In seaports sector in India, government has retained the power to alter rates approved by TAMP, the regulator for major ports. There are several other similar examples across project countries.

There are cases where government intervenes to meet some social objectives, but ends up distorting the regulatory regime. For instance, in the electricity sector in India, government intervenes in tariff regulation in the name of providing subsidies. Due to continuous government intervention in regulators' functioning, regulatory environment in power sector is perceived as poor. Moreover, investment in the sector is not coming primarily because principal buyers, the state electricity boards, are bankrupt. In Vietnam, the only independent regulatory agency is the State Bank of Vietnam, country's central bank, whose autonomy is severely limited, as government interferes with the credit allocation mechanism to serve multiple socio-economic objectives of the economy. There are also difficulties in enforcing prudential regulations, due to

excessive lending to State enterprises that amounts to violating regulations limiting credit to a single borrower.

The situation of ICASA in South Africa is quite disturbing. The degree of independence given to ICASA varies with respect to its functions in telecommunications and broadcasting. In communications sector, for instance, it has to function in accordance with policy directions issued by the minister; whereas in case of broadcasting sector, it has to only 'consider' the policy directives. Further, Minister has a fairly wide discretion in respect of issuing licenses in telecom sector. This is not so with broadcasting. This dual regulatory model for ICASA affects its ability to respond swiftly to rapid technological changes in telecommunications and broadcasting sectors.

When it comes to regulating the SOE or taking measures that could impact the interest of SOEs, cases of micro-management by minister are observed, and independent regulators are perceived to be ineffective or powerless. In Kenya, for instance, when Minister for Communications disbanded the telecom regulator, it was alleged that decision was prompted because regulator was handling various disputes involving Telkom Kenya, the SOE incumbent, and some of the rulings had gone against the parastatal. In Zambia, the telecom regulator, CAZ is perceived to have failed in curbing restrictive practices of Zamtel, the state owned incumbent. Consequently, operators have approached Zambia Competition Commission. Concerns about CAZ's efficacy also stem from the fact that the regulator sits on the board of ZAMTEL leading to a conflict of interest situation. Similar situations are observed in other project countries. Such scenarios are likely to dent private investors' confidence in the regulatory regime, and private investment may hit a roadblock stalling growth of the sector.

Nevertheless, there are certain cases where regulators have been successful in regulating SOEs. For instance, the electricity regulator in Kenya and the energy regulator in South Africa have been successful in taking measures that were against the interest of incumbent SOEs, and government has upheld their decisions. Interestingly, in case of both the regulators, there is lot of ministerial intervention in selection, funding, etc. In this light, the success of these regulators in regulating SOEs might be due to an already existing cordial relation with Minister, as these are selected at minister's discretion and are likely to be close to minister. Anyhow, these are personal traits and are required to be addressed in a systematic way.

In this context, the practice followed in South Africa in electricity sector could be a way forward for other countries. Eskom, the dominant vertically integrated state-owned utility in power sector, reports to Department of Public Enterprises, and not Ministry of Minerals and Energy, the line ministry for energy sector. In this scenario, line ministry does not have any interest in protecting Eskom, and regulator is able to take action that affects SOE's interests. The regulator's assertiveness was shown when in year 2004 it turned down Eskom's request for an above-inflation tariff hike of 8.5% and instead approved a low 2.5% rise, which resulted in Eskom appealing to the ministry of minerals and energy department (which then enjoyed appellate powers), but Minister retained the order passed by regulator.

Lack of required skills and capacity is another major factor that affects regulators' ability to implement their mandate. This emerges from the state of, for instance, CAZ, Zambia's telecom regulator, where lack of skilled personnel has rendered price regulation futile. Even Ministry of Post and Telematics in Vietnam is observed as handicapped by a general lack of skilled personal and institutional capability.

Some regulators have taken certain specific measures to ensure effective regulation of a sector. For instance, Zambia's energy regulator has developed standards to monitor efficiency and

performance of regulated undertakings, and has developed inspection procedures, and guidelines for prospective investors. These measures have instilled investor confidence.

The water regulator in Zambia has developed information system, which facilitates competition amongst utilities by benchmarking, creating comparative competition in the absence of market competition. Interestingly, politicians no longer dictate tariff adjustments in water sector. NWASCO prevents consumers from paying for inefficiencies of service providers, and at the same time commercial utilities are allowed to charge tariffs to attain full cost recovery. This way regulation not only serves the interests of consumers and public but also service providers.

We now look at effectiveness of regulatory regime where minister performs regulatory functions, a model primarily followed by Vietnam. The Ministry of Post and Telematics (MPT) in Vietnam regulates the telecom sector. Concerns are often raised regarding the ability of VNPT, the state owned incumbent, to influence MPT in the governance of the sector. There is continued close relationship between MPT and VNPT, due to substantial rotation of personnel amongst MPT and VNPT. Inspite of this, MPT has taken a number of initiatives to improve access for newcomers and promote competition in the sector, and some of these actions have been against the interest of VNPT. Due to its active role, MPT has facilitated remarkable progress in telecom sector, and has changed the monopoly environment into business competition!

In Cambodia, on the other hand, where ministry concerned performs regulatory function, ambiguity of procedures, and lack of coordination between multiple agencies results in poor regulatory regime. Regulatory framework is marked by discretionary decision-making, and lack of transparency and predictability.

An important objective of regulation is to protect consumer interest. Several regulators have taken necessary measures to protect consumer interest. Most regulators have established procedures for handling consumer complaints. Some have even prepared consumer charters, as in electricity sector in Zambia and telecom sector in India. Anyhow, consumer protection measures are not always successful. For instance, electricity regulator of Kenya has a full-fledged department that handles all issues related to electricity consumers. However, political interference in regulator's functioning limits consumers' ability to effectively apply existing provisions for consumer protection. The telecom regulator in India finds itself helpless to ensure proper quality of services in the absence of penal powers. Instead, its reaction is confined to issuing periodic quality of service reports.

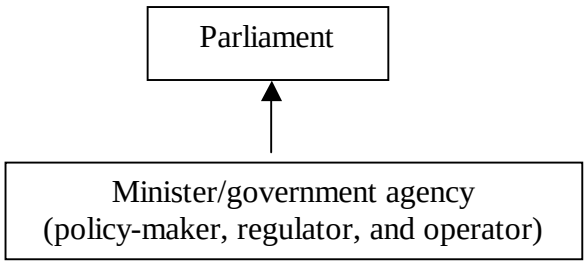
A good practice in addressing consumer complaints, and involving consumers in the regulator process emerges from Zambia. The regulators in energy, telecom, and water supply & sanitation have formed joint consumer councils or watch groups that cut across three sectors namely communications, energy and water. These groups act as regulators' link between consumers and service providers. They serve as an important contact point to channel consumer complaints, queries and other concerns pertaining to quality of services. The concept has proven to be very successful in establishing regulator's presence on the ground.

It is argued that regulatory institutions need to enjoy a certain degree of autonomy. Yet, autonomy should not come at the price of less co-ordination or conflict between policymaker and regulator. The line between policymaking and regulation is often blurred. Given the issues that developing countries face, such as promotion of universal access, there is no simple way of deciding where this line should be. Since regulatory agencies in developing countries are prone to political interference in decision-making, this could encourage industry to participate in rent-

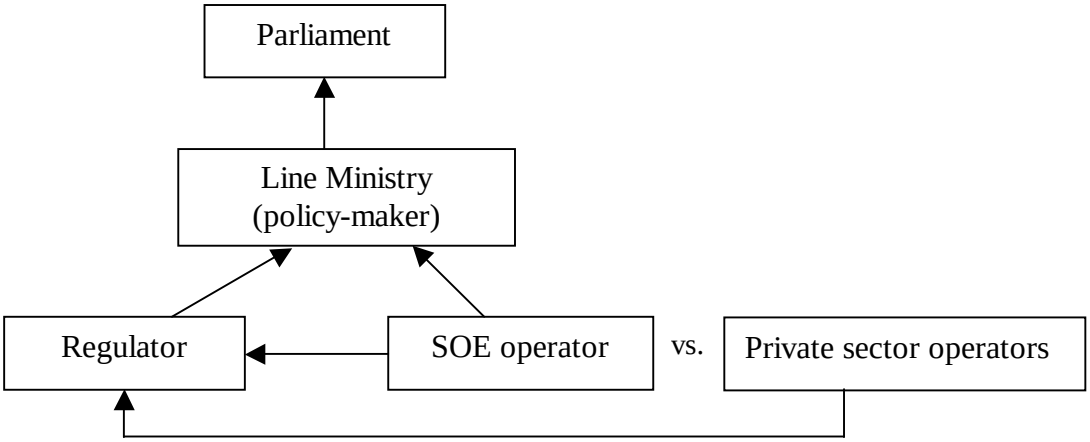
seeking activities[12]. One has to guard against such issues and design a regulatory regime that integrates the conditions prevailing in developing countries.

6. Concluding Remarks

The study does a review of regulatory environment that exists in select developing countries in Asia and Africa. The seven countries whose experiences have been surveyed have experienced regulation in different ways due to variations in their economies and political environments. The project countries started with a situation where line ministry or a government agency undertook all the three functions of policy-making, regulation and operation. The regulatory model followed was of the following type:



As a result of regulatory reforms, project countries have significantly progressed from the situation as depicted above to a situation where in most cases, operation function has been separated and in several cases, regulatory function has also been separated. The regulatory model that has now emerged is of the following type:



Nevertheless, separation of the three functions has not been effected in true sense as functions continue to be interlinked, and line ministry is made to assume performing the three roles. This often leads to ministerial intervention in functioning of regulatory agencies. The most prominent being cases where an independent regulator has been set up, but is made to report to a line ministry, which also manages SOE.

The study brings out that while countries have taken measures to establish regulatory bodies, not much effort has gone to imbibe the principles of regulation in regulatory process. Regulatory regime is expected to provide a set of transparent, consistent and non-discriminatory rules that

[12] Gertrude Makhaya, The Determinants of Regulatory Effectiveness in Liberalised Markets: Developing Country Experiences, TIPS Working Paper No.4, 2002

creates a competitive, dynamic environment in which firms can thrive, consumer interest is protected, and orderly growth of sector is facilitated. The project countries score poorly on this front. There are of course good practices in certain areas, but these are nullified by bad practices in several other areas, making overall regulatory system weak.

Public choice theory suggests that politicians and bureaucrats are self- seeking[13] and this has been a powerful argument for privatisation of state-owned utilities; but it is these very same politicians and civil servants who are expected to establish and maintain a credible regulatory structure after privatisation! The study highlights that there is tendency of bureaucracy to perpetuate itself in regulatory roles. In cases where independent regulator has been established and private operators compete with incumbent SOE, there are instances of ministerial intervention to protect SOE.

A key lesson is that for regulatory reforms to succeed, more important is a commitment on the part of government, and clear and consistent policy objectives. In this context, functioning of regulatory regime in telecom and banking sectors in Vietnam present an interesting contrast. In banking, the functioning of central bank has been constrained by government intervention in various ways. In contrast, functioning of MPT in telecom has done wonders for the sector. In telecom, government objectives are clearly laid down in various government documents, which have provided the necessary guidance for MPT to spur competition and facilitate an orderly growth of telecom services. However, in banking, there are conflicts in policy objectives – objectives of government are in variance from the goals set for the State Bank of Vietnam. Consequently, government intervenes to realise objectives other than that set for regulation.

Political will to create a strong regulatory agency from the outset is crucial for future success, as a strong regulator will be able to balance the demands of various interest groups, among other challenges. Unfortunately, as the case of Communications Commission of Kenya illustrates, state may try to further its interests by creating a weak regulatory institution over which it can continue to exert control. The relationship between Ministry and regulator should be well-defined, as it can become a source of tension and uncertainty.

A question that is left open is what precise forms of regulation are appropriate in the context of developing countries. The 'independent' agency model is normally favoured by western advisors, who draw from the experience of regulation in UK and US. Even in these systems it is possible to argue that political executive retains fundamental control. In United States, for instance, where the concept of independent regulatory commission was born and has evolved over the past century, regulatory agencies are not completely free from political pressures, and their information and staff expertise are often inadequate.

If we apply this more politically sensitive analysis to developing countries we simply cannot expect creation of arms-length agencies that can hope to establish any real 'independence' of dominant political and bureaucratic institutions, especially where partisan organisation itself may depend on the careful exercise of political patronage. In short, where regulators, and even in many cases judges, owe their positions to the political-bureaucratic elite, the possibilities for exercise of independent judgement and action are considerably reduced, or may be non-existent.

Furthermore, since privatisation and regulatory reforms are largely concentrated in public utilities where there is a strong public interest factor, and therefore political sensitivity to both policy reforms and to regulatory practice, it is difficult to envisage what 'independent regulation' could possibly mean, or how it might be insulated from overriding political considerations. It would

[13] David Parker et al, op cit

make more sense if regulatory reforms deliberately recognised these realities and incorporated them in to agency models, rather than constantly attempt to create an unlikely autonomy. Moreover, the experience of Vietnam in telecom sector regulation suggests that even government agencies could perform better and thereby questions the assumption that insulation from political establishment is a necessary pre-condition for effective regulation.

While there are lessons to be learned from the reform experience of industrial countries, it is important to recognise that these lessons cannot be applied mechanically to developing countries. Trying to apply a one-size-fits-all approach can severely limit the performance improvements that sector reforms hope to achieve. Considering the variation between national, political and administrative cultures across countries, regulatory regime should be specific to the requirements of each country[14]. In its absence, policy transfer process from one country to another is likely to produce the 'implementation deficit', as observed in project countries. For instance, in Kenya the design of regulatory institution has not taken into account the power wielded by political system. Therefore, regulatory bodies such as Communications Commission of Kenya face difficulty in implementing their mandate. As against this, in cases where minister has been given enough power, such as in case of Kenya Electricity Regulatory Board, regulatory body is found to be effective in implementing its mandate.

The credibility of any kind of 'independent regulation', modelled on the UK or US regulatory structures, may be weak and even where it does exist, deciding on appropriate degree of discretion to be given to regulators is likely to be problematic in the absence of experience of delegating decision-making powers to quasi governmental agencies. For a regulatory agency to be credible, it needs to inspire confidence in the eyes of regulated and general public. A lot of effort has to be put into communicating the aims of the institution and measures it takes to reach those goals. The case of NWASCO in Zambia is worth noting in this respect.

The study attempts to identify obstacles that developing countries have to overcome in the implementation of their regulatory regimes. Given the politically sensitive nature of services provided by utilities, there is bound to be political intervention in regulatory process. It is therefore important that regulatory regimes in developing countries are designed in a manner to integrate such factors rather than designed on the basis of international best practices.

1414 Martin Minogue, Governance-based analysis of regulation, CRC Paper No.3, October 2001

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Chapter II
Regulatory Environment in Kenya

1. Introduction

Kenya is located in East Africa, bordering Somalia to the east, Uganda to the west and Tanzania to the south.

With a gross domestic product (GDP) of about $14 billion, Kenya is the most developed economy in East Africa. Compared to its neighbours, Kenya has a more sophisticated and diversified economy and is considered the regional hub for trade and finance in East Africa.

Kenya's economy relies heavily on agriculture, which accounts for 30 per cent of GDP and employs an estimated 75 per cent (2003) of the labour force.

KENYA COUNTRY PROFILE	
Population:	31.9 million ***
GDP (Current US$):	13.8 billion ***
Per Capita Income: (Current US $)	450 (Atlas method)*** 1037 (at PPP) ***
Surface Area:	580.4 thousand sq. km
Life expectancy at birth:	47.2 years ***
Literacy (percent):	73.6 (of ages 15 and above)***
HDI Rank 2005:	154***
Sources: - World Development Indicators Database, World Bank, 2004 - Human Development Report Statistics, UNDP, 2004 (***) For the year 2003	

With an estimated population of 32 million people (almost half of whom are under the age of 15), the country's GDP per capita is less than $400. Over half of Kenya's population lives below the poverty line.

Kenya's economic performance has been in reverse gear for over two decades, dipping into the negatives during the 1990's. The country has been hampered by the failure to sustain prudent macro economic policies, the slow pace of structural reform and the persistence of governance problems. This is reflected in the high cost of doing business in the country because of corruption, deteriorating infrastructure and an inefficient parastatal sector. Political instability and suspension of external aid and support by the International Monetary Fund (IMF) and World Bank worsened the situation in the 1990s, which was compounded by a severe drought from 1999 to 2000. As a result, for the first time since independence, GDP contracted by 0.2 percent in 2000.

The rising perception that Kenya is a risky place for business has seen the decline in foreign direct investment (FDI) from $57 million in 1990 to $50.4 million in 2003 and fell further to only US$ 46 million in 2004. The rate of private investment has stagnated to about 10 percent of GDP.

In 2002 elections, the ruling Kenya African National Union party's regime ended and the country witnessed the arrival of the National Rainbow Coalition (NARC). The new government took on the formidable economic problems facing the nation. In 2003, progress was made in curbing corruption and encouraging donor support, with GDP growth edging up to 2.8 percent. The Kenyan economy continued its recovery in 2004 and real GDP expanded by 4.3 percent.

2. Evolution of Economic Policy Regime

The current economic set up in Kenya is one of market-oriented economy, influenced by development partners and international donor agencies, such as the IMF and the World Bank. The Kenyan government has systematically continued to de-link itself from the market to allow private sector's participation in the economic growth process especially after the recommendations of structural adjustment programmes (SAPs) by the international community which advocated for: liberalization of the economy and privatisation of state enterprises among others. Following paragraphs trace the evolution of economic policy regime in Kenya.

Before independence in 1963, there was very little private commercial activity by indigenous Africans in Kenya and people relied on the colonial government for provision of basic social services such as roads, transport, water provision, electricity and communications. The colonial government set up parastatals as channels to supply goods and services under the perception that these could not be provided efficiently and equitably through the market process by private sector participants.

Kenya's development strategy, post-independence, was informed by the need for rapid economic growth primarily through import substitution. In pursuit of these policies, economic planning was centralised and tended to be inward-oriented. This involved the creation of public enterprises in main areas of the economy. A majority of these enterprises were allowed to retain monopoly status in the quest to build them through economies of scale. The general feeling was that there was a need to create homegrown corporations to compete with transnational corporations (TNCs).

Following the first oil crisis, and the collapse of the East African Community (EAC) in 1977, the Kenya Government was compelled to review its strategy and allowed a relaxation of import restrictions. This policy shift was primarily directed towards raising the pressure on domestic manufacturers, in order to facilitate export earnings.

As the declared intention was to encourage the growth of state-owned enterprises, there were no periodic assessments of the costs and benefits from the maintenance of these monopolies. By early 1980s, it was clear that this strategy did not work because majority of state-owned enterprises were not only providing poor services, but were debt ridden and had high expenditures. It was apparent that these were symptoms of inherent inefficiencies and poor management. Due to their dependence on public resources, the need to keep these enterprises running had enormous budget implications. Therefore, the Government made the decision that expenditure control was imperative.

Kenya got on the road to economic reforms in 1992, in response to internal pressure for change as well as initiatives by the World Bank, IMF, and other multilateral and bilateral donors. Reforms included lifting price and foreign exchange controls, reducing tariffs and removing other trade barriers, adopting sound fiscal and monetary policies, and beginning a program of parastatal privatisation. These were in the form of SAPs, which saw Kenya government outline privatisation measures in the Policy Framework Paper of 1993-96. The reforms led to a brief turnaround in the economic performance.

Under the first phase of the privatisation program, initiated in 1992, the government privatised a large number of small and medium-sized enterprises, but progress in privatising key utilities and transportation enterprises has been slow. The privatisation process is still in progress and the

government has published a Privatisation Act, which seeks to lay the legal framework for the privatisation programme.

3. Evolution of Sectoral Regulation

The drive to deregulate and liberalise the market in Kenya has led to attempts at more precise economic definitions of what constitutes a natural monopoly. Kenya's process of introducing competition in regulated sectors is seemingly premised on several analyses done on the competitive potential, world-wide, in such sectors. Major ways of introducing competition into regulated utilities was to separate the monopolistic and competitive components.

As state-owned enterprises have been privatised in Kenya, the Government created regulatory authorities for those industries where there was a need to ensure proper market practices. Amongst the regulatory agencies created are the Communications Commission of Kenya (CCK), the Electricity Regulatory Board (ERB), the Capital Markets Authority (CMA) and the Retirement Benefits Authority (RBA). Besides, there is the Central Bank of Kenya (CBK), which regulates the banking and financial institutions. All these bodies operate under separate statutes.

Follows a brief on the evolution of sectoral regulation in select sectors in Kenya.

3.1 Telecommunications

The Kenya Posts and Telecommunication Corporation Ltd (KPTC), a parastatal established by an Act of Parliament in 1977, controlled the telecommunications and postal services till 1999. The role of KPTC was to provide postal and telecommunication services; and regulate and control radio communications. The ministry of transport and communication was in charge of setting the policy framework and tariffs.

Private players were allowed in 1991 in the sale, installation and maintenance of telecommunications terminal equipment. This was the first attempt towards introducing competition in certain aspects of the sector.

In 1997, the Government released a Telecommunications and Postal Sector Policy, which seeks to ensure availability of efficient, reliable and affordable communication services throughout the country. The policy statement provides a framework for the introduction of certain structural changes in the sector. This was prompted by the extraordinary technical progress in the sector. Donor conditionalities were also a driving force in carrying out reforms in this sector.

The release of the policy statement was followed by the enactment of the Kenya Communications Act in 1998, which gives legislative teeth to the policy statement. Key to this Act was the establishment of an independent regulatory authority, the Communications Commission of Kenya (CCK), the split of posts and telecom from the corporation and their establishment into two licensed limited companies: Telkom Kenya Ltd. (TKL) and Postal Corporation of Kenya.

Kenya chose to protect by law, the monopoly of TKL, the incumbent for the following services up to June 2004:

- Nairobi market where TKL generates 75% of its revenues
- Domestic long distance services
- International gateway and services
- Very Small Aperture Terminal (VSAT)

- Global Mobile Personal Communication by Satellite (GMPCS)
- Internet node and backbone (through JamboNet)

This arrangement was meant to accord TKL a grace period for re-organising itself to face competition and/or make itself attractive enough to fetch a good price on sale. Similar exclusivity provision had been followed in the UK (with British Telecom), in Argentina and even in South Africa.

The resultant industry structure is monopolistic in nature resulting into inefficiencies in the sector and having a bearing on the performance of the telecommunications sector. Performance of fixed-line services has been poor. For instance, only two percent of households have fixed lines, 60 percent of them located in the Nairobi area; and waiting time for new lines is eight years.

In 2000, eight licences for fixed telephony were sold to three regional telecommunications operators (RTO). As a result, four companies now provide fixed telephony services in Kenya: the incumbent operator (TKL), and three regional telecommunications operators.

Nevertheless, the fixed telephony market remains highly controlled by the incumbent. The RTO licences do not allow covering the Nairobi zone, reserved for TKL. Furthermore, according to their licences, RTOs have no right to provide inter-connectivity between regions. They have to rely on their competitor's (TKL) switches for inter-regional connections.

There are two mobile operators in Kenya, Safaricom and Kencell. The third operator is awaiting a court hearing to start operations.

Overall, the telecom sector has witnessed tremendous growth – a total of approximately 3 million subscribers were added into the network during 2000 to 2004. This was largely due to the spurt in mobile telephony; fixed line services did not perform well. The rapid growth of mobile telephony suggests that people were finding it a substitute for fixed-line services. Thus, exclusivity provided by law did not prove to be of much significance in an environment where technology created substitutable products and services.

3.2 Electricity

Prior to 1996, there were five parastatals involved in electric power generation, transmission and distribution. The Kenya Power and Lighting Company Limited (KPLC) purchased power from the Kenya Power Company (KPC), the Tana River Development Company Limited (TRDC), and the two regional authorities: Tana and Athi River Development Authority (TARDA) and the Kerio Valley Development Authority (KVDA) under some form of power purchase agreements. KPLC managed the operations of the other four organizations, under a management contract, giving it a *de facto* monopoly in the power sector.

Reforms in the power sector commenced through the passing of the Electric Power Act (EPA), 1997, which formalized the restructuring of the electric power industry and saw the separation of generation from transmission and distribution functions. Restructuring of the sector was a response to the drought, which affected the predominant hydro-power supply by the KPLC. To lessen the effects of power rationing, Independent Power Producers (IPPs) were commissioned to feed the national grid. The donor community too influenced the restructuring process. As the Kenya government continued to seek further development aid from the World Bank, more power sector oriented conditions were introduced covering electricity tariffs and rationalisation of the public sector electric power players.

The *de facto* monopoly of KPLC in power sector was brought to an end with the consolidation of public sector generation activities under Kenya Electricity Generating Company (KenGen), a state-owned enterprise. In addition, a framework was created in which Independent Power Producers were allowed to generate electricity for bulk sale to KPLC. Thus, competition has been introduced in power generation. However, KPLC enjoys a monopoly in transmission, distribution and retailing activities.

The thrust of the restructuring was to create arm's length commercial type-relationships between the sector entities, and create legal and regulatory framework that facilitate the restructuring of the sector and encourage private sector participation. Reforms of the sector resulted in the separation of commercial operations, policy setting and regulatory functions. The Ministry of Energy's role has been confined to overall policy formulation in the sector, and an independent body, Electricity Regulatory Board (ERB), was established to take over the regulatory function from the Minister. Ideally the regulatory systems should be in place before the opening up of the sector. However, this was not the case when the first two IPPs were licensed.

The sector continues to be dominated by KPLC, which enjoys a monopoly in transmission and distribution of electricity in the country. Consumers experience poor-quality service, including unexplained power fluctuations, blackouts and unreasonable hike in power tariffs.

The government is in the process of throwing open the distribution segment to private sector, ending KPLC's monopoly in this area, as well. However, transmission will remain the preserve of KPLC. This is part of a strategy by the Electricity Regulatory Board to bring down electricity prices, which are one of the highest in the region, as compared to other countries. The ERB has prepared a draft of the Kenya Electricity Grid Code with the aim of promoting competition wherever practicable and facilitate a commercial environment.

According to the year 2005 Economic survey, the total installed capacity increased by 4.9 per cent from 1,142.2 MW in 2003 to 1,198.1 in 2004. The total electricity generated increased by 7.1 per cent from 4851.6 Gwh in 2003 to 5,194.5 in 2004. However hydro power generation declined by 7.4 percent, requiring importation of power from the neighbouring countries to meet the demand, with imports from Uganda and Tanzania being 161.9 Million KWh. the demand for electricity has outstripped supply, precipitating a significant level of unserved demand, which in 2000/2001 was estimated to be 380GWh. A severe drought which occurred in 1999/2000 led to unprecedented power supply shortfall resulting in a devastating power rationing program. many industries either closed down or operated at minimal capacity. The domination of KPLC in the markets also results into high energy costs such that the power tariffs are set at 100% of the LRMC.

3.3 Transportation

The transport sector has several sub sectors including Road, Railway, Marine, and Air. So far road and air services are fully privatised.

Road transport is regulated by the transport licensing board (TLB), which seeks to ensure harmony in the provision of road transport services. The transport licensing board was established in 1962 following the enactment of the Transport Licensing Act, to nationalize transport services in Kenya and develop public transport services in the country. However the transport licensing board has not been effective. The previous government that ruled for 24 years had disbanded the TLB; reinstated by the current NARC government to streamline public transport services.

Air transport services were liberalized in 1996 with the privatisation of Kenya airways, although the airport management has remained in the hands of the state under the Kenya airports authority. The Kenya Civil Aviation Authority (KCAA), established in 2002, performs the role of air industry regulator in the aviation industry. Kenya Airways is the only local airline company operating international and regional flights – other players in the industry are Air Kenya, which operates only local flights; Regional Air, the only other airline operating regional flights collapsed in early 2005. Lately, there have been complaints about flight delays relating to Kenya airways, especially on the regional routes due to lack of competition. There is a general feeling that Kenya Airways is exploiting the regional market by charging high prices. For instance a flight to Entebbe in Uganda (where there is absence of competition) costs about US$400 while that to Dubai (a competitive route) is about US$300.

Railway transport has only one player, the Kenya railways corporation, which is wholly owned by the government but privatisation is underway. This means unless there are other participants offering services, Kenya railways will be a private monopoly. The government views the involvement of the private sector to increase efficiency and raise funds necessary to improve the rail services. Currently the rail tariffs are much less than those of the road transport with about 50%, however the services are much less efficient causing most commuters and transporters to prefer the road transport.

Water transport has Kenya ports authority, which is wholly owned by the government and a few private participants. Kenya ports authority manages maritime and inland waters. The Kenya Maritime Authority (KMA) has been established recently, de-linking the regulatory functions of Kenya Ports Authority, to regulate maritime affairs in the country. The Authority will oversee the enforcement of the maritime and shipping laws. The infrastructure at the ports will remain within the jurisdiction of Kenya ports authority and Kenya railways corporation, respectively[15]. The KMA will oversee the port sector in preparation for deregulation. This is the result of government plans to convert the Mombassa port to landlord port[16].

Generally, everything is in place for the regulation of the transport sector in accordance with the law. In practice, however, the laws are at times either inadequate or insufficiently comprehensive or are downright outdated. The government is working towards an integrated national transport policy, by reviewing the existing systems of laws and their enforcement.

3.4 Water Supply

The government has been the sole provider of water services but is now in the process of liberalising the sector, following the enactment of the water Act 2002. The implementation of the Act entails the separation of policy formulation, regulation and service delivery functions. Accordingly the water services regulatory board (WSRB) has been established to carry out the regulation function, while the water services boards will do management and service delivery. All these changes are aimed at providing an enabling framework for the private sector to invest in the water sector. These reforms are expected to enhance national fresh water availability from the current level of 247 cubic metres to 900 cubic metres in 2007.

3.5 Financial Services

The financial services sector is one, which has been open to private participation for quite sometime now. As a result, there is very little presence of public owned institutions. The state

[15] The infrastructure at the port of Mombassa is maintained and upgraded by the Kenya Ports Authority. The Kenya railway is currently the manager and operator of inland water transport.

[16] A landlord port is a widely used model for introducing private provision of services into port operations.

divested from commercial banking operation with the restructuring and privatisation of the National Bank of Kenya and the Kenya Commercial bank in 2001.

The Central Bank of Kenya (CBK) founded in 1966 is the regulatory body for the banking sector. CBK supervises the banking system and formulates and implements the monetary policy. The government has also initiated reforms in the microfinance sectors. It's in the process of developing a legal framework to regulate micro finance institutions and SACCOs. Once the legal framework is in place large SACCOS effectively collecting deposits from the public and with front office service areas will be subjected to licensing standards and prudential regulation by the central bank. However very little progress has been made on this as the microfinance bill is yet to be passed by the parliament to become a law.

In the 1980s, the Government of Kenya realized the need to design and implement policy reforms to foster sustainable economic development with an efficient and stable financial system. It had become evident that the commercial banks could not support and sustain a desirable economic development because they could not offer the necessary long-term credit. A study undertaken by the Central Bank of Kenya and the International Finance Corporation became the blueprint for structural reforms in the financial markets and ultimately led to the establishment of the Capital Markets Authority (CMA) in 1990 to promote, regulate and facilitate the development of an orderly, fair and efficient capital market in Kenya. Before the CMA, the Capital Issues Committee at the Treasury regulated the capital market.

In the insurance sector, the Treasury and Kenya Reinsurance undertook regulation till 1987 when the Commissioner of Insurance was appointed to regulate this sector. The commissioner, subject to the directions of the minister, is responsible for the administration and performance of all functions of regulating the industry. The sector has several locally owned and multinational companies but regulatory structures are weak and the sector is vulnerable to mal-practices. In recent years, Kenya has witnessed the collapse of many public service vehicles and medical insurers. Realizing this, the government has set up a task force to speed up the formation of an authority to regulate the insurance business.

The Treasury was responsible for regulating the retirement benefits schemes until 1997 when the Retirement Benefits Authority (RBA) was formed to regulate this sector. The creation of the RBA is part of the ongoing financial reform process in Kenya's economy geared at mobilizing domestic savings, developing the country's capital markets and enhancing economic development. The role of the RBA is similar to that of the Central Bank in the banking sector or the Capital Markets Authority in the capital market.

In brief…

The establishment of sector-specific regulatory bodies is still evolving in Kenya. Regulatory agencies have recently been established in seaports, civil aviation, and water supply; in road transport, it has been revived; and in insurance it is being overhauled. The primary motive for establishing regulatory agencies has been to facilitate entry of private investment, and separate policy-making, regulation and commercial operations.

As part of regulatory reforms, the government has sought to preserve the monopoly of state-owned service providers in telecom and electricity sector, (i.e. of TKL and KPLC, respectively); while in air services a private monopoly has been created. In all the three cases, consumers and the performance of the sector has taken a beating. In telecom, technology (in the form of mobile phones) came to the rescue of consumers, but there was no such respite for consumers in the other two sectors. In railways, private sector monopoly is set for creation. The government

needs to learn lesson from the experience of creating a private monopoly in air-transport services, and put in place proper regulatory framework to ensure that private monopoly does not abuse its position.

4. Evaluation of Sectoral Regulatory Framework

In this section, we do a preliminary review of the regulatory framework in select sectors with regard to institutional and governance aspects, such as regulatory institutional design in a sector, appointment to regulatory bodies, regulatory mandate and its enforcement, funding of regulatory agencies, staffing and training, accountability mechanism, interface with other agencies, and decision making process. This preliminary review would help in assessing the nature and effectiveness of the regulatory framework that is evolving in Kenya.

4.1 Regulatory Institutional Framework

The regulatory institutional structure in select sectors is summarised in table 2.1

Table 2.1 Regulatory Institutional Framework in Kenya

Sector	Enabling Legislation	Regulatory Body	Appellate Body	Other Agency and its role	
Telecommunications	Kenya Communications Act, 1999	Communications Commission of Kenya	Communications Appeals Tribunal	National Communications Secretariat	Policy advisory body within the ministry
Electricity	Electric Power Act, 1997	Electricity Regulatory Board	Minister for Energy		
Road Transport	Transport Licensing Act, 1962	Transport Licensing Board	Appeals Tribunal	Kenya Roads Board	Operations and management of national highways
Civil Aviation	Civil Aviation (Amendment) Act, 2002	Kenya Civil Aviation Authority	An appeals tribunal can be established by the minister	Kenya Airports Authority	Operations and management of airports
				Director General of Civil Aviation	Planning and maintaining air navigation facilities
Railways	Kenya railways corporation Act chapter 397	Ministry of Transport	-	-	-
Seaports	President Executive Order, March 2005	Kenya Maritime Authority	-	Kenya Ports Authority	Operations and development of seaports
Water Supply	Water Act, 2002	Water Services Regulatory Board	Water Appeals Board	Water Services Board and Water and Sanitation Companies	Management & service delivery
Banking	Central Bank of Kenya Act, 1966	Central Bank of Kenya			
Capital Markets	Capital Markets Act, 1990	Capital Markets Authority	Capital Markets Tribunal		
Retirement	Retirement	Retirement	Appeals Tribunal		

Sector	Enabling Legislation	Regulatory Body	Appellate Body	Other Agency and its role	
Benefits	Benefits Act, 1997	Benefits Authority			
Insurance	The insurance Act chapter 487 1988	Commissioner of Insurance (within the Ministry of Finance)	An Appeals tribunal can be established by the minister through a gazette notice	Association of Kenya insurers	Operations and managements of the insurers especially on price setting and guidelines

With the exception of railways, measures have been taken in all other sectors to separate policy making and regulatory functions. In railways, the ministry of transport performs the regulatory functions.

All sectoral regulatory bodies, except the Commissioner of Insurance have been established as specialised agencies, outside of government. Separate legislations have been passed for the creation of these regulatory bodies, though the Kenya Maritime Authority (KMA) has been created through an executive order issued by the President. A bill is likely to be put before the National Assembly towards end 2005 setting out the details of the KMA's duties and responsibilities.

In insurance, regulatory function is performed by the Commissioner of Insurance, a department within the Ministry of Finance. Given its weakness in performing regulatory functions (see Box 2.3), the government has recently taken steps towards establishing a separate authority for regulating the insurance business.

Telecommunications, road transport, water supply, capital market and retirement benefits are the sectors where a specialized appellate tribunal has been established. Interestingly, in the electricity sector, the minister of energy is empowered to settle appeals against decisions of the ERB.

As opposed to other sectoral regulators, which are established as autonomous agencies by their respective acts, the Electricity Regulatory Board (ERB) and the Kenya Civil Aviation Authority (KCAA) are not autonomous due to their establishment as state corporations. This implies they are also subject to the provisions of the State Corporations Act, which provides for the dissolution of a state corporation, dismissal of a board member or even the entire board by the President. Further, the State Corporation Act places the two regulatory bodies under the purview of their respective line ministries. This legal arrangement imposes limitation on the autonomy of the two regulatory bodies. Hence, it is apparent that despite the provisions in their respective legislations, the autonomy of ERB and KCAA is limited.

4.2 Management Structure and Selection Mechanism

Though the government of Kenya has taken steps to separate regulatory functions from policy formulation and bestow it in a specialized agency, the selection of people to man these agencies is heavily influenced by the line minister (Table 2.2), which significantly undermines their functional independence. The role of the minister in selection and removal came out powerfully when the Minister of Communications (MoC) suspended the CCK board in March 2005 and sent the then director general on leave (Box 2.1).

Box 2.1 Minister Disbands Communications Commission of Kenya (CCK)

In March 2005, the Minister of Communications suspended the CCK board alleging the board of impropriety, particularly in the award of license for the third mobile operator, which is still being battled out in the court, and in the tendering for the second national fixed operator license, which was later cancelled by the Minister.

After disbanding the board, the government appointed an acting Director-General from a Ministerial Department. This was in contrast to the appointments of the outgoing DG and Commissioner, both of who were earlier appointed from outside the government. This step paved the way for appointments from within the government, casting shadow on government's commitment towards providing an independent regulator, as mandated by the Communications Act. The board was later re-constituted in May 2005.

The new CCK Director General is the former Managing Director of Telkom Kenya. Swapping positions, the outgoing CCK Director-General was made the Managing Director of Telkom Kenya. Moreover, the new Chairman of CCK, prior to his appointment, was the Chairman of the Postal Corporation of Kenya (PCK), the public postal utility. Again swapping positions, the outgoing Chairman of CCK, has been made the Chairman of PCK.

As per information available, remuneration, allowances, etc of the members of Communications Commission of Kenya, Communications Appeals Tribunal, Capital Markets Authority, Capital Markets Tribunal, and Retirement Benefits Authority are determined by the respective line ministers. This further undermines the independence of these bodies at the hands of the line minister.

Except the electricity sector, no other sectoral legislation has provisions for appointment of representatives of stakeholderson the board of the regulatory body. Though a good step, the Electric Power Act is surprisingly silent on the appointment of a representative of consumers on the board of the ERB. Thus, an important stakeholder group is not represented on the ERB board.

Table 2.2 Selection Mechanism for Regulatory Agencies in Kenya

Regulatory Agency	Number of board members	Members and their appointment				Salary, allowances, etc of Members
		Chairman	Person responsible for day-to-day management	Permanent Secretaries from related Ministries	Members with expertise in related matters	
Communications Commission of Kenya (CCK)	11	Chairman (*appointed by President*)	Director General (*appointed by Minister*)	4 (PS in Ministries of Communications; Finance; Internal Security; Information & Broadcasting)	5 other members (*appointed by Minister*)	Determined by line minister
Communications Appeals Tribunal	3	Chairman (*appointed by Minister in consultation with Attorney General*)	-	-	2 other members (*appointed by Minister in consultation with Attorney General*)	Determined by line minister
Electricity Regulatory Board (ERB)	7	Chairman (*appointed by President*)	Executive chairman	1 (PS in Ministry of Energy)	2 representative of private sector; 1 each to represent workers, employers, and manufacturers (*appointed by Minister*)	Determined by line minister
Transport Licensing Board (TLB)	9	Chairman (*appointed by President*)	Chairman	-	8 members to represent Nairobi area and each of the 7 provinces (*appointed by Minister*)	Determined by line minister
Transport Appeals Tribunal	5	Chairman (*appointed by President*)	-		4 other members (*appointed by Minister*)	Determined by line minister
Kenya Civil Aviation Authority (KCAA)	9	Chairman (*appointed by President*)	Managing Director (*appointed by Minister in consultation with KCAA board*)	3 (PS in Ministries of Transport; Finance; Internal Security)	MD of Tourism Board; 3 other members (*appointed by Minister*)	Determined by line minister
Kenya Airports Authority (KAA)	6	Chairman (*appointed by President*)	Managing Director (*appointed by Minister in consultation with KAA board*)	2 (PS in Ministry of Transport; PS to Treasury)	2 other members (*appointed by Minister*)	Determined by line minister

Regulatory Agency	Number of board members	Members and their appointment				Salary, allowances, etc of Members
		Chairman	Person responsible for day-to-day management	Permanent Secretaries from related Ministries	Members with expertise in related matters	
Kenya Maritime Authority (KMA)	11	Chairman (*appointed by President*)	Director General (*appointed by Minister in consultation with KMA board*)	2 (PS in Ministries of Transport; Finance)	Attorney General; 6 other members (*appointed by Minister*)	Determined by line minister
Water Services Regulatory Board (WSRB)	11	Chairman (*appointed by President*)	Chief Executive (*appointed by WSRB board with Minister's approval*)	-	10 other members (*appointed by Minister*)	Determined by line minister
Water Appeals Board	3	Chairman (*appointed by President on recommendation of the Chief Justice*)			2 other members (*appointed by President*)	Determined by line minister
Central Bank of Kenya (CBK)	8	Governor (*appointed by President in consultation with Minister*)	Governor	1 (PS to Treasury)	Deputy Governor; 5 other members (*appointed by President in consultation with Minister*)	Determined by President
Capital Markets Authority (CMA)	11	Chairman (*appointed by President in consultation with Minister*)	Chief Executive (*appointed by President in consultation with Minister*)	1 (PS to Treasury)	CBK Governor; Attorney General; 6 other members (*appointed by Minister*)	Determined by line minister
Capital Markets Tribunal	5	Chairman (*appointed by Minister*)	Chief executive	-	4 other members (*appointed by Minister*)	Determined by line minister
Retirement Benefits Authority (RBA)	10	Chairman (*appointed by Minister*)	Chief Executive (*appointed by RBA board in consultation with Minister*)	1 (PS in Ministry of Finance)	Commissioner of Insurance; Chief Executive of CMA; 5 other members	Determined by line minister
Appeals Tribunal (for RBA)	5	Chairman (*appointed by Minister*)	Chairman	-	4 other members (*appointed by Minister*)	Determined by line minister

4.3 Financial Resources

In terms of mode of funding regulatory agencies, Kenya is observed to be following different approaches:

- Financial autonomy has been provided to the Communications Commission of Kenya, Kenya Civil Aviation Authority, Kenya Airports Authority, Kenya Ports Authority, Central Bank of Kenya, and Capital Markets Authority. These regulatory bodies are empowered to raise resources on their own to finance their operations.
- Certain regulatory bodies are funded from the government's budget. These are Transport Licensing Board (TLB), and Commissioner of Insurance. Even though TLB collects license fees, the amount collected is remitted to the exchequer, which is not obliged to pass over the same to the TLB. The TLB is made to rely on government financing.
- Electricity Regulatory Board and Retirement Benefits Authority are funded from levies/fees, etc. i.e. from resources independent of government's budget, but the levy is determined by the line minister concerned.
- Kenya Maritime Authority (KMA) and Water Services Regulatory Board (WSRB) are funded from Parliament appropriations. However, in both cases the money available is heavily influenced by the line minister concerned. In case of KMA, the budget estimate is itself approved by the Minister, whereas in case of WSRB, the money is provided at the discretion of the Minister in the form of grants, loans or subsidies.

Table 2.3 Funding Arrangements for Regulatory Agencies in Kenya

Regulatory Agency	Mode of Financing	Approving Agency
Communications Commission of Kenya	Levy/fees (annual license fees, spectrum fees)	• Budget estimates prepared and approved by the CCK board • CCK empowered to prescribe levy/fees
Electricity Regulatory Board	Levy imposed on electricity sales	• Budget estimates prepared by ERB board; approved by Minister of Energy • Levy determined by Minister
Transport Licensing Board	Government's budget	-
Kenya Civil Aviation Authority	Revenues collected from licensing of air services	• Budget estimates are prepared by the board • The authority determines fees and charges
Kenya Airports Authority	Revenues collected from provision of various services	• Budget estimates are prepared by the board • The authority determines rates and charges
Kenya Maritime Authority	Parliament appropriations	• Budget estimates prepared by KMA board; approved by Minister of Transport
Water Services Regulatory Board	Parliament appropriations, but money provided at the discretion of Minister	• Minister, out of the money provided by parliament, provides funds in the form of grants, loans or subsidies
Central Bank of Kenya	Net profits of the bank	The board prepares budget estimates

Regulatory Agency	Mode of Financing	Approving Agency
Capital Markets Authority	General fund primarily consisting of fees charged	• Fees, etc. determined by the CMA
Retirement Benefits Authority	Retirement benefits levy; grants made by Minister out of Parliament appropriations	• Budget estimates prepared and approved by RBA board; but any increase in estimates subject to Minister's approval • Levy determined and imposed by the Minister in consultation with the RBA board
Commissioner of Insurance	Government's budget	• Part of Ministry of Finance budget

In case of regulatory bodies that are given financial autonomy, two issues arise immediately. One, their autonomy may be impaired because of the fact that the line minister plays a significant role in the selection/appointment of people who take the decision regarding budget. Secondly, a concern often cited in empowering regulator to impose fees for financing its operations is that the regulator might misuse the power and over-charge consumers. There are, in fact, such complaints against the Communications Communication of Kenya (CCK).

At present CCK imposes a flat levy on consumers to finance its operations. With a flat levy rate, the observed increase in consumer population (considering the observed growth in number of mobile telephone consumers) has meant that the levy generates more money than CCK initially budgeted for. A concern being expressed in this regard is that Kenyan consumers are being subjected to charges, which gives the CCK funds far in excess of its planned budget requirements. Failure to build effective controls and transparency in these levies encourages overcharging of customers while other regulators are also encouraged to seek similar levies[17].

An alternative (on another extreme, though) to this funding arrangement is that levies are determined and imposed by the line minister concerned – a practice followed in the case of Electricity Regulatory Board (ERB) and Retirement Benefits Authority (RBA). However, the power vested on the line minister to decide the levy seriously undermines the financial independence of the two regulatory bodies.

Financing a regulatory body through imposition of levy/fee is considered prudent, since appropriation of a regulator's budget by Parliament is considered inappropriate in the Kenyan context because of national budgetary constraints. In fact, the ERB funding through the levy was decided upon due to this reason. The financing through the levy provides more than would otherwise be available by appropriations by the parliament. However, the Kenyan government does not seem to have put proper arrangements in place, which provide financial autonomy to a regulatory body and simultaneously ensures that this autonomy is not misused.

4.4 Staffing and Training

Regulatory bodies in Kenya are observed to put emphasis on providing training to their staff (table 2.4). Regulators also have the powers to appoint their own staff.

[17] Source: www.idasa.org.za/gbOutputFiles. asp?WriteContent=Y&RID=843

There seems to be apathy towards the functioning of the Transport Licensing Board (TLB). The TLB is in existence for the past over four decades, but it still has neither its own staff nor its own office space. It uses the staff of Kenya revenue authority (KRA) to assist in its work. In fact, the chairman of the TLB board sits in the KRA building.

The Water Services Regulatory Board and the Kenya Maritime Authority are currently in the process of recruiting staff and their staff structure is still evolving. The Capital Markets Authority (CMA) maintains a policy of attracting and retaining a small multidimensional team of professionals and administrative staff.

Table 2.4 Staffing and Training in Regulatory Agencies in Kenya

Regulatory Agency	Number of staff	Training	Power to appoint staff
Communications Commission of Kenya	130	Staff exposed to training; short visits to other ICT regulators	CCK Board
Electricity Regulatory Board	30	Staff exposed to training	ERB Board
Transport Licensing Board	No staff of its own	-	-
Kenya Civil Aviation Authority	650	Staff exposed to training	KCAA Board
Kenya Airports Authority	3000	Staff exposed to training	KAA Board
Central Bank of Kenya	1300	Has a college to train staff; staff exposed to other training as well	Governor appoints staff in accordance with service conditions established by board
Capital Markets Authority	30	Staff exposed to training	CMA board
Retirement Benefits Authority	38	Staff exposed to training	RBA board

4.5 Regulatory Mandate and Enforcement

Telecommunications

The Communications Act assigns the followings functions to the Communications Commission of Kenya (CCK):

- Licensing
- Price regulation
- Frequency management (Allocation & Monitoring)
- Establishment of interconnection principles

The Commission is charged with the expansion of telecom service nationally under a universal obligation scheme. The Act vests CCK with adjudicative powers in the discharge of its statutory mandate. CCK is expected to promote, develop and enforce fair competition and equality of treatment among all licensees relating to communications. The Commission has the power to settle disputes between licensees of communications services, including disputes relating to interconnection and frequency coordination. Any person, aggrieved by the decision of the Commission, can appeal to the Communications Appeals Tribunal.

Kenya's telecommunications sector, nevertheless, remains under state control. According to the Communications Act, the Minister of Communications (MOC), in consultation with CCK prepares regulations, which provides guidelines on issues such as interconnection, pricing and dispute resolution, among others. The MoC is empowered to give policy directives to the CCK. Moreover, cases of micro-management by the ministry have come to light. One such case relates to the licensing of a second national operator (SNO). CCK adjudicated on tenders for the SNO but the licensing has run into a roadblock. The MoC stopped the announcement of the winning bidder on the grounds of alleged irregularities in a recommendation by the regulator to lower the minimum bid price from US$50mn to US$25mn. The matter is still being contested in court. This pits the regulator against the government and has the potential to threaten regulatory independence.

The role of the minister in the regulatory functioning of the CCK came out powerfully when the minister suspended the CCK's board in March 2005 and sent the then director general on leave (see box 2.1). Interestingly government's decision followed a ruling given by CCK, a day before, ordering Telkom Kenya to restore its Voice Over Internet Protocol (VoIP) services that were suspended in February 2004. The Minister's action surprised many as the CCK had grown to become a beckon of hope for the regulatory institutions in Africa, also reflected in its DG's appointment as the Chairman of the International Telecommunications Union (ITU) Council. The industry alleged that the Minister took the decision because CCK was handling various disputes involving Telkom Kenya (the state-owned incumbent) and some of these rulings had been made against the parastatal instructing it to stop it's anti-competitive practice.

Regulatory Enforcement vis-à-vis Public Sector Incumbent

Save for some quality of service indicators, Telkom Kenya Ltd. (TKL) has failed to meet all its license obligations. It has also been found violating its licence conditions. Accordingly, in the fully exercise of its regulatory powers CCK has given necessary directions to TKL and also levied penalties on the state-owned incumbent. But the actions of the CCK have not been effective, as TKL has not complied with its orders/directives.

Failure of CCK to take any further action is a sign of weak regulatory enforcement vis-à-vis the state-owned incumbent.

Box 2.2 CCK (the Regulator) directs, Telkom Kenya (the SOE incumbent) disregards

Case 1

CCK fined TKL a sum of KSh110m (approximately US$1.41mn) for failing to comply with conditions for its various trade licenses for 2001-02. TKL has not paid the money, claiming unaffordability and appealing that the targets were unrealistic in the first place.

Case 2

In another development, relating to a dispute between TKL and ISPs in 2004, the regulator gave a ruling against TKL. The ISPs had complained that TKL was providing direct internet access to end users bundled with infrastructure (dial up services), which was anti-competitive and unfair. The Commission held that Telkom Kenya had contravened licence conditions in its international Internet Backbone services licence and instructed Telkom Kenya to cease the provision of bundled services and provide Internet services to end users through its ISP subsidiary, Jambonet.

Though TKL is yet to comply with this ruling, the ISPs approached the regulator with another complain relating to yet another anti-competitive practice of TKL. This is about TKL's decision

of increasing bandwidth prices for ISPs by as much as 160 percent starting September 2004. Evidently, TKL is applying market skimming tactics during the period when its pricing has been decontrolled, but before competition sets in. This case is going to be another test of regulatory efficacy.

Tariff Regulations

In the fixed network service segment, CCK regulates the tariffs of Telkom Kenya. For the period of exclusivity (July 1999 to June 2004), TKL was required to rebalance its tariffs to ensure that prices charged reflect the real cost of service provision and any cross-subsidies between local, long-distance and international telecommunications services are eliminated. After the expiry of the monopoly period, a price-cap method is being used to arrive at charges for fixed services. All these charges are to be filed with the Commission for its approval. In mobile services, competitive forces are expected to align prices. Anyhow, mobile operators are required to present their prices to the Commission before these are applied.

Consumer Protection

CCK is the watchdog of consumer; making sure that standards of quality are maintained in both services and equipment provided. Providers of communications services are required to provide effective mechanisms for addressing consumer complaints. If the complaint is not solved, the consumer can approach the Commission, which has the power to settle any disputes between a licensee and a subscriber or a class of subscribers.

The regulator has taken several steps to promote consumer interests and protect consumers from abusive practices of service providers. For instance, in March 2002, CCK suspended a 300 percent tariff increase proposed by the Cyber Café Operators Association of Kenya (CCOAK). As a mark of regulator's successful action, internet access charges in Cyber Café has dropped from a high of almost KSh 15 per minute in 1999 to about KSh 3 per minute in 2002, to only KSh 1 per minute in 2003 and KSh 0.08 per minute in many places.

Electricity

The Electric Power Act empowers the Board to:

- Set, review and adjust transmission and distribution tariffs
- Approve electric power purchase contracts and transmission and distribution service contracts
- Enforce environmental, health and safety regulations in the power sector

The Act empowers the Electricity Regulatory Board (ERB) to make rules and regulations governing tariffs, quality of service standards, obligations to supply, etc. ERB is expected to promote competition in the electricity sector, where feasible. ERB is empowered to investigate complaints made by, and mediate disputes between parties.

There is however deficiency in terms of empowerment of the ERB to fulfill its stated functions. With regard to licensing, ERB's role is advisory to the Minister. Further, the Minister is empowered to impose fines on the licensee upon advice by the ERB and there is no provision for recourse if the Minister fails to act on these advices.

In certain instances, there are commensurate provisions in the Electric Power Act to enable the ERB execute some of its functions. For example, there is a provision for the ERB to reduce tariffs, after carrying out investigations, if the proposed increases are not justified in the

application. However, there are no specific provisions for enforcement of environmental and safety standards in the EPA.

Tariff Regulation

With respect to setting of tariffs, ERB approves power purchase contracts between KenGen and KPLC and also approves and sets the retail tariffs between KPLC and consumers. Since inception ERB has undertaken one tariff setting exercise in August 1999 and a tariff review in May 2000. The latter was in response to the unprecedented capacity crisis of 1999-2001. ERB publishes retail electricity tariffs review policy aimed at establishing open, fair and transparent regulatory framework.

Consumer Protection

ERB has a full-fledged department that handles all issues related to electricity consumers. The board protects the consumer interest, which includes conducting investigations and hearings, and monitoring levels of service delivery by regulated utilities. However, political interference in ERB's functioning limits consumers' ability to effectively apply the existing provisions for consumer protection. Efforts by consumer organisations to effectively influence the deliberations leading to adjustments of electricity tariffs did not bear fruit until 2002 when the upward tariff adjustments, requested by the KPLC, was suspended.

Transportation

The Transport Licensing Board (TLB) has the powers to licence transport operators. TLB can grant or refuse any application for license or grant license subject to such conditions as it may see fit to impose. However, other than this function, TLB is deprived of certain other mandates, which a regulator should typically have to ensure proper regulation. Thus, TLB does not have the mandate to regulate tariffs. It neither sets tariffs nor does it regulate them, resulting in constant hiking of fares. TLB doesn't prepare road transport plans such as the number of public vehicles plying on each route (required to ensure all routes are served). It is also not empowered to specify service and vehicle standards. TLB lacks institutional autonomy for decision-making considering that its decisions are subject to ratification by the government.

In regards to the development of the road transport services, the minister's role is quite pronounced. The role of the minister was felt when the former minister for transport imposed new rules for fixing speed governors and safety belts in what came to be known as the 'Michuki' rules. In this case the role of TLB was confined to just enforcing of rules. TLB could not issue licenses to vehicles that had not passed the government inspectorate, which was required to certify that the vehicles have been fitted with speed governors and safety belts.

The Kenya airports authority has been established as a corporate body under the Kenya Airports Act. The authority constructs, operates and maintains aerodromes and other related facilities, and determines and imposes charges/fees for the services provided.

The Kenya civil aviation authority's main role is to facilitate sound development of the civil aviation industry in Kenya and implement related government policies. It has been given the powers to grant licenses for provision of air services. The authority provides air navigation services, ensures safety and is responsible for technical regulation of civil aviation.

Kenya ports authority (KPA) is responsible for the construction, maintenance, upkeep and operation of ports. Before the establishment of the Kenya Maritime Authority, KPA was performing the regulatory functions as well. The Kenya Maritime Authority (KMA) has been

established to administer and enforce the shipping Act and other legislations relating to the maritime sector. The regulatory functions of KPA has been de-linked and passed on to the KMA. KMA coordinates the implementation of policies relating to maritime affairs and promotes the integration of such policies into the national development plan. The Act, however, provides for the minister to make regulations for carrying into effect the provisions of this Act.

Water Supply

The water services regulatory board (WSRB) issues licences for the provision of water services. It determines standards for the provision of water services and monitors compliance of established standards. The board develops guidelines for the fixing of tariffs for water services. It has established procedures for handling complaints made by consumers against licensees. It is empowered to determine fees, levies, premiums and other charges in accordance with the national water services strategy. Be that as it may, the enforcement of water services regulatory board's powers and functions are subject to the directions of the minister.

Financial Services

The Central Bank of Kenya (CBK) regulates the banking and financial institutions under the Central Bank of Kenya Act. The principal objective of the Bank is to formulate and implement monetary policy directed at achieving and maintaining stability of the financial system. The CBK is empowered to formulate and implement foreign exchange policy; license and supervise authorized dealers; formulate and implement such policies as best to promote the establishment, regulation and supervision of efficient and effective payment, clearing and settlement systems; act as a banker and adviser to and as fiscal agent of the government; and issue currency notes and coins.

As per the Banking Act, no institution can increase its rate of banking or other charges except with the prior approval of the minister, who consults the central bank in the exercise of his functions. In 1991, the interest rates charged by commercial banks in Kenya were decontrolled, enabling them to fix their own interest rates. However, commercial banks (local as well as multinational) were found to charge almost similar rates, which were viewed as unjustifiably high pointing towards the existence of collusion. This evidence was followed by amendments to the Central Bank Act, which came into force in August 2001, reinstating regulation on interest rates charged by commercial banks.

The CBK is empowered to act upon misleading information or advertisement. Interestingly, the Act empowers the Minister for Finance to approve mergers and takeovers in the banking sector.

The Government is currently looking into new regulations to strengthen the supervisory and enforcement capacity of the CBK by transferring the Banking Disciplinary Authority from the Ministry of Finance to the CBK. In the pipeline is the development of a legal framework to regulate micro finance institutions and savings and credit cooperatives (SACCOs). The objective is to compel larger SACCOs who collect deposits from the public to be subjected to rigorous form of licensing standards and prudential regulations by the CBK.

The Commissioner of Insurance, within the Ministry of Finance, is charged with administering the Insurance Act and advises the government on policy matters regarding insurance. Its mandate is to regulate and develop the insurance industry in Kenya.

Box 2.3 Kenya Insurance Sector: A Case of Regulatory Failure

Presently, the insurance industry in Kenya serves more like a cartel, through the Association of Kenya Insurance. In October 2002 the Association issued a circular to its members to increase premiums across the board ranging from 20 to 50 percent, with a reason that they were tired of price wars in the industry. Those caught undercutting were to suffer severe penalties. The commissioner of insurance did not take any action to protect consumers as regards pricing fixing or even the performance of insurance industry players.

The commissioner is observed to have failed in effectively regulating the industry following the collapse of United Insurance Co. Ltd., one of the oldest passenger vehicles underwriters. The company collapsed with billions of claims that date back to early 1990's. In fact, the company had been collecting premiums from members of the public with no action or warning from the commissioner. There has been a realization of the need to review the regulation of the insurance industry and speed up the formation of an authority to regulate the insurance business. Stakeholders such as the Institute of Certified Public Accountants of Kenya complain that the commissioner has failed to ensure that insurance companies comply with international financial reporting standards.

The primary objective of the Retirement Benefits Authority (RBA) is to protect the interest of members and sponsors of schemes, to develop the sector and to alleviate old age poverty through enhanced saving for retirement. Prior to the creation of the RBA there was no harmonised legal framework governing the sector. This resulted in the well documented cases of mis-appropriation of scheme funds, dubious investments of member's funds, denial of benefits to members, delay in payments of benefits to members and a myriad of other ills that bedeviled the sector. The RBA seeks to create competition among the various players in the pension sector.

The Capital Markets Authority has been established to promote, regulate and facilitate the development of an orderly, fair and efficient capital markets in Kenya. It ensures the development and maintenance of an appropriate legal and regulatory framework to boost investor confidence, enhance efficiency and create and maintain a fair and orderly market. The authority reviews existing policies and makes recommendations to the government on new policy issues that could promote and enhance market development. It also provides guidance to market operators.

4.6 Interface with Competition Authority

There is a concern that some regulators have developed a culture of egotistical independence leading to regulatory competition. A recent example is where the Association of Kenya Insurers issued a circular to its members to increase premiums across the board in order to bring an end to the price wars in the industry. The indulgence of the Monopolies and Prices Commission (MPC), country's competition authority in trying to resolve this matter was taken as an infringement of the powers bestowed upon the Commissioner of Insurance.

Nevertheless, MPC and other sector regulators, in an effort to circumvent the problem created by information asymmetry have continued to share information instead of relying on information provided for by the industry. This has helped to reduce informational rent enjoyed by the industry. Secondly, it has helped reduce the economic costs of regulation: - (1) the costs of directly administering the regulatory system and; (2) the compliance costs of regulation.

In Kenya, quite often, the laws creating sector regulators contain a portion dealing with competition in the sector with no deliberate harmonization of the role of MPC and the sector regulators. However, there are some indications that sector regulators, although not obliged, are increasingly consulting with the MPC. For example, in the area of mergers and takeovers, the Central Bank of Kenya liaises with the MPC. The Civil Aviation Authority has been liaising with MPC in the area of restrictive trade practices. The Communication Commission of Kenya has also been cooperating with the MPC in the investigation of restrictive trade practices and in the area of mergers and takeovers. The Capital Markets Authority cooperates with the MPC in matters concerning listed companies.

4.7 Decision making Process

Telecommunications

Communications Commission of Kenya (CCK) recognises the need for consulting with the stakeholders on various issues. A link is provided on CCK's website to invite inputs from stakeholders. Consultation on certain issues has been mandated by the Act itself. For instance, after an application for the grant of a license is lodged with the Commission, the Act requires the Commission to give notice to the public of the intention to grant the license and asking for written representations or objections in respect of the proposed license.

Electricity

The Electricity Regulatory Board (ERB) after consulting with the stakeholders forwards its recommendations to the minister on related issues. It conducts regular stakeholders meeting to deliberate on matters affecting electric power regulation and holds public hearings on objections to tariff adjustment. The ERB is presently consulting stakeholders on retail electricity tariffs review policy 2005 and has published it severally in the locally dailies and on its website for public participation.

Transportation

The board members of Kenya Civil Aviation Authority (KCAA) and Kenya Airports Authority (KAA) are required to make proposals to the minister after consulting with stakeholders. Currently the KCAA is inviting comments on its new Kenya civil aviation regulations from stakeholders and members of public. The Transport Licensing Board (TLB) decision to issue licenses rests solely on the board. Kenya maritime authority is required to make its decisions after consulting with the minister.

Water Supply

The Water Services Regulatory Board (WSRB) liaises with water services board and water services providers for better regulation and management of water services. The minister formulates water services strategies after public consultations.

Financial Services

There are consultations on monetary policy between the minister of finance and the central bank. In exceptional circumstances, where the minister is of the opinion that the monetary policy adopted by the bank is inconsistent with the principal object of the bank, the minister may, upon resolution by cabinet direct the bank to adopt such monetary policy as the minister may specify. There is presently no mechanism followed to get inputs from stakeholders.

The capital markets authority consults with the minister on all aspects of the development and operation of capital markets. Commissioner of insurance also takes decision after consulting with the minister.

The retirement benefits authority (RBA) makes decisions after consultations with the minister. The stakeholders in the industry are not consulted when decisions are being made. For instance, in 2005 the minister increased the number of years for accessing pension by making it mandatory for people to wait until they are 55 years to access their funds. This decision caused a lot of uproar amongst the contributors but it was not reviewed despite stakeholders feeling their concerns were not represented.

As observed, in most cases, regulatory agencies take decisions in consultation with the Minister concerned. One notable exception to this feature is the Communications Commission of Kenya (CCK). Not surprisingly, in the past this has led to differences between the CCK and the Minister of Communications, leading to the disbanding of the CCK board.

4.8 Accountability Mechanism

The regulatory agencies in Kenya have explicit legal accountability; which is manifested by review and appeals procedures. Further, transparency has been enhanced through open regulatory processes. Decisions and reasons for such decisions are made public.

Table 2.5 Accountability Mechanisms for Regulatory Agencies

Regulatory Agency	Minister/Parliament	Appellate Body
Communications Commission of Kenya	Annual report of activities with audited accounts submitted to Minister, *who tables it before Parliament*	Communications Appeals Tribunal arbitrates on cases where disputes arise between the parties under the Act
Electricity Regulatory Board	Annual report of activities with audited accounts submitted to Minister, *who tables it before Parliament*	Parties aggrieved by the Board's decisions may seek recourse from the Minister for Energy
Kenya Civil Aviation Authority	Annual report of activities submitted to Minister, *who tables it before Parliament*	An appeals tribunal can be established by the minister for which a person aggrieved by the authority can seek recourse
Kenya Airports Authority	Annual report of activities submitted to Minister, *who tables it before Parliament*	The minister may make regulations generally with respect to services performed and functions provided by the authority.
Water Services Regulatory Board	Annual report of activities with audited accounts submitted to Minister, *who tables it before Parliament*	Water appeals board hears appeals against decisions made by regulator
Central Bank of Kenya	Annual report of activities with audited accounts submitted to Minister, *who tables it before Parliamen t*	-
Capital Markets Authority	Audited report submitted to Minister, *who tables it before*	Capital Markets Tribunal to appeal against the decision of the

Regulatory Agency	Minister/Parliament	Appellate Body
	Parliament	CMA
Retirement Benefits Authority	Audited report submitted to Minister, *who tables it before Parliament*	Decisions of the authority are challenged in the Appeals Tribunal

As is observed, all the regulatory bodies are required to submit their annual reports and/or audited accounts to the line minister concerned, who then tables these before the National Assembly. However, the Kenyan Parliament does not seem to be reviewing these reports with the seriousness that is required. The regulator's actions are questioned only when there is an impending crisis or a serious debate in the country. For instance, in 2004 certain Members of Parliament had asked the CCK to respond on the issue of granting the third GSM license, after the financial and technical capability of the prospective licensee's were questioned. The CCK responded that it was satisfied with the licensee's capability to operate the third GSM network, and the matter was resolved. On the other hand, the outcome was different when the Minister of Communications was not satisfied with CCK's functioning, as noted earlier. As a result the entire CCK board was disbanded. This action reflects the weak and inadequate mechanism for proper evaluation of regulator's performance in Kenya. For, if the performance evaluation and accountability mechanisms would have been right, the allegations of corrupt decision making process by the CCK, if any, could have been addressed through this mechanism rather than disbanding of the entire board.

Other than the National Assembly, an appellate body has been established in certain sectors. This provides a check on the decisions taken by the respective regulatory agency. Besides the appellate body, regulator's decision can be appealed by approaching the judiciary.

The situation in the electricity sector in this context is of concern. Parties aggrieved by ERB's decisions may seek recourse from the Minister for Energy, with the High Court of Kenya being the final arbiter. Since the minister in any way has several ways to interfere in the decisions of the ERB, the chances of ERB's decision going against the minister's wishes are low. In addition, making the aggrieved parties appeal to the minister against ERB's decisions, undermines the credibility of the regulatory framework in the electricity sector. This process will be found wanting and unsatisfactory by private investors. Though the aggrieved parties have the option to approach the High Court but then this involves huge transaction cost, besides putting that much strain on the country's judicial system. Moreover, the high court cannot be expected to judge on technicalities of the grievances. Under the circumstances, the new energy bill 2004 is a big step forward, as it allows for a public inquiry to enable review of decisions made by the ERB.

Interestingly, the capital markets authority is already following a similar approach. It has an institutionalised annual review forum, which allows stakeholders to review the progress of the CMA as well as raise any issues or suggestions to help stimulate domestic capital markets.

5. Concluding Remarks

Kenya is undergoing transition from a regime characterised by public sector dominance in different segments of the economy to one marked by privatisation and liberalisation with a view to moving towards a competitive environment. This process has been accompanied by the setting up of regulatory bodies in several sectors to ensure proper market practices.

Given this background, the paper presents the sectoral regulatory framework being followed in Kenya along with a preliminary analysis on its working. It makes an attempt to identify the Kenyan government's approach towards regulation of certain sectors by assessing the extent of space provided to sector regulators to implement their mandate.

Sector regulators in Kenya have been created by separate pieces of legislation. Regulatory agencies are accorded autonomy through legislation. However, the functioning of regulatory agencies in Kenya is largely subject to the wishes of the line minister, who is involved in the regulatory process in one way or the other. This is manifest in the appointment of members to regulatory bodies, mode of funding of regulatory agencies, their (in)ability to enforce regulatory mandate, decision-making process, etc. Thus, separation of policy-making and regulatory functions has not taken place in a true sense in Kenya.

Regulatory decision-making process is not as participatory as it should be in several regulatory agencies. There is, however, improvement on this aspect as seen in the case of the Communications Commission of Kenya (CCK), the Electricity Regulatory Board (ERB), and the Kenya Civil Aviation Authority (KCAA). These regulatory agencies involve stakeholders in the decision-making process, which is a positive feature of Kenya's regulatory framework.

However, the effectiveness of stakeholder participation in regulatory decision-making is doubtful. This is because decisions are, most often, taken in consultation with the line minister concerned. One notable exception is the practice followed by the CCK and the results are evident in the recent friction between the Minister of Communications and the CCK.

While autonomy to regulatory agencies has been provided in a half-hearted manner, accountability mechanisms too are inadequate. Other than the annual reports to the minister, which is then tabled in the National Assembly there is no effective mechanism to judge the performance of sectoral regulatory agencies and make them accountable for their actions. The only exception is the (good) practice followed by the Capital markets authority, which has institutionalised an annual review forum that allows stakeholders to review the working of the authority. There is a need to replicate this practice in other regulatory bodies as well.

As regards interface with the competition authority, regulatory authorities in Kenya have been established without recognising the need for this interface. As a result, industry regulators tend to determine issues of competition law, as they emerge from their industries, without definite recourse to the competition authority. Be that as it may, there are some indications that sector regulators are increasingly consulting the competition authority. This trend needs to be further buttressed by putting in place a formal collaboration mechanism between sector regulators and competition authority.

One of the important tasks to be performed by regulatory agencies is to ensure competitive neutrality between public sector and private sector enterprises. Certain experiences of the application of this principle emerge from the telecommunications and electricity sectors. In both these sectors, the respective regulators have taken certain measures, which adversely affect the interest of the state-owned incumbents. However, in telecommunications, the parastatal (Telkom Kenya) has disregarded regulator's directives. Further, the line minister went to the extreme of disbanding the CCK board (manned by people from outside the government) to later reinstate a new board (manned by people from within the government). This has dealt a severe blow to CCK's credibility. The ERB on its part has recently sought to end the monopoly of the Kenya Power and Lighting Company Ltd. (KPLC) in the distribution segment. The outcome of this recommendation is yet to be seen.

As compared to CCK, ERB enjoys relatively low degree of independence from the line minister. The Minister of Energy determines the financial resources of the ERB, takes decisions on key issues and the role of ERB is advisory in nature. Therefore, it is expected that the relationship between the Minister of Energy and the ERB would be that much cordial in contrast to the friction observed between the Minister of Communications and the erstwhile CCK board.

The Kenya civil aviation authority, established as the air industry regulator, too has not been effective in regulating Kenya Airways, the public sector turned private monopoly on international and regional routes. Railway is set for privatisation and another private monopoly is in the making, however, as yet there is no regulatory framework in place. The government needs to learn from these lessons and ensure a proper regulatory framework which can ensure an orderly growth of the regulated sector.

The several lacunas observed in the sectoral regulatory framework of Kenya are largely systemic in nature. There are a few good practices as noted above, which need to be replicated elsewhere. Most important is the need to ensure government's commitment towards the regulatory reform process, which is severely lacking. Though the government has established regulatory bodies, but has not allowed them to function independently, which has affected their credibility to regulate the sector. There is a need to sensitise the government and other stakeholders concerned about the existing poor state of regulatory framework in Kenya. Consultation with stakeholders and further in-depth research is required to develop a regulatory framework that is suitable to Kenya.

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Chapter III
Regulatory Environment in South Africa

1. Introduction

South Africa is situated at the southern tip of Africa, forming part of the Southern African region and is bordered by Namibia, Botswana, Zimbabwe, Mozambique and Swaziland.

SOUTH AFRICA COUNTRY PROFILE	
Population:	45.3 billion ***
GDP (Current US$):	159.9 billion ***
Per Capita Income: (Current US $)	2,780 (Atlas method)** 10,070 (at PPP.)***
Surface Area:	1.2 million sq. km
Life Expectancy:	48.8 years **
Literacy (%):	86 (of ages 15 and above)**
HDI Rank:	119 ***

Sources:
World Development Indicators Database, World Bank, 2004
Human Development Report Statistics, UNDP, 2004
(**) For the year 2002
(***) For the year 2003

In 1910, South Africa became a self-governing union as a member of the Commonwealth. In 1961, South Africa became a Republic and withdrew from the Commonwealth. The United Nations refused to recognise the Republic for racial discriminations were being made hence began a 30-year period of international isolation. Economic and trade sanctions were imposed on South Africa that served to slow down the economy, to such an extent, that it could no longer survive in isolation.

The 1990s brought a political end to apartheid and ushered in black majority rule. With the first democratic election in 1994 South Africa emerged from three centuries of racially based minority rule. A new constitution came into effect in 1996, and the African National Congress (ANC)-led government undertook a broad legislative programme to address the legacy of apartheid. This included legislation reforming the labour market, health, education, and social services, as well as various measures to promote socio-economic development.

South Africa employs a mixed economy. The Constitution requires that the state take proactive action to ensure that the injustices of the past are overcome in a manner that ensures fairness and equity. State-owned enterprises (SOEs) clearly have a role to play in the process.

Compared with other countries in sub-Saharan Africa, South Africa is both prosperous and large. With only 3 per cent of the surface area, South Africa accounts for approximately 28 percent of gross domestic product and 40 per cent of industrial output of the continent. It has a population of over 45 million people and an annual GDP of US$128 billion. However, it also has one of the highest Gini co-efficients in the world: the poorest 20% of households earn less than 3% of total income and the richest 20% of households earn 65% of total income.

Compared to other emerging economies, South Africa is still characterised by low levels of investment. The investment/GDP ratio decreased from 18 per cent in 1995 to 16 percent in 2002. Foreign direct investment in South Africa remains meagre. In 2002, FDI inflows amounted to $754 million. Conversely, South Africa is the main source of outward FDI in Africa (amounting to $401 million in 2002).

2. Evolution of Economic Policy Regime

During the decade of 1980s, South African government was increasingly under severe resource constraints. State-owned enterprises (SOEs) which were established primarily to strengthen import-substitution industries were incurring losses. Low efficiency of SOEs was one of the sources of criticism of the government. To address this, privatisation of state assets was considered as appropriate policy response and in year 1987 a white paper was issued on Privatisation & Restructuring Policy. However the privatisation drive did not take off and was eventually put on hold during the period of constitutional negotiations. The African National Congress's (ANC's) suspicious of the then government's approach to privatisation and the possible hidden agenda of selling the family silver before a new government could come to power effectively put a halt to these initiatives. As a result, only national steel parastatal, Iscor, was privatised though initially five of such state institutions were to be privatised. Rest of the parastatals were corporatised and the government retained ownership.

In 1994, the post-apartheid government sworn in, which inherited over 300 state-owned enterprises. Majority of parastatals were facing challenges such as capital starvation, over-borrowing, bureaucratic inertia, and managerial stagnation. Penetration rates for basic utilities were low and racially-skewed as well. The ANC government undertook a process of restructuring and liberalisation and announced a Reconstruction and Development Programme (RDP). In June 1996 to tackle a foreign exchange crisis the government released its macroeconomic strategy, known as 'Growth, Employment and Redistribution' (GEAR). Realising the limitations of the import substituting industrialisation approach the South African government has now shifted the focus towards trade liberalisation to promote export-led growth.

The government embarked on a progressive restructuring of state assets i.e. corporatisation and commercialization of state-owned enterprises, and increased private ownership. However, both the business community and organised labour in South Africa criticised the privatisation policy of the government. In response, the government is proceeding very cautiously and the privatisation programme is now euphemistically referred to as "restructuring of state assets". In August 2000, the Department of Public Enterprises published the Policy Framework for an accelerated agenda for the restructuring of State Owned Enterprises. This was observed as a renewed commitment of the government to the privatisation programme.

The South African approach to restructuring and privatisation of state owned enterprises is unique. The general thrust puts more emphasis on the restructuring of the state sector than on privatisation. The government is generally not in favour of full privatisation. Rather partial privatisation has been done through selling equity to "strategic equity partners" and Black Empowerment Groups while government continues to retain a majority interest. The policy is viewed as an outcome of the compulsions of coalition politics.

3. Evolution of Sectoral Regulation

Certain laws in South Africa have fundamental effect on the manner in which proceedings relating to regulation and competition are conducted.

The Bill of Rights, which applies to all law and sets out rights of all people in the country, is considered as cornerstone of democracy in South Africa. It is at this level of the legislative framework that the first examples of regulatory authorities emerge in the form of various

commissions and authorities established to evaluate and monitor some of the issues arising from the Bill of Rights.

The legislation promoting access to information was enacted to give effect to the constitutional right of access to any information held by the State. Coupled with this is a legislation promoting administrative justice that deals with the right of a person to administrative action that is lawful, reasonable and procedurally fair. The preambles of each of these laws refer to transparency, accountability and openness.

The restructuring programme of state-owned enterprises (SOEs) was motivated by several objectives such as, to improve access of historically disadvantaged sections of the population to basic services; to increase efficiency and reduce costs; to reduce public debt through revenues gained from privatisation.

Many of the large SOEs in transport, telecommunications and broadcasting, and energy sectors were either partly privatised or are undergoing a major restructuring. The enterprises those were privatised were granted specified periods of exclusivity in exchange for a contractual commitment to meet specified public service mandates.

In the changed context, new regulatory systems have been established in various sectors including in transport, telecommunications and energy. As far as the sequencing is concerned, establishment of a regulatory regime prior to the restructuring of a public monopoly has become standard practice in South Africa.

Below is given a review of regulatory authorities in select sectors to provide a first order view of the way in which regulatory agencies have been created and institutionalised in South Africa.

3.1 Communications

Historically, telecommunications services were provided by a state owned monopoly i.e. South African Posts & Telecommunications (SAPT), which operated out of the office of the Minister of Transport and Communications. In 1991, the posts and telecommunications functions of SAPT were separated and the telecommunications arm was corporatised. The new entity was called Telkom SA Limited (Telkom), which was owned by the state entirely.

In 1993, the year before the first democratic elections, the government granted two mobile cellular licences to private operators i.e. Vodacom and MTN. The move brought in a great deal of political unhappiness and the government was alleged for unilateral restructuring of the industry.

However, the political negotiations on South Africa's future constitutional dispensation did not focus on telecommunications rather broadcasting was seen as a more urgent political priority. For over forty years broadcasting had been tightly controlled by successive apartheid regimes and the public broadcaster, the South African Broadcasting Corporation (SABC), enjoyed monopoly and was subject to direct governmental interference.

Under the circumstances, the negotiators agreed on the provisions of the Independent Broadcasting Authority Act (the IBA Act) to ensure smoother transition from Apartheid to democracy. The IBA Act introduced a number of changes including a competitive private broadcasting sector, prohibitions on political control over broadcasters, and creation of an independent regulator. The Independent Broadcasting Authority (IBA) was set up in 1994 to regulate broadcasting in the public interest and to ensure fairness and diversity of views.

Till 1994, the black population did not have any ownership in the broadcasting industry. The situation changed considerably after establishment of the regulatory regime. Privatisation of SABC's commercial radio stations and issuance of new commercial radio licences promoted historically disadvantaged groups to own radio stations. During the last decade the regulator (earlier IBA, now ICASA) has helped in transforming the broadcasting sector from state monopoly and censorship regime to a vibrant, competitive and increasingly black-owned & controlled sector.

The transformation of telecommunications regulation took a few years longer than broadcasting. The new government introduced a White Paper on Telecommunications Policy and the Telecommunications Act was enacted in 1996. These policy statements and laws established a framework to separate the regulatory, operational and policy-making functions in the telecommunications sector. The Telecommunications Act introduced far-reaching changes, notably, the establishment of the South African Telecommunications Regulatory Authority (SATRA) as an independent body to regulate telecommunications in public interest. The Telecommunications Act for the first time put the general public interest at the forefront of telecommunications policy emphasising on the provision of telecom services to all South Africans at affordable rates, whilst maintaining high standards for services.

In 1997, the government undertook a policy of managed liberalisation of the telecommunications industry. To achieve increased teledensity in the country the Telecommunications Act provided Telkom with an exclusive license granting it the privilege of being the country's only public switched telecommunications service provider for the next five years. This privilege came with certain roll out obligations. At the same time the government embarked on a partial privatisation of Telkom.

SATRA was assigned with the responsibility to regulate the telecom sector to ensure fair competition amongst industry players and encourage choice for consumers. SATRA determined the contributions by telecom licensees to two funds created to facilitate development of skills of personnel and promotion of access to telecommunication services i.e. the Human Resource Development Fund (HRF) and Universal Service Fund (USF).

In July 2000, the South African government took a major initiative when the broadcasting regulator (IBA) and the telecommunication regulator (SATRA) were merged to form the Independent Communications Authority of South Africa (ICASA). The ICASA Act 2000 provides for the establishment of ICASA to regulate broadcasting and telecommunications in public interest. The ICASA is required to perform the duties and exercise the powers as were provided to IBA and SATRA. The merger of the two regulatory agencies was aimed to facilitate effective and seamless regulation of telecommunications and broadcasting and accommodate the convergence of technologies.

In the new set up, the Department of Communications advises the Minister on policy matters and ICASA has the responsibility of a regulatory watchdog including issuing licences and monitoring compliance with the Act.

3.2 Energy

The South African energy sector includes coal, gas, oil, electricity, nuclear and renewable power, and has historically been at the centre of country's development. South Africa has large coal resources that supply three-quarters of the country's energy. About 40 percent of the entire

electricity generated is from coal. Regulation in terms of market access and price of coal is non-existent and ownership is entirely in private sector.

The petroleum industry in South Africa on the other hand is highly regulated in terms of market access and price. The Minerals and Petroleum Resources Development Act 2002 provides for granting of exploration and production rights and issuance of technical co-operation permits and reconnaissance permits on upstream side by the Petroleum Agency. The Petroleum Agency performs these functions on behalf of the Minister of Minerals and Energy. The downstream industry is controlled by the Petroleum Products Act 1977 and several other industry agreements. The government controls import of petroleum products as well as the ex-refinery gate price, the wholesale margin, and the retail margin. In year 2003, a new Petroleum Products Amendment Bill was tabled in Parliament and draft regulations have been promulgated that specify the procedures to be followed in applying for and issuance of licences. The Director Hydrocarbons in the Department of Minerals and Energy is the licensing authority, designated by the Minister.

In gas sector there was no explicit legislation to regulate the sector until the Gas Act was passed in 2001. The enactment of the Gas Act provides for the establishment of a gas regulator to issue licences for the construction and/or operation of gas transmission, storage and distribution facilities. The Regulator, is however, bound to a prior agreement entered into between the Minister of Trade and Industry and Sasol[18] over the development of a particular gas pipeline. The agreement incorporates exclusive transmission and distribution rights to Sasol in certain geographic areas for a period of 10 years along with limiting third-party access and excluding the regulator from setting or reviewing prices.

Electricity industry was developed in South Africa to meet the power requirements of the booming mining industry. Several power projects were initiated during 1960s and 1970s with the assumption of continued rapid increases in electricity demand. However the pace of capacity addition surpassed the demand for electricity, as a result the national utility was left with large excess capacity during 1980s and 1990s. Excess generation capacity has helped in keeping electricity prices low.

During recent past the demand for electricity has increased significantly and South Africa no more remains a surplus state in generation capacity. The focus of the present government is on increasing the household access to electricity.

The structure of South African electricity supply industry is still along the lines of the traditional public monopoly model. Eskom which was recently converted to a wholly state owned limited company produces 96% of power generated in South Africa, while some of municipalities generate 1.3%, and a small number of private power producers generate 3.1%.

The National Electricity Regulator (NER) was set up in April 1995 with the expectations that regulatory independence would de-politicize tariff-setting and improve the climate for private investment through more transparent and predictable decision-making. The goal was to create competent, professional institution that is independent, works in transparent manner and create economic incentives for improved efficiency and performance.

[18] Sasol is one of the major players in SA's synthetic fuel market. It is the world's largest manufacturer of oil from coal, gasifying the coal and then converting it into a range of liquid fuels and petrochemical feed stocks.

In 2001, the South African Cabinet decided to unbundle the state-owned utility Eskom and sell-off a percentage of its generation assets, and introduce competition in the industry through encouraging private investment. However, none of these decisions was implemented. Ideological resistance to privatisation remains strong in South Africa. State, once again, is reaffirming the development role of national utilities. Many of the stakeholders are in favour of continuing with the public owned Eskom, as is the case with Electricité de France, and to delay the execution of restructuring and so-called reforms as much as possible.

Eskom supplies electricity at the price that is among the lowest in the world and has consistently made a positive return on assets. Reliability and quality of supply are good. The average energy availability from its power stations has increased from 76 per cent in 1991 to 92 per cent in 2000. The proportion of households with access to electricity has increased from 32 per cent in 1996 to 70 percent in 2001. The South African government has re-affirmed Eskom's dominant market position and has made it primarily responsible for new investment.

In 1998 a White Paper on Energy Policy was issued to set out policy objectives for the energy sector. The White Paper recognises the need for South Africa to make optimum use of all its energy sources for the benefit of all South Africans. In this context, the proliferation of energy sub-sector regulators was considered to be a matter of concern. Rationalization of different institutional arrangements and regulatory approaches to electricity, piped-gas and petroleum pipeline was considered desirable to ensure effectiveness, cost efficiency, compliance and promotion of uniform regulatory methodologies and applications.

Accordingly, in November 2005, the government established the National Energy Regulator of South Africa (NERSA) as the regulatory authority for energy sector in terms of the National Energy Regulator Act, 2004. NERSA undertakes the functions of the Gas Regulator as set out in the Gas Act of 2001, the Petroleum Pipelines Regulatory Authority as set out in the Petroleum Pipelines Act of 2003 and the National Electricity Regulator as set out in the Electricity Act of 1987 as amended. While the electricity industry has been regulated for the past ten years, the piped-gas and petroleum pipeline industries in South Africa will be regulated for the first time.

3.3 Transportation

South Africa is characterised by a multi-modal transport system comprising mainly of rail, road, aviation and maritime transport. In transport sector, emphasis is given on safety and standard regulation, however there is lack of economic regulation such as price or revenue regulation; access or interconnection regulation. State owned enterprises provide bulk of the transport services. Private sector participation has been minimal and government departments continue to regulate the sector.

The parastatal Transnet, which is a conglomerate of multi-modal transportation and related services, comprises of thirteen companies and dominates South African transport industry. The Department of Public Enterprises (DPE) owns Transnet and makes decisions on the transport services being offered by Transnet. Interestingly, the Department of Transport hardly has any say in management and operation of Transnet.

The roots of the giant South African transport organization, Transnet, can be traced back to the late 1850's, when railway transport was proposed for the Cape and Natal harbours. In 1910 when South Africa became a self-governing union its planners were adamant that the railways and harbours should be used to unify and develop South Africa's economy. The South African Railways and Harbours administration (SAR&H) was therefore established as an arm of government. In the 1920s, private road operators began to compete with rail causing the

government to enact the first restrictive legislation in an effort to protect their rail investments and the jobs that had been created in the rail industry. The railway administration saw itself as the "national carrier", having a social obligation to provide services to urban and rural communities. With development and diversification of South Africa's economy, railway operators were unable to provide adequate services at competitive rates in certain freight sectors.

During the 1970's the government agreed that the SAR&H should restructure itself along business lines. Integral to the process was a change in the name and image of the organization, which would reflect its new mission as a state business enterprise. In 1981, the country's railway, harbour, road transport, aviation and pipeline operations became known as South African Transport Services (SATS). At the same time, the enterprise was restructured into units and divisions with a strong emphasis on localized management. In April 1990, after 80 years of government and parliamentary control, SATS was given company status and a new limited liability company representing a vast transport network was established with the name of Transnet Limited.

During the decade of 1990s corporatisation and restructuring of Transnet witnessed the establishment of numerous transport agencies such as Airport Company of South Africa (ACSA), Air Traffic and Navigation Services Company (ATNS), and the National Roads Agency (NRA).

A White Paper on National Transport Policy was released in 1996 to capture the policies and strategies in respect of the transport sector in South Africa. It provides for approaches to improve the competitiveness through improved effectiveness and efficiency; and get government to focus on policy, strategy formulation and substantive regulation. The paper mentions about reducing government's direct involvement in operations, infrastructure provision and services and allows for a more competitive environment.

The regulatory environment in transportation is characterised by a fragmented structure with inconsistent levels of safety and economic regulation across sectors. Though the transport sector in South Africa has been corporatised and commercialized to a great extent, it still remains largely unregulated in the economic sense. While no autonomous regulatory agency has been formed, the responsibility of policy formulation and governance is divided between several government departments with little co-ordination. The state owned service providing enterprises are left with the responsibility of self-regulation on economic and safety related aspects.

Presently, the structure of Department of Transport (DoT) in South African consists of three main Benches within the ministry i.e. (i) Bench for Policy, Strategy, and Implementation; (ii) Bench for Regulation and Safety; and (iii) Bench for Corporate Support Services. The mandate of the Policy, Strategy and Implementation Bench includes facilitation, management, development, planning, implementation and monitoring of transport policy and strategy. The Bench for Regulation is responsible to enable, co-ordinate, and promote quality and safety in road traffic; and create an environment which facilitates development of safe, efficient and internationally competitive air transport and maritime industry. The Division on Road Traffic Management is primarily involved in safety and other management related aspects of the industry including financial management, while the Division on Aviation and Maritime Regulation is entrusted to regulate both safety as well as economic aspects. The Corporate Support Services Bench provides support to other Benches in terms of human resource management, communication etc. In practice, the institutional arrangement for the sector as a whole is quite complex.

A relatively specialised form of economic regulation can be observed in the aviation sector where a part-time dedicated regulatory body, the Regulatory Committee (RC), exists to advise the ministry. A transitional regulatory entity is also envisaged in the ports in which separation of ownership is being conducted as part of restructuring to separate the state-owned enterprise, the Ports Authority from its current owner Transnet. A bill has been passed in this regard recently.

Several important issues are to be addressed in relation to future regulatory arrangements in the transport sector, especially related to appropriate institutional arrangements and mechanisms to regulate the ports and railway. This is crucial for the reason that both the sectors are proposed to be restructured.

3.4 Water & Sanitation

The Department of Water Affairs and Forestry (DWAF) has the mandate to ensure meeting effectively the needs of both the people and the economy. Way back, at the onset of apartheid the Republic of South Africa was divided into eleven different "homeland" administrative and political areas. Since the local authorities were managing water resources and services, in the absence of a coherent strategy or guidelines, the division resulted into fragmented approach to service provision. The availability of services in black-population areas was either not there or extremely limited with being maintained poorly.

1994 onwards, the new government set addressing the water supply and sanitation backlog at top priority and a new Department of Water Affairs and Forestry was established. The White Paper on Water Supply and Sanitation Policy 1994 set out the policy for the new Department with specific regard to these services. To execute the approach the government embarked on a major investment programme in 1994 with the aim to provide basic services primarily in poor rural areas. The Department consulted with a range of stakeholders and formulated the Community Water Supply and Sanitation (CWSS) Programme whose primary objective was to extend the access of basic water supply and sanitation services to all people resident in South Africa.

The Constitution of the Republic of South Africa, adopted in 1996, assigned the local government with the responsibility of providing water and sanitation services to all. A range of municipal legislation have been developed and implemented since 1994 to transform the local government. Some of them are the Local Government Municipal Demarcation 1998, the Municipal Structures 1998, the Municipal Structures Amendment Act 2000, and the Municipal Systems Act 2000. However, in the absence of fully developed local government structures, the Department of Water Affairs and Forestry (DWAF) was mandated to ensure that all South Africans have equitable access to water and sanitation services where local government was unable to carry out this mandate.

As noted above, the focus of government regulation has been on expansion of services to meet out universal provision of basic services and little attention has given to economic regulation. Though the existing regulations provide for basic elements, required to establish a framework for practical implementation of economic regulation of water services. Ignorance to economic regulation of water services in South Africa is being attributed to acute budgetary constraints, being faced by the DWAF. Maintaining a desirable trade-off between social and economic objectives has always been challenging for any government, and South Africa is no exception to that.

3.5 Financial Services (Banking, Insurance & Capital Markets)

From regulatory perspective, the financial sector in South Africa is divided into three broad categories i.e. Banking and credit services; Insurance and related services; and Investment

services. Further, within the Investment services a distinction can be made between securities related investment services and non-securities related investment services. The South Africa Reserve Bank (SARB) is responsible to regulate the banking and credit services while the rest two streams fall under the jurisdiction of the Financial Services Board (FSB). Several Offices of Registrars are there to regulate each of the micro-sector within the broad categories discussed above.

Prior to the 1980s, capital requirements were based on simple gearing ratios of capital to assets; off-balance-sheet items were virtually disregarded; and the financial sector components: banks, insurance and the capital markets were regarded as separate species. The regulators were hardly looking beyond the national frontiers despite the fact that a rapid growth in cross-border business was registered. There was little coordination between regulators, and country risk was not taken heed of.

The first steps towards opening the financial sector came about in the 1980s and the process of deregulation started to gain momentum in the 1990s. In 1983, the Registrar of Cooperation was abolished and banks were allowed to compete on price (interest rates). Building Societies had favourable funding benefits from government that effectively resulted in controlled lending and deposit rates until the mid-1980s. The playing field between banks and Building Societies was leveled when the Deposit-taking Institutions Act of 1990 was renamed as Banks Act in 1996.

The FSB was established through enactment of Financial Services Board Act 1990 and supervises the control over the activities of non-banking financial services. The FSB also acts in an advisory capacity to the Minister of Finance. The FSB supervises Long-term and Short-term Insurance, Friendly Societies, Pension Funds, Unit Trust Companies, Stock Exchanges and Financial Markets.

In early 1990s the regulatory regime in financial services transformed rapidly. Increasingly, consumer interests gained importance and were at the centre stage. As a result, corporate governance rules, disclosure requirements, transparency and accountability mechanisms became key concepts in regulation. During the recent decade several constraints to competition have been removed, however certain restrictions have been imposed on foreign banks.

To sum up ….

South Africa is gradually moving towards having specialized and independent institutions to regulate various sectors. The primary purpose of setting up independent regulatory bodies seems to be to facilitate rational decision-making based on economic principles.

Though the sate owned enterprises are being corporatised in most sector however no immediate plans are there to privatise them. Rather, the approach is to strengthen and effectively regulate the state owned enterprises.

Telecommunication and energy are the sectors where independent regulatory bodies have been set up. A specialised body has been constituted within the ministry in aviation sector to advise the ministry on economic regulatory aspects. Ministry in the government still regulates the entire transport sector. Setting up of independent regulatory agency to regulate seaport sector is on anvil.

Though independent regulation has been adopted in South Africa only in recent times, the government is learning out of the experiences. For instance, setting up of multi-sector regulator is the latest trend. The communication and broadcasting regulators have already merged, and the

postal regulator is set to merge with ICASA. National Energy Regulator of South Africa (NERSA) will take charge of entire energy sector from April 2006 to regulate electricity, piped-gas, and petroleum pipeline sectors. A proposal to merge existing regulatory agencies in financial sector is also under consideration.

4. Evaluation of Sectoral Regulatory Framework

The rapid evolution and proliferation of independent regulatory bodies in relatively short period have raised issue related to type and degree of autonomy conferred on these bodies and about the mechanisms to make these institutions and their personnel accountable.

In the past, several ministers have expressed concerns about the practice of establishing new regulators alleging the regulators of assuming policy-making role, independent of the government. This has raised the need for establishing a common framework to govern functions, responsibilities, operations, and accountability of regulatory authorities. Consolidation of regulatory institutions, wherever desirable, has also been considered desirable. Accordingly, the telecom and broadcast regulators were merged and the same approach is being followed in energy sector. Financial sector too is likely to see similar action soon.

Generally, it has been realised that to function properly the regulatory agencies need a fair amount of managerial autonomy and separation from the constraints normally imposed upon government departments. However need for more autonomy would create a need to have effective mechanism to ensure accountability.

4.1 Regulatory Institutional Framework

Table 3.1 Regulatory Institutional Framework in South Africa

Sector	Enabling Legislation	Regulatory Body	Appellate Body	Other Agency and its role	
Telecommunications and Broad-casting	ICASA Act, 2000; IB Act, 1993, Broadcasting Act, 1999; Telecommunications Act, 1996	Independent Communications Authority of South Africa	Line Ministry in specific matters; Judiciary	Department of Communications	Policy making; and few regulatory functions
Electricity	Amended Electricity Act, 1994; National Energy Regulator Act, 2004	National Electricity Regulator (will merge into the National Energy Regulator in April 2006)	Line ministry		
Gas	Gas Act, 2001	National Energy Regulator (since April 2006)	Judiciary		
Petroleum	Petroleum Pipelines Act of 2003	National Energy Regulator (since April 2006)			
Road Transport	Transport Licensing Act, 1962; National	Department of Transport	-	South African National Roads Agency	

Sector	Enabling Legislation	Regulatory Body	Appellate Body	Other Agency and its role	
	Road Traffic Act, 1996				
Civil Aviation	South African Civil Aviation Authority Act, 1998	Ministry (on advise of 'Regulatory Committee')	-	Civil Aviation Authority (CAA)	Regulation of safety and related aspects
Railways	Railways and Harbour Act;	Department of Transport; Dept. of Public Enterprises	-		
Seaports		Government owned service provider (Transnet) [19]	-	South African Maritime Safety Authority	To regulate safety related aspects
Water Supply	National Water Act, 1998	Department of Water Affairs and Forestry			
Banking	Banks Act, 1990; Mutual Banks Act, 1993	South African Reserve Bank	Appeals Board against decisions of different Registrars	Policy Board for Financial Services and Regulation	To advise the government on broader policy issues
Non-banking Financial Services	Financial Services Board Act, 1990	Financial Service Board (FSB)			
Financial Market Services (Retirement Benefits, Insurance, capital market)	Financial Markets Control Act 1989; Pension Act; Long-term Insurance Act; Short-term Insurance Act				

As far as the structure of the regulatory regimes in South Africa is concerned, following approaches are broadly being followed:

- The ministry concerned continues to regulate sectors such as Highways, Railways, Water & Sanitation.
- The second approach is having specialized bodies within the ministry to advise on regulatory matters. Such agencies are specialised bodies that function under direct control of the ministry concerned. For instance, in Civil Aviation, the Regulatory Committee advises the ministry on economic regulation issues.
- The third approach is to have specialized regulatory agencies independent of the relevant line ministry, such as in telecom, energy, banking.

The trend in South Africa is that of separating policy formulation from regulation. Regulatory framework in South Africa is moving towards having multi-sector regulatory agencies.

Regulatory structure in financial sector of South Africa is rather complex (see Figure 1). The Reserve Bank of South Africa (RBSA) regulates the banking sector through the Registrar of

[19] Constitution of independent port regulator is likely in near future

Banks who is fairly independent. Besides, the Financial Services Board (FSB) was established to oversee the activities of the non-banking financial services and act in an advisory capacity to the Minister of Finance. However, FSB primarily acts as an advisor to the ministry. The FSB supervises institutions and services in terms of sixteen Parliamentary Acts, which entrust regulatory functions to the Registrar of Long-tem Insurance, Short-term Insurance, Friendly Societies, Pension Funds, Unit Trust Companies, Stock Exchanges and Financial Markets. Regulatory control over Insider Trading and the participation bonds industry are also included. The Executive Office of the FSB has some regulatory functions such as issuance and cancellation to supply financial services; to investigate and impose criminal sanctions in event of obstruction, and can apply to court for an prohibition of financial institutions if necessary. The Policy Board for Financial Services and Regulation ('Policy Board') was set up through enactment of Policy Board for Financial Services and Regulation Act in 1993 to advise the ministry on broader policy issues related to regulation of the financial sector in South Africa.

The Financial Markets Control Act 1989 enabled setting up of the Financial Markets Advisory Board (FMAB). The FMAB is empowered to conduct investigation regarding matters relating to financial markets and stock exchanges; to advise the Registrar of Financial Markets (and Stock Exchange); to make recommendations to the Minister of Finance; and advise the Minister on matters referred to the Board by the Minister.

Considering the complexities of having several regulatory agencies in the financial sector, the Government has recently decided to move towards a single, mega-regulatory structure, as exists now in the UK.

4.2 Management Structure and Selection Mechanism

Table 3.2 Selection Mechanism for Regulatory Agencies in South Africa

Regulatory Agency	Number of board members	Members and their appointment				Salary, allowances, etc of Members
		Chairman	Person responsible for day-to-day management	Permanent Secretaries from related Ministries	Members with expertise in related matters	
Independent Communications Authority of South Africa (ICASA)	7	Chairperson (*appointed by President based on advice of Parliamentary Committee*)	Chief Executive Officer	4 (PS in Ministries of Communications; Finance; Internal Security; Information & Broadcasting)	6 other members (*appointed by President, public is invited to nominate and public hearing is organised for selection*)	Determined by line minister
National Energy Regulator of South Africa (NERSA)	8	Chairperson (*appointed by Minister*)	Chief Executive Officer (one of the members)	-	6 other members- part time (*appointed by Minister*)	Determined by line minister
Reserve Bank of South Africa (RBSA)	14	Governor (appointed by President)	-		3 Deputy Governors and 3 Directors (appointed by the President) 7 Director elected by shareholders to represent sectors such as agriculture, industry, commerce and finance.	
Financial Services Board (FSB)	As many minister deemed fit	Chairperson (appointed by minister)	-	-		

The President of South Africa appoints the regulators in telecommunications and banking sectors, while the concerned line ministry is vested with such powers in rest of the sectors. In case of telecommunication sector the parliamentary committee on communications invites the public to nominate persons for consideration and public hearings are held in respect of each candidate. The president appoints the regulators, on the basis of the recommendations made by the committee.

There is a provision for appointment of part-time members in the regulatory boards of energy, civil aviation, and financial services sectors. Having relevant knowledge and experience is one of the prerequisites for appointment in all regulatory agencies.

Line ministry determines the remuneration and allowances of the chairperson and other councilors in respective sector, and usual term of appointment is for five years with variation in some cases. Reappointment is provided for in telecommunications sector.

The provisions for removal of councilors/regulators vary across sectors. In telecommunications a councilor may be removed only when proved guilty in a finding of the National Assembly and the Assembly adopts resolution thereof. In energy, the minister can withdraw the appointment of a member should it find the member incompetent or unfit to fulfill the duties. Clearly, regression can be observed in the approach of the government as far the provisions for removal are concerned. Such regressive provisions will only dampen the independence sought to be provided to regulators.

4.3 Financial Resources

The approach with regard to financing the administrative expenditure of the sectoral regulatory agencies in South Africa is not uniform. In telecom, the government allocates budget to the authority on annual basis. The Financial Services Board is allowed to raise funds through imposing fee/levy on companies it regulates (in insurance, retirement funds, asset management firms, stock brokers etc), however, government decides the quantum of the levy/fee. As a result, though FSB does not depend on government for resources, it still does not have complete financial autonomy.

The funding mechanism of the electricity regulator presents a contrast as it follows an approach that comprises combination of the two approaches described above. Part of the expenses of the National Electricity Regulator (NRR) is funded out of the levy imposed on electricity generators and the rest comes from the government's annual budget. These provisions have been retained in the case of the NERSA to which the NER will soon merge.

The Reserve Bank of South Africa earns return on various investments it has made. The Bank is self-sufficient to fund its administrative expenditures hence does not rely on the government. Rather, after deduction of certain amount as per provisions the excess income of the Reserve Bank is deposited to the state treasury.

The crucial role of financial autonomy is evident from the case of the telecommunications regulator in South Africa. Relying entirely on budgetary allocations, the telecommunications regulator (ICASA) has been facing significant funding constraints. This has limited its ability to regulate the sector, which is increasingly getting complex. Recently, the ICASA has proposed to the government to amend the law and alter its funding mechanism to match with the changed context.

Making regulatory agencies dependent on the line ministry for budget compromises on their autonomy as the availability of funds with regulatory agencies eventually determines the number of staff a regulatory agency can hire, and other operational expenses.

Table 3.3 Funding Arrangements for Regulatory Agencies in South Africa

Regulatory Agency	Mode of Financing	Approving Agency
Independent Communication Authority of South Africa (ICASA)	Grants from the government, interest on deposits	• Parliament appropriates grants • Parliamentary Portfolio Committee on Communication approves budget
National Energy Regulator of South Africa (NERSA)	Levy imposed on electricity generation license; contributions from government and others	• Minister determines amount of Levy • Budget proposals to be approved by the Minister
Reserve Bank of South Africa (RBSA)	Profits accrued from operations	-
Financial Services Board (FSB)	Fee charged for certain services; annual levies from companies it regulates in sectors including insurers, retirement funds, asset managers, and stock brokers	• Fee and service charges are raised as prescribed by the Government in the Gazette.

4.4 Staffing and Training

The South African regulatory agencies are empowered to set up their own office administration, however, they are not empowered to offer remuneration to their staff better than that is being offered by the public sector. The NERSA, which is the most recent regulatory institution in South Africa, has to get the remuneration structure of their staff approved by the ministry concerned. Regulatory authorities often compete with the private sector to attract and retain qualified and talented staff, in which they often do not succeed mainly for the reason that the public sector salaries, which regulatory agencies offer, are way behind the market rates.

Table 3.4 Staffing and Training in Regulatory Agencies in South Africa

Regulatory Agency	Number of staff	Training	Power to appoint staff
Independent Communications Authority of South Africa (ICASA)	Permanent-283 Temporary/ On contract-8 (March 2005)	Efforts are there to develop soft skills, and technical training in engineering and technology. During 2004-05, 4.47% of payroll costs was spent on training and development	ICASA Council
National Electricity Regulator (NER)	89	Staff exposed to training	Chef Executive Officer of NER
South African National Road Agency Limited (SANRAL)	123	Staff exposed to training	
South African Reserve Bank (SARB)	1988	Staff exposed to training	
Financial Services Board (FSB)	251	Staff exposed to training	

Attention is being given to expose staff to training and development programmes, and project these programmes as an incentive. For instance, the entire staff of the energy regulator have signed a performance contract that also includes training and development plans. ICASA has started offering performance rewards such as bonus that has helped retaining competent staff.

In larger context, the ability of regulatory agencies to offer attractive emoluments and to invest in skill development of their staff is subject to the extent of autonomy (financial and functional) provided by the law. Regulatory agencies will find it difficult to attract and retain high quality staff unless they are allowed to raise required resources, and given the freedom to structure the pay scales to make it attractive for their staff.

In South Africa, an important aspect of human resource management is of mainstreaming the black population which has historically been disadvantaged. Like any other public sector organization, regulatory agencies are making conscious efforts to increase the proportion of such disadvantaged groups within their workforce.

4.5 Regulatory Mandate and Enforcement

Communications

The ICASA Act states that the regulator is independent and subject only to the Constitution and the law. ICASA derives its mandate from four statutes; the ICASA Act of 2000, The Independent Broadcasting Act of 1993; the Broadcasting Act of 1999 and the Telecommunications Act of 1996. The functions of the ICASA are:

- Formulate regulations and micro policies to govern the sectors and enforcement
- Issue licenses to telecommunications and broadcasting service providers on behalf of Ministry
- Dispute resolution among stakeholders
- Frequency spectrum management
- Protecting interests of consumers

The broad policy of the South African Government is to provide access to basic telecommunications services at affordable prices and ICASA is instrumental in achieving that. The Authority promotes the attainment of universal service and access by including the roll out requirements in the under-serviced areas as a condition to the operator's licenses and ensure that licensees contribute to the Universal Service Fund (USF). ICASA does not however administer the USF but receives money on behalf of it. The Authority is also responsible for extending the relevant and appropriate broadcasting services to all citizens. ICASA also has a mandate to promote and encourage the ownership and control of telecommunication and broadcasting services by people from historically disadvantaged groups. As a regulator ICASA is responsible to ensure level playing fields to all industry players through framing appropriate regulations.

However, ICASA's power to enforce its mandate is rather weak, as it does not have powers to impose penalties in most events of contravention of regulations by an operator, except in some limited circumstances such as non-achievement of universal rollout targets. In other events of contravention of the Act the regulator can order to desist from the actions and revoke the operating licence. However, given the sunk costs of most of the firms involved, the latter option is hardly a credible threat, in practice.

The degree of independence given to ICASA varies with respect to its functions in telecommunications and broadcasting. With respect to communications sector, ICASA operates with rather limited independence, for instance it has to function in accordance with policy directions issued by the minister. On other end, in case of broadcasting sector, it has to only 'consider' the policy directives.

Furthermore, the Telecommunications Act provides for the Minister to determine the process, conditions, and the manner in which applications seeking licenses should be made i.e. by way of auction, or tender, or both. ICASA's role is to evaluate the applications and recommend the cases to the Ministry who decides on granting the licenses. The Minister has a fairly wide discretion in respect of issuing licenses, which has caused some disputes with the regulator. In one of such disputes ICASA expressed its disagreement with the Minister's decision of having three-part process for issuing license to Second Network Operator in the fixed-line market. The matter was eventually settled after a high-level political intervention. Ministerial intervention in telecom regulation on several occasions has created a situation in which industry participants tend to 'bypass' the regulator who see the Minister as having the final say on regulatory matters.

The variations in the approaches followed in the Telecommunications Act and the Information Broadcasting Act, in certain aspects, creates problems for the merged regulator i.e. ICASA. For instance, no regulation made by ICASA in respect of telecommunications is valid unless the Minister has approved and published it in the Government Gazette. This is not with broadcasting. This has given rise to disputes between the Minister and ICASA, notably in respect of facilities leasing and interconnection (see Box 3.1). Further, distinction between telecommunications and broadcasting technologies is increasingly vanishing that requires ICASA to move away from the present approach of continuing with maintaining an artificial boundary between telecommunications and broadcasting. Service providers are required to obtain a separate license for each type of technology they use. Such restrictions limit the full exploitation of the benefits of advancements in information and communications technology and have limited competition in telecommunications. The Convergence Bill 2004 proposes to address these issues.

Regulating public sector incumbent

The Telecommunications Act 1996 granted exclusivity to the state owned enterprise Telkom for a period of five years. During this period Telkom has performed quite well in terms of improving telecommunications access and has complied with the bulk of its roll out targets by installing over 2 million new lines. However, by the end of Telkom's five-year exclusivity period in year 2002, up to two-thirds of the new lines were disconnected due to non-payment.

The exclusivity period was over in year 2002 and license could be issued to second network operator. However, Telkom still continues as the only player in fixed line telephony for the reason that the process of issuing license to second network operator has been dogged with controversy and two bids have already failed. Recently, the minister intervened and resolved the issue and second operator is likely to be given the license soon.

Valued Added Network Service (VANS) and Private Network (PTN) were among those services which were opened for competition and several disputes between the state owned incumbent service provider, Telkom, and other VANS operators have emerged on issues relating to access to telecom infrastructure and anti-competitive conduct. Such disputes have been affecting the growth prospects of the sector.

Box 3.1 Judiciary Acts to Preserve Telecom Regulator's Autonomy

The Telecommunications Act requires the telecom regulator to prescribe guidelines relating to the form and content of interconnection and facilities leasing agreements. The regulator went through the process of publishing draft guidelines and obtaining comments thereon from interested stakeholders. As per provisions of the law, the Minister published and approved the regulations made by the regulator. However, given that the state owned incumbent service provider, Telkom, was not happy with the guidelines, the Minster issued a notice to withdraw the regulations within a month after its approval. The notice was issued without the regulator having made a request for withdrawal, and without consultation with the regulator. The matter went to High Court and the court held that the provisions of the Telecommunications Act made it clear that Minister cannot unilaterally withdraw regulations and ruled that the regulations were still in force. The Court stated that the function of the Minister in respect of an amendment or withdrawal is confined to approving and publishing it hence the amendment or withdrawal cannot emanate from the Minister. It must come from the regulator.

Tariff Regulation

Year 1997 onwards Telkom's tariffs have been regulated by the telecom regulator. This has been done in accordance with the new license conditions. However, the Minister still intervenes in tariff determination to safeguard Telkom's interest (See Box 3.2). The telecommunication services have been divided into two broad categories i.e. Volume1 and Volume2. The Volume1 services are provided by Telkom only and are not subject to competition while the others are open for competition.

As per the provisions of the Act the regulator follows a price-cap form of regulation and has embarked on a major exercise to review Telkom's tariffs. The regulator is given the mandate to ensure that consumers are not unduly burdened, accordingly the regulator is in the process of finalising the regulations to restrict the price adjustment proposals of Telkom if need arises.

Consumer Protection

The consumer protection department is responsible to educate consumers about the role and functions of ICASA, their rights, and the procedures in complaints handling. ICASA has an outreach programme on consumer education which is aimed at informing communities about regulatory activities, consumer rights in telecom sector and ways to access services offered by ICASA. As regulator, ICASA is responsible for resolution of consumer complaints and it has signed a Memorandum of Understanding with the telecommunications operators on handling of consumer complaints. The telecommunications service providers are bound to give aggrieved consumers a fair hearing.

Box 3.2 Telkom (South Africa's SOE incumbent) Influences Ministry

In telecom sector, the price cap method of rate setting was adopted in May 1997, valid for the subsequent three years. That time, the productivity improvement factor X was negotiated with very limited information and understanding. Three years later, in 2001, the regulator published draft price cap regulation and the proposals along with comments received from the public were forwarded to the Minister for approval.

Telkom lobbied the Minister and approval of the new price regulation proposals was delayed. Meanwhile, *Telkom* filed an application to allow a price increase in year 2002 including a 23.9% increase in local calls. The regulator rejected the application filed by Telkom and the matter reached the court.

Finally, a negotiated settlement was reached whereby Telkom's price increase was approved subject to the introduction of a new lifeline service to try and keep customers in the network. The Ministry approved the amendment in October 2002.

Energy

The National Electricity Regulator (NER) regulates and controls the supply of electricity in South Africa. NER drives its mandate from the Electricity Act and the Eskom Act 1987. Its functions are:

- Issue licenses for generation and distribution of electricity
- Determine the prices and conditions of supplies
- Settle disputes between licensees among themselves and/or with consumers
- Collect information from the stakeholders
- Perform inspections of the equipment of licensees'
- Advice the Minister on any matter relating to the industry
- Carry out investigations wherever appropriate

NER operates under the mandate given by the Minister of Minerals and Energy as custodian and enforcer of regulatory framework to monitor, meet, and safeguard interests and needs of present and future customers of electricity in South Africa. The regulator is supposed to ensure sustainability of the electricity supply industry, and facilitate efficiency and effectiveness. NER is primarily responsible for protection of consumer interests and it reports to the Parliament via the Ministry of Minerals and Energy.

<u>Regulating the state owned incumbent service provider</u>

South African Electricity industry is dominated by Eskom that is state-owned vertically integrated utility. Eskom ranks among the five largest in the world and supplies electricity at amongst the lowest prices in the world. Eskom reports to the Ministry of Public Enterprises who is the sole shareholder on behalf of the government. The industry has accomplished an unprecedented national electrification programme under which about 2.5 million additional households were connected during the past 6 years. This has resulted into an increase in the proportion of the population with access to electricity from about one third of the population to about two thirds.

One of the challenges that the regulator faces is to ensure consistency between its regulatory objectives and the performance agreement signed between Eskom and the Ministry of Public Enterprises. Significant information asymmetries do exist in the industry and the state-owned

utility may seek to influence key provisions of the performance contract in a way that might limit regulatory discretion.

Tariff Regulation

Rate of Return (RoR) methodology is used in the determination of tariff schedules. With improvement in capacity of the regulator, more rigorous analysis of Eskom's price increase is done. For instance, in year 2004 the annual review of the Eskom price resulted in a price increase of 2.5 percent for distribution. Eskom filed a review petition against the decision to the Ministry of Mineral and Energy who is the appellate authority. The Minister subsequently retained the order passed by the NER and upheld the initial determination of increasing the tariff by 2.5 percent.

As of 1st April 2006, NER will merge into the National Energy Regulator of South Africa (NERSA). In addition to existing legislations in energy, gas and petroleum sectors, NERSA derives its mandate from the National Energy Regulator Act 2004. It is empowered to:

- Issue licenses pertaining to the three industries under its mandate
- Act as mediator or arbitrator in disputes
- Set and approve tariffs and charges
- Monitor access to petroleum pipeline facilities
- Promote competition in the petroleum pipeline and gas industries
- Promote optimal use of gas resources
- Settle customer disputes.
- Gather and store information pertaining to gas and petroleum pipeline

Aviation

The Ministry of Transport regulates the aviation sector. A 'Regulatory Committee' has been constituted within the Department of Transport to advise the ministry in the regulation of the aviation sector on economic aspects. The Committee works under direct control of the ministry. Besides, policy formulation and regulation, Government also delivers services in a big way.

Financial Services (Banking, Insurance & Capital Markets)

The South Africa Reserve Bank (SARB) Act assigns the Board of Directors of the Bank with the responsibility of management of the functions of the Bank. The mandate of the SARB includes achieving a sound and efficient banking system in the interest of the depositors and the economy. SARB issues banking licenses and monitors their activities for the compliance of the Banks Act, 1990 or the Mutual Banks Act, 1993. The Monetary Policy Committee (MPC) within the SARB advises the Governor in formulation of the monetary policy for South Africa. Operations of monetary policy tool, determining the repurchase rate are some of the functions that are prerogative of the Governor of the Reserve Bank. However, in practice, Minister of Finance is always consulted at the time of a change in the monetary policy.

The Financial Services Board oversees the Non-Banking Financial Services Industry. FSB acts in advisory capacity to the Minister of Finance on matters related to listing requirements, public issues, takeovers and mergers. Besides, FSB supervises financial institutions and services in terms of 16 Parliamentary Acts. These functions are entrusted in the office of the Executive Officer of FSB who interacts with other members of the executive and heads of various departments. Regulatory control over insider trading, participation bonds industry, certain trust and depository institutions, and central security depositories responsible for the safe custody of securities are also included in these functions.

The Executive Officer of FSB is vested with powers which includes cancellation of authorisation to supply financial services, to investigate with criminal sanctions in an event of obstruction, to file petition for winding up of financial institutions (such as insurer/pension fund) or to place it under judicial management. The Inspection of Financial Institutions Act 1998, allows FSB to obtain warrants to search and question third parties who might have information about unregistered financial institutions.

Nevertheless, most of the regulatory powers given to the Chief Executive can be enacted only in an event of financial institution/s contravening the provision of law, or action of a firm is observed to be inappropriate for trade. Hence, FSB has little role to regulate the financial sector in a proactive manner.

A Financial Services Consumer Advisory Panel also exists who is responsible to advise the FSB and the Registrar of Banks within the SARB on consumer-protection issues which fall within the regulators' jurisdiction.

4.6 Interface with Competition Authority

The issue of the relationships and potential jurisdictional conflicts between competition and regulatory authorities has received wide attention in the Policy Framework document of year 2000. The Amended Competition Act 2000 provides for concurrent jurisdiction on competition matters in sectors which were previously subject to the exclusive jurisdiction of specific sector regulators. The existing provisions require the Competition Commission to conclude agreements with the sector regulators and make provision for exercise of concurrent jurisdiction. Therefore, the exact jurisdictional boundaries are not a matter of law but depend upon the agreement reached between the competition authority and sector regulators.

In addition, the Regulators Forum was established in March 2002 as an informal body through which sector regulators envisage maintaining a consistent and coherent approach while dealing with competition matters. The Forum facilitates a process of information sharing and discussion of common issues so as to avoid overlaps, duplication, or contradictions.

Communications

ICASA and the Competition Commission signed a Memorandum of Agreement in September 2002 to deal with several issues including, merger & acquisition evaluation and analysis, investigation, and handling of competition related complaint in telecommunications and broadcasting sectors.

In certain cases of merger, approval of both regulatory authorities is required. In such matters, parties are required to file separate and concurrent applications, and each authority makes independent determinations based on their respective legislative requirements. The authorities may consult in the process. With regard to handling competition related complaints in the telecommunications and broadcasting sectors the Agreement clearly identifies the jurisdictional boundaries for both the authorities. Furthermore, specific rules of procedure in the case of concurrent jurisdiction have been framed to ensure exchange of information between the two regulators.

As per the provisions in the Agreement, the two regulatory agencies have constituted a Joint Working Committee. The mandate of the Committee is to: (i) Manage and facilitate cooperation and consultation in respect of matters dealt with by each regulator; (ii) Propose amendments to

the Agreement when necessary; and (iii) Advise management of both authorities on matters affecting competition in the telecommunications and broadcasting sector.

Further, a draft Convergence Bill is under consideration that along with several other proposals intends to demarcate specific roles for the regulator and the competition authorities in the law.

Energy

A formal agreement between the Competition Commission and the NER does not exist as yet, which has led to a jurisdictional conflict between the two agencies. Conflicts often arise especially with respect to those provisions which authorise the NER to regulate market access and approve electricity prices.

NER will soon merge into NESRA. Therefore, a potential agreement between NERSA and the Competition Commission is desirable to ensure consistency and coherence in the application of regulatory laws.

Transportation

The Competition Act requires the Competition Commission to negotiate agreements with each of the sectoral regulatory authorities, to co-ordinate the exercise of collective jurisdiction over competition related matters. In civil aviation sector, such an agreement has not been concluded so far. As result of that, concurrency of jurisdiction between the authorities is creating scope for 'forum-shopping which might lead to inconsistency/contradictions in approaches.

Box 3.3 Concurrent Jurisdictions in Aviation Sector in South Africa

In 2003, the Airline Association of South Africa and few others filed a complaint with the Competition Commission in protest to the manner in which the 'Regulatory Committee' determined the tariffs of Airport Company of South Africa (ACSA) and Air Traffic and Navigation Services Company (ATNS), the state owned enterprises (SOEs). Allegation was made on both SOEs of charging excessive tariffs, hence violation of the provisions of the Competition Act on abuse of dominance.

The petitioners objected in particular to the 16 percent returns that ACSA was allowed to reap. The Airline Association of South Africa was of the view that the return should not be more than 11 percent. In addition to that, several other complains were also filed related to passenger, landing and parking fees.

The Competition Commission initiated an investigation and examined the methodology followed by the Regulatory Committee to set tariffs and found that as appropriate. The report concluded that the rates of return should not be reviewed frequently but at a gap of several years. The case illustrates the potential for 'forum-shopping' that is created by the concurrency of jurisdiction framework.

Financial Services (Banking, Insurance & Capital Markets)

Again, no agreement on concurrent jurisdiction has been reached so far between the SARB and the Competition Commission. In such a scenario, a merger proposal in the banking sector sometime back triggered a crisis concerning the concurrent jurisdiction of the Reserve Bank and the Competition Commission. The acquiring firm who presented a hostile bid argued that as per the provisions of the Banks Act 1990 mergers in the banking industry were subject to the control of the Registrar of Banks and the competition authorities was not having jurisdiction. On the

other end, the targeted firm argued that the merger would be anti-competitive hence sought the assistance of the Competition Tribunal to prevent the transaction.

In sum, the practice of two regulators getting into a formal contract to collectively handle competition related issues sounds appropriate. However, the fact that so far such contracts have been signed only with telecommunications regulator indicates practical difficulties.

4.7 Decision-making Process

Communications

Stakeholders and public in general participate and offer viewpoints when invited by ICASA on a range of issues such as, issuance of licenses, framing regulations, and micro policy formulation. As provided in the legislation, the process is participatory and transparent. The regulator also makes effort to disseminate relevant information among the public in general.

Energy

The National Electricity Regulator holds public hearings on issues such as supply disputes and land expropriation disputes that emerge in laying transmission lines etc. However, this is not the case when key regulatory matters such as tariffs are set. The regulator issues statements in the media explaining the general reasons for tariff determinations, however formal written decisions and explanations are not published. The situation is expected to improve with setting up of the new regulator for the energy sector, as the enabling legislation provides for greater transparency.

Nevertheless, NER is making efforts to improve its interaction with the public. In 2004, the NER Board appointed a public relations consultant to assist in the implementation of its stakeholder management and communication strategy. Thereafter a series of breakfast briefings were organised with a variety of stakeholders and media which has helped the regulator to establish direct communication with the stakeholders.

Transportation

The Department of Transport (DOT) is responsible to define transport policy and guidelines. It creates legislation and provides funding for infrastructure development. The final authority over the choice of transport strategy remains the mandate of the Minister of Transport. In recent years the DOT has reduced its direct involvement in operations, infrastructure and services, to 'allow for a more competitive environment'.

Financial Services

The SARB Act does not prescribe a completely transparent framework for monetary policy formulation. The Monetary Policy Committee (MPC) is the key body within the SARB that remains responsible to reach decisions on monetary policy and the desired level of the Bank's repurchase rate. MPC is constituted out of the Bank's key staff members. Decisions with regard to monetary policy are taken during the six-weekly formal meetings of MPC scheduled during a year.

Efforts to improve transparency and awareness of the Bank's activities has led to the establishment of Monetary Policy Forum meetings where the Bank's governors explain developments in monetary policy to organised business, labour, politicians and academics, and get feedback from them. This exercise takes place twice a year. Senior staffs of the SARB also participate in panel discussions and other public events.

In case of FSB, an advisory board assists the Board on financial markets. Similarly, several other advisory committees are there to provide assistance on sectors including financial services industry, long-term insurance, short-term insurance, pension funds, and collective investment schemes. The FSB maintains a close relationship with industry associations. A Financial Services Consumer Advisory Panel also exists who is responsible to advise the FSB and the Registrar of Banks within the SARB on consumer-protection issues which fall within the regulators' jurisdiction. FSB has a communication strategy in place which is tailored to achieve successful and effective communication with staff and the external stakeholders and media.

4.8 Accountability Mechanism

Table 3.5 Accountability Mechanisms for Regulatory Agencies in South Africa

Regulatory Agency	Minister/Parliament	Appellate Body
ICASA	The ICASA Council submits its annual report of activities and audited financial accounts to the Minister, which is then tabled in the Parliament.	• High Court of South Africa • Minister in certain license related matters
National Electricity Regulator (NER)	Annual report of activities with audited accounts submitted to Minister, *w*ho tables it before Parliament	• Line Ministry
South Africa Reserve Bank (SARB)	SARB submits annual report to the Parliament. Being a constitutional body, any deviation from the primary objective of the SARB could be contested in the Constitutional Court. The bank also publishes monthly statement of its assets and liabilities.	-

Communications

ICASA is held accountable to the public through the Parliament and its committees. The regulator submits a report of its activities on annual basis. Parliamentary Portfolio Committee on Communications maintains an oversight over ICASA. The Minister tables the annual report in the Parliament. Auditor-General carries out an audit of the financial accounts of the regulator and a copy of the audited financial statement is provided to the Minister, which is then presented in the Parliament.

Energy

NER submits its annual report to the Minister that comprises of its functions, affairs and financial position. The Minister presents the report in the Parliament. An aggrieved party can challenge a decision of NER through filing an appeal to the Minister. The Minister being the appellate authority on the decisions made by the government, the NER is perceived ineffective in regulating the state owned incumbent service provider. A set of reviews undertaken by the Presidency and National Treasury in South Africa concluded, "*the National Electricity Regulator has not yet implemented a robust approach to regulating Eskom prices.*" While the NER has been able to restrain monopoly pricing by the national utility, its decisions have often been found to be inconsistent.

Aviation
The Minister of Transport is responsible for the Aviation Act that regulates aviation in South Africa. The Department of Transport provides economic regulation, with the assistance of Regulatory Committee.

Financial Services
The Constitution of South Africa provides for regular consultation between the Bank and the Cabinet member responsible for national financial matters. Any deviation from the primary objective of the SARB could be contested in the Constitutional Court.

The SARB Act provides for the publication of a monthly statement of the Bank's assets and liabilities, and submission of annual report to the Parliament. The Bank is therefore accountable to Parliament as the representative body of all the people in South Africa. The arrangement ensures that the Government cannot exercise undue influence over the Bank in furthering any party-political agenda. The Act, however, does not specify explicit benchmarks against which the performance of the South African Reserve Bank can be judged.

The Bank holds a general meeting of shareholders annually in the month of August, where the Governor, as Chairperson, delivers an annual address on the state of the economy and monetary policy, which is covered widely in the media.

5. Concluding Remarks
Independent regulatory structure is in its evolution stage in South Africa. Telecommunications and broadcasting regulators have merged to form one overarching regulator and similar approach is being followed to form an energy regulator which would cover electricity, piped-gas, and petroleum pipeline sector. Setting up a multi-sector regulator in the finance sector is also being considered. Clearly, interaction of multiple line ministries with such mega-regulators would potentially serve as deterrent to possibility of regulatory capture. The model is worth consideration to other developing countries as well.

Mandate of regulatory agencies in South Africa is sufficiently wide and protection of consumer interests has been given prominence in almost all regulatory legislation. Public sector enterprises dominate most of the sectors hence emphasis is on regulating the state owned enterprises effectively.

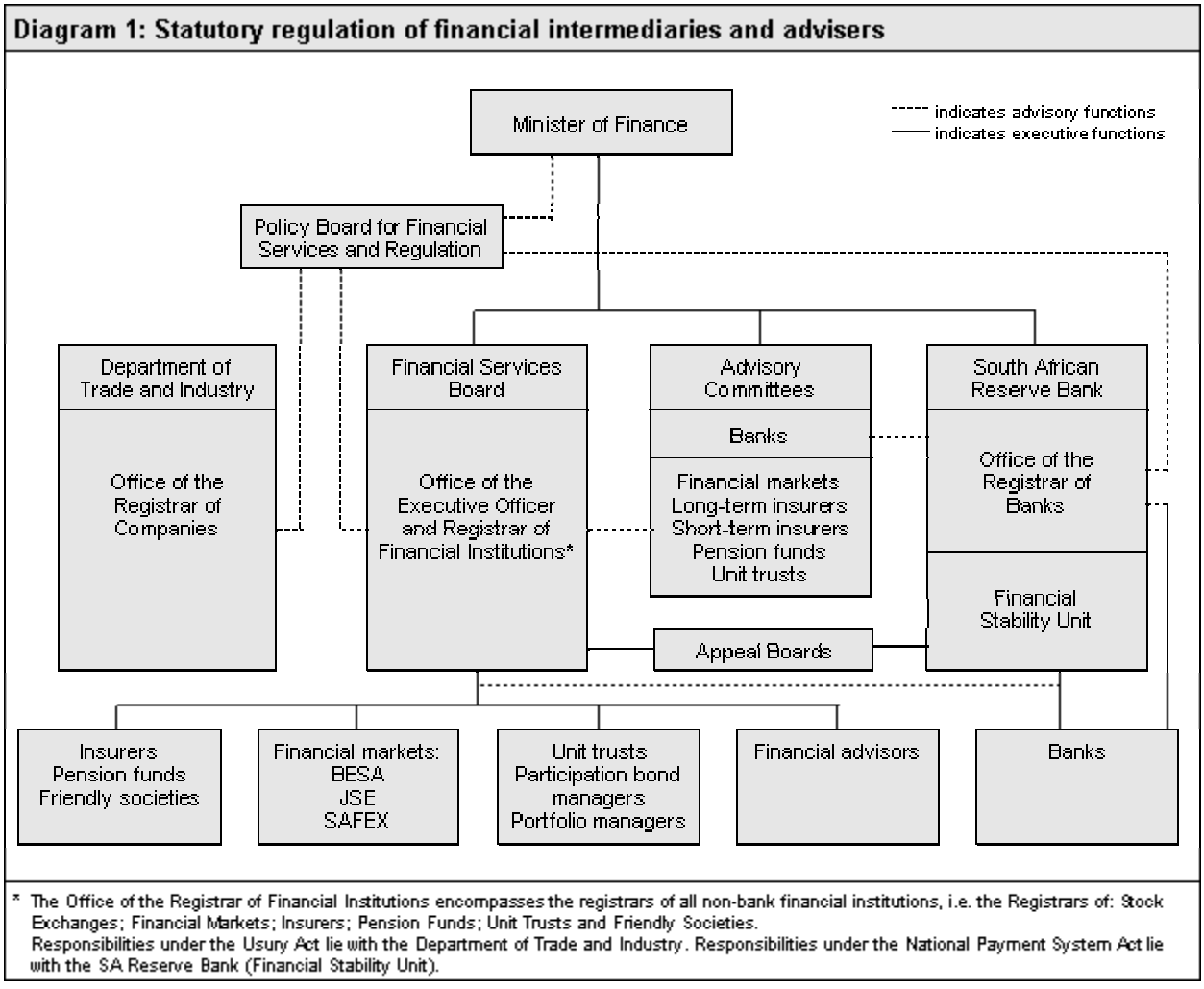
Though state owned enterprises have been corporatised, there is no immediate plan of their privatisation. Rather, private investment is desirable through green-field mode. The role of government in economic activities was pervasive in the past, and recent experience with privatisation testifies to the continued role played by the government in economic activities. Renewed emphasis is being placed on the role of state owned enterprises in delivering basic services.

Regulators in telecommunication and electricity sector have been struggling to discipline the respective state owned service providers, as the ministries concerned continue to influence regulatory decision-making.

The selection process of regulators is far more transparent in South Africa. It also involves nomination from public. However removal procedures varies across sectors. The recent energy regulator can be ousted at the will and whim of the minister while a probe and resolution by National Assembly is required in telecommunications.

Consumer organizations are weak in South Africa, and consumers generally are not aware of sector regulation and the facility of bringing complaints to the sector regulator. There are very few attempts to conduct regulatory impact assessments in South Africa. Currently a World Bank project has been launched to assess the impact of regulation, on efficiency and competitiveness in key sectors such as telecommunications and transport. Effective regulatory enforcement requires very specific capacities not only in the regulatory authorities but also in the private sector, legal and economics professions and among consumers. Regulatory authorities face the challenge of attracting and keeping good staff.

Figure 1



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Chapter IV
Regulatory Environment in Zambia

1. Introduction

Zambia is in Southern Central Africa. The country covers a total of 752,614 sq km (290,584 mil) and has common land border with Congo, in the north, Tanzania in the north-east, Malawi and Mozambique on the east, Zimbabwe, Botswana and Namibia in the south and Angola to the west.

ZAMBIA COUNTRY PROFILE	
Population	10.4 mn***
GDP (Current $)	$ 4.3 bn***
Per Capita Income	$ 380.0 (Atlas)*** $ 840.0 (PPP)
Land Area	752.6 thousand sq kms.***
Life Expectancy	32.7 years**
Literacy	79.9 %**
HDI Rank	164

Sources:
World Development Indicators Database, World Bank 2005
Human Development Report Statistics, UNDP, 2004
(**) For the year 2002
(***) For the year 2003

Zambia became a republic in 1964 after gaining independence from the United Kingdom. It is one of Sub-Saharan Africa's most highly urbanized countries. About one-half of the country's 10 million people are concentrated in a few urban zones strung along the major transportation corridors, while rural areas are under-populated.

In late 1960s, Zambia was the world's third largest copper producer, after the United States and the Soviet Union. A collapse in copper prices, oil price shocks, and misguided economic policies in the 1970s had an extremely negative effect on the economy. This was compounded by the contraction of food production. The resulting economic decline was catastrophic, with per capita income falling almost 5 percent annually between 1974 and 1990 and other macro-economic problems surfaced: external debt of 7.0bnUSD and a three-digit inflation level by 1991.

Continued macro-economic disturbances forced Zambia to adopt economic liberalisation and structural adjustment programmes in 1991. Since then, macroeconomic and human development performance of the country has witnessed several changes. Growth in gross domestic product (GDP) has averaged 2.0 percent per annum while inflation has fallen from the triple digit levels of the early 1990s to below 30 percent. The fiscal deficit has also been brought down during the same period. Be that as it may, Zambia continues to depend on large external grants, which are in the form of budget and balance of payments support and food aid.

Agriculture sector contributes 22 percent to GDP in 2002 and accounts for approximately 85 percent of total employment. Maize (corn) is the principal cash crop as well as the staple food. Floriculture is a growth sector, and agricultural non-traditional exports now rival the mining industry in foreign exchange receipts. Contribution of industry and services to country's GDP stand at 26 percent and 52 percent respectively.

Economic decline and debt have had a particularly serious impact on poor. Structural adjustment programs, designed by the World Bank and IMF to enable debt repayment, have forced drastic cuts in government spending on social services.

Unemployment and underemployment are serious problems. Per capita annual incomes are currently at about one-half their levels at independence and place the country among the world's

poorest nations. The high population growth rate of 2.3 percent per annum makes it difficult for per capita income to increase. Due to its huge accumulated external and internal debt, Zambia has been classified as a heavily indebted poor country (HIPC) and a beneficiary of HIPC initiatives of debt cancellation and special external assistance.

2. Evolution of Economic Policy Regime

From 1964 and until 1990, Zambia followed a socialist model of economic and political system with a single party rule. The economic policies were characterised by import substitution, promotion of local industries and dominance of the state sector in all key sectors of the economy.

In 1991 government of Zambia began implementing a set of structural adjustment programmes (SAP) being supported by the International Monetary Fund (IMF) and the World Bank (WB). The SAP focused on mainly achieving three macroeconomic objectives:

- Restoration of macroeconomic stability through monetary and fiscal reforms;
- Facilitation of private sector growth by freeing price and exchange rate regulations and import and export regulations;
- Shift agriculture and industry from public monopolies to private and decentralised institutions.

Zambia embarked on its reform programme with a view to transforming the state-led, economy into a market driven economy. The new Government which came to power in 1991 dispensed with national development planning in preference for sectoral policies and programming as tools of economic reforms. The policy regime sought to open the economy to allow domestic firms to compete internationally and adopted an improved and more modern regulatory framework by drafting new laws on trade and investment, competition, liberalisation, privatisation and deregulation.

Against this background, new institutions such as the Zambia Privatisation Agency (ZPA), the Zambia Competition Commission (ZCC) and a number of sector regulatory bodies were established, and existing ones, such as the Zambia Investment Centre (ZIC) and the Bank of Zambia (BoZ) were reformed during the 1990s. Overall, these measures aimed at reducing bureaucratic procedures by removing licensing requirements, increasing private sector participation, controlling inflation, removing exchange rate restrictions, and uneconomic subsidy regime.

The public sector reform programmes aimed at streamlining the role of the government administration to one that is conducive to private sector development. The government adopted a policy of decentralisation by shifting services to sub-national levels of government, and sought greater involvement of communities in public service delivery.

The government set about dismantling of the state owned sector, which accounted for 80 percent of GDP, with the enactment of the Privatisation Act and the establishment of the ZPA in 1992. Privatisation of key enterprises were linked to the IMF/WB support to the country. Beginning with smaller companies, privatisation went into full swing in 1996-97 and so far, 300 out of 313 companies have been privatised. However, now the political commitment to privatising remaining parastatals remains low. This is because the speedy privatisation had brought about large number of labour retrenchment and increasing hardship among the working class. Most of the investors were offered tax holiday and once the tax holidays expired, they

closed up their businesses leaving a number of employees without jobs which they had earlier promised. While privatisation of state-owned utilities has slowed down, private sector participation has taken place in a limited way in broadcasting, telecom and energy.

Since the initiation of economic reform programme, considerable achievements have been made towards improving macroeconomic management, the opening up of the economy to international competition and the establishment of sector regulatory regimes through legal and institutional reform. However, these measures are yet to result in tangible improvements in development-related indicators.

3. Evolution of Sectoral Regulation

While introducing economic liberalisation, Government realised that in order to enhance economic growth and also development, private investment is a key factor. Since private investment decisions are a function of expected income streams, regulatory environment and therefore the investor perceptions about present and future conditions for commercial activity in the country is an important variable. Accordingly, the Government sought to deal with these necessities that constitute 'investment climate' and enacted suitable policies and legislations that were deemed supportive for the growth of the private sector.

The legal framework and institutions that have been introduced are:

- Investment Act and Investment Centre
- The Privatisation Act and Agency
- The Communications Act and Authority
- Competition and Fair Trading Act and Competition Commission
- Pensions and Insurance Act and Authority
- Energy Regulation Act and Board

These laws and institutions provide the basic enabling environment for deregulation, private sector participation and efficiency. The following section examines the evolution of regulatory governance introduced in select sectors in Zambia.

3.1 Telecommunications

The telecommunications industry in Zambia has traditionally been state-owned, enjoying full monopoly status. Like most other countries, Zambia is restructuring its telecommunications sector, through various initiatives, including, privatisation and introducing competition in order to enhance service delivery.

The government liberalised telecommunications sector, as early as 1994, by passing the Telecommunications Act, which created a regulatory authority and allowed more players in the sector. The Act resulted in restructuring of the sector and separation of posts and telecommunications functions from the then Post and Telecommunications Company (PTC). Giving rise to two commercial entities: Zambia Telecommunication Company (ZAMTEL) and the Zambia Postal Services (ZAMPOST).

The Act provides for separation of policymaking, regulatory and operational functions in the sector. Accordingly, the Communications Authority of Zambia (CAZ) was established to regulate provision of all telecommunication services. The purpose of CAZ is to allow for an orderly and stable development of the telecommunications sector by promoting investment as

well as ensuring fair and balanced competition and fair treatment of consumers. Prior to CAZ's establishment, PTC was the regulator. The Ministry of Communications and Transport (MCT) is responsible for policy issues in the sector. The Ministry also oversees the functions of the Communications Authority, ZAMTEL and ZAMPOST.

The liberalisation saw entry of new players in mobile phone service. Telecel was the first to enter the market, quickly followed by Zamcell (now Celtel). Foreign investors have a majority share holding in Telecel and Celtel. State owned Zambia telecommunication also entered the mobile segment through its subsidiary Cell Z.

Zamtel continues to be the sole provider of fixed line services in the country. Not surprisingly, fixed line network is still at a very low level of development with fewer than 90,000 connected main lines for a population of almost 11 million. ZAMTEL does not seem to be seeking market expansion in fixed line services. The poor performance of fixed line services has seen rapid growth of mobile market. There are now more mobile subscribers than fixed line. From about 15,000 in 1997, there are now over 250,000 mobile users (2003).

The market share of mobile players is: Celtel 48 percent, Telecel 31 percent, and Cell Z 21 percent, a fourth player (Vodacom) was expected to join the market but pulled out due to spectrum capacity problems. Competition in mobile market has become stiff as the three players keep coming up with several incentives to attract customers. The two private operators have concentrated on urban markets. Faced with competition from other operators, Zamtel, through its subsidiary Cell Z, has rolled out mobile services in areas where there were poor or no fixed lines. It is offering mobile services at affordable rates to the rural as well as the urban poor. As a result, other operators have been forced to revise their tariffs and offer other incentives in order to retain their market share.

The low level of development of fixed-line network has impeded growth in the Internet sector. Today there are approximately 10,000 Internet subscribers and an additional 30,000 Internet users in Zambia, but the potential for rapid growth is underlined by low level of infrastructure development, poor telephony accessibility and high access costs. Though there are no legal market entry restrictions for new ISPs, the $40,000 entry fee for an ISP license has proven too prohibitive in the past. This has since been revised downwards to US$25000. Other regulatory barriers include delays in spectrum allocation and licensing for wireless Internet provision.

Therefore, while provision of telecom services has been liberalised, entry in internet sector continues to be very expensive and is also subject to Government tender through the Ministry of Communication and Transport. The Communication Authority is reviewing this entry requirement in order to attract more players, especially those who are willing to offer their services in rural and underserved areas. There has been talk about privatising ZAMTEL but due to pressure from citizens as well performance of other investors this seems to have somewhat simmered down.

3.2 Energy

Zambia is endowed with several types of energy sources including woodlands and forests, hydropower, coal and new and renewable sources of energy. The hydropower resource potential is estimated at 6,000 MW, while the total installed capacity is 1,715.5 MW. Thus, so far, only 28 percent of this potential has been utilised.

Power sector reform in Zambia, like in many African countries, has been driven by several forces: One of these is the need for the sector to contribute more to economic development and

poverty reduction. Another important force has been the lending conditionalities of international financing institutions (World Bank and IMF).

The path towards reforms in Zambia includes three milestones:
(a) Government's promulgation of a National Energy Policy in 1994
(b) Energy Regulation Act under which the Energy Regulation Board (ERB) was established
(c) Electricity Act which permits private sector investment in power sector.

The National Energy Policy (NEP) seeks to develop the largely untapped hydro potential for power generation and provides for the opening up of power industry to private sector and establishment of power industry on a commercial footing.

In seeking to implement this strategy, the Government repealed the Zambia Electricity Supply Act in 1995 abolishing the monopoly enjoyed by Zesco, and passed the Energy Regulation Act. The Act provides for the establishment of an Energy Regulation Board (ERB), which became operational in 1997. ERB is the sole licensing authority for operators in energy sector. The Ministry of Energy and Water Development (MEWD) has the overall responsibility to develop, articulate and implement policy on energy.

The National Energy Policy (NEP) accords priority to rural electrification programme. Accordingly, the Zambian Government created a Rural Electrification Fund in 1994 with the objective to raise funds for rural electrification. This fund is being resourced by charging a levy on all electricity consumption. The Ministry of Energy and Water Development (MEWD) has been administering the Rural Electrification Fund. Further, a Rural Electrification Authority (REA) was created in 2003 to enhance access of rural poor to electricity and reliable energy services. REA is in charge of developing and implementing rural electrification master plans for systematic electrification of rural areas.

The electricity industry is currently characterized by three main players: ZESCO, which is a vertically integrated state-owned utility, the Copperbelt Energy Corporation (CEC), a privately owned Transmission and Distribution Company and the Lunsemfwa Hydro Power Company (LHPC). Despite liberalisation measures, power sector in Zambia continues to be dominated by Zesco, which generates and distributes more than 90 percent of electricity in the country.

In 2001, the Government outlined steps for the divestiture of Government's interest in ZESCO. However, given its past experience in dealing with privatisation of other state enterprises, the Government is now focusing on commercialization of ZESCO's operations instead of privatisation. The road map towards commercialisation involves appointment of a board of directors independent from government interference.

As per current estimates, only 50 percent of the urban population in Zambia has access to electricity, and only 2 percent of the rural population has been connected to the national power grid. In keeping with the New Partnership for African Development (NEPAD), Zambia plans to provide commercial energy services to 15 percent of the population by the year 2010.

In this context, the ERB, with involvement of stakeholders, prepared a power sector restructuring proposal, which has been accepted by the Government. Accordingly, Zambia has started restructuring its energy sector and privatisation is being pursued in phases. The modern concepts such as Independent Power Producers (IPPs) and Energy Service Companies (ESCOs) are being implemented. The large hydropower sector has been opened to private investment and several projects are under negotiation.

3.3 Water Supply and Sanitation

Zambia is one of the most urbanized countries in sub-Saharan Africa with around 43 percent of the population living in urban areas. Although the country has abundant water resources, clean drinking water only reaches around 47 percent of the urban population and more than half of the urban population has no access to adequate sanitary facilities. The largely desolate water infrastructure in low-income areas offers insufficient and often unacceptable service levels with frequent interruptions.

Water sector reforms were introduced in early 1990s to focus was on water supply and sanitation (WSS) services. These were a response to addressing the poor performance of institutions charged with the responsibility of service provision. This performance was a result of a number of factors including unclear roles and responsibilities of institutions, low investment in the sector, low cost recovery, etc. Introduction of public service reforms and liberalisation of the economy during 1990s created a conducive environment for sector reforms. Additionally, the drought from 1991-1993 accelerated the need of a sector reform.

Consequently, in 1994, the Government of Zambia formulated the National Water Policy (NWP) to guide developments in conservation, management, demand and supply of the water resources in the country. The first step in the implementation of reforms was the adoption of certain principles, which served as the basis or guide during the entire reform process. The principles include: Separation of Water Resources Management (WRM) from Water Supply and Sanitation (WSS); Separation of regulatory and executive functions within the water supply and sanitation sector; Devolution of authority to Local Authorities and private enterprises; Full cost recovery on the long run.

The major legal enactment relating to water in Zambia, prior to reforms, is the Water Act of 1948, which stipulates ownership of water and procedures of authorisation and invalidation of water use. As the Water Act of 1948 did not include WSS it was decided to introduce a new Act, the Water Supply and Sanitation Act in 1997, which provides for commercialisation of water supply and sanitation services and for establishment of water supply and sanitation utilities

In accordance with the sector reform principles, service provision (WSS) was separated from WRM and the responsibility for provision of water services was transferred to local authorities (LAs). The Water Supply and Sanitation Act of 1997 provides the LAs with several options by which they can deliver the services, and most LAs opted to establish commercial utilities. This process of commercialisation constituted one of the core activities of reforms. The main idea of commercialisation was that LAs would outsource management of WSS services to institutions established on the principle of achieving full cost recovery.

Realising that water supply and sanitation service provision is a natural monopoly the government established the National Water Supply and Sanitation Council under the Water Supply and Sanitation Act of 1997 to regulate water supply and sanitation services in the country. NWASCO was established in 2000. It's mandate is to balance social and commercial interest, protect consumers from exploitation and water utilities from undue political interference. The decision to establish an autonomous regulator was taken in order to ensure professional management of regulation without any hidden interests or bias.

The reform process was completed by the adoption of a strategy to reform water resources management by creating the Water Resources Action Programme (WRAP) in 2002. Through the WRAP, the government has developed a new institutional framework and is now in the process

of revising the 1948 Water Act to bring it in line with current international trends, and promote integrated water resources management.

The delegating of functions for service provision from Ministries to LAs through corporatised/private companies has helped Ministries becoming leaner and concentrate more on policy making, resource mobilisation and coordination. Delegating regulatory functions has allowed the set-up of an autonomous regulator.

Prior to reforms, urban water supplies were largely run by local authorities (LAs). Of late, the situation has changed as Urban WSS services are now mainly provided by Commercial Utilities (CUs), which are owned by Local Authorities as shareholders. 84 percent of urban population resides in service area of the ten CUs. The remaining 16 percent are still serviced by Local Authorities directly (15 percent) or by private companies that supply water to their employees (1 percent). Generally, service level has improved under CUs while, a continued deterioration can be observed for areas still served by LAs. Coverage of Operation and Maintenance costs at CUs is slowly increasing as collection efficiency is rising (from approximately 20 percent under the management of LAs to an average of 60 percent under the CUs) and water quality is constantly improving since the take over of operation by CUs.

Rural supplies, which were earlier managed by the Department of Water Affairs, are now handled by the Department of Infrastructure and Support Services (DISS).

3.4 Transportation

The transport sector can be grouped into mainly three sectoral sub-groups namely; Road, Railway and Air, with Water being fourth but with minimal contributions to the sector because the country is landlocked.

The Ministry of Communication and Transport is responsible for overall policy formulation and monitoring of transport sector, and has following departments charged with various responsibilities: Road Transport, Zambia Railways, Civil Aviation, and Maritime and Inland Waterways. Besides, there are various statutory bodies that regulate activities in the different sub-sectors. These bodies are not autonomous and their operations are driven by respective Departments within Ministry of Communication and Transport.

The government formulated a national transport policy in 2002 to provide a framework for the development of transport sector so that it meets the requirements of other sectors of the economy. The policy clarifies the role of government and private sector in provision of transport services. The private sector's role is recognised for delivering road and air services, with government establishing an enabling environment.

Among the different transport modes, road transport is a key form of transport to cater for transportation of goods and movement of people especially within borders. Upon approval of the transport policy in 2002, the Government revised the Roads and Road Traffic Act in 2004 and split it into three distinct acts - The Public Roads Act, The Road traffic Act, and the Road Fund Act. Through these legal reforms, the Government established three agencies namely: Road Transport and Safety Agency (RTSA); National Road Fund Agency (NRFA); and Road Development Agency (RDA). Further, the Road Traffic Commission (RTC) and the National Road Safety Council (NRSC) were placed under RTSA, following the passing of the Road Traffic Act. These agencies are responsible for management and disbursement of funds, construction, maintenance and rehabilitation of all roads, and enforcement of road traffic and safety regulations. These agencies became operational in 2005.

Following the demise of the state owned United Bus Company of Zambia (UBZ) in early 1995, the government took measures to encourage private sector to fill the vacuum of passenger transport left by the defunct UBZ. The response has been overwhelming and there is now more than adequate capacity to meet passenger travel demand and allow for healthy competition amongst operators.

The railway transport is a backbone of Zambia's transport system. It has been a major carrier of minerals, country's main export, and accounts for a significant percentage of movement of country's foreign trade. However, railway transport sector has experienced a downward slide because of poor resource allocation and maintenance. Further, the sub-sector is faced with problems of poor state of rail tracks and operating inefficiencies, competition from other modes, weak management and inadequate investment. In order to address these concerns, the Ministry has involved private sector to construct several railway routes on Build Operate and Transfer Basis. Further, Zambia Railways limited was concessionaired to Railway System of Zambia in 2003 to allow the private sector to inject capital into the company which was collapsing.

The railway network in Zambia is at the centre of international routes linking Zambia and the Democratic Republic of Congo to their neighbouring countries, as well as to the seaports in Mozambique, Tanzania, Angola, and South Africa. The Tanzania-Zambia Railway Authority (TAZARA) operates between Dar es Salaam and Kapiri Mposhi in Zambia where it connects to the http://www.nationmaster.com/country/zaZambia Railways system.

The air transport industry was liberalised in 1995 to encourage private sector participation in air transport industry following the demise of Zambia Airways. As a result, a number of private local airlines have entered to fill the gap left by the national carrier. Besides, the Ministry has encouraged revision and signing of additional Bilateral Air Services Agreements with other States whose airlines were interested to operate into Zambia. The Ministry is now in the process of re-establishment of a national airline because of numerous benefits such as: enhancement of national pride and identity; facilitation of regional and international co-operation; and enhancement of security and crisis management. Nevertheless, the policy direction continues to allow private sector participation in both airlines as well as airports. In total, there are 144 airports of which National Airport Corporation manages four, one-third are government-owned and the rest are managed by private sector.

The Department of Civil Aviation (DCA), established by an Act of Parliament in 1954 under Ministry of Communications and Transport is the regulatory agency on air transportation in Zambia. The Aviation Act provides for the control, regulation and orderly development of aviation within Zambia. Its main functions include: implementation and monitoring of standards regarding airworthiness and operations of aircraft; licensing of flight crew, aircraft engineers, air traffic controllers and aerodromes; certification of air operators; and formulation and amendments of aviation legislation.

The water transport system contributes little in both movement of people and transportation of goods. The port of Mpulungu, a small port on the southern end of Lake Tanganyika, handles a minor amount of traffic bound for Rwanda and Burundi and links with the East African rail system. In line with the privatisation programme in Zambia, the Government in September 2000 granted a concession to Mpulungu Harbour Management Limited (MHML) for increasing productivity and efficiency of the harbour, port, freight, transportation and associated services.

3.5 Financial Services

One of the widely recognised principal obstacles to economic growth in Zambia has been the state of financial sector, which currently plays a limited role in the economy. The financial sector is characterised by low financial intermediation (with limited access to financial services for the rural population and the low-to-middle income earners), high costs of funds and undeveloped money and capital market.

Since independence in 1964, the financial sector in Zambia has undergone two notable phases in its development. First, during the early 1970s the Government's nationalisation program had an important impact upon the sector. Although commercial banks were not nationalised, all other major financial institutions were nationalised and merged to form government owned institutions such as the Zambia State Insurance Corporation (ZSIC) and the Zambia National Building Society (ZNBS). A state owned Zambia National Commercial Bank (ZANACO) was established to compete with international banks. The second phase of notable change in the financial sector in Zambia has been the liberalisation of the sector, and the economy generally, since 1991.

Prior to Zambia's economic reforms of the 1990's, the financial sector was strictly regulated. Credit, interest rates and exchange flows were controlled and the legal framework constrained the development of the banking industry. Credit controls entailed direct or selective allocation of funds to certain sectors of the economy, preferably Government, agriculture and mining. In particular, parastatal organizations were given priority and received bulk of the total credit allocated. Interest rates were administratively set with upper ceilings on lending rates and lower ceilings on saving rates while exchange controls were in the form of fixed exchange rate and restrictions on capital flows. Under this paradigm of administrative controls, financial system remained under-developed and repressed.

A growing awareness of these economic costs of financial repression led to liberalisation of the sector. Financial reforms since 1992 have entailed interest rate liberalisation, development of money and capital markets, removal of exchange rate controls and adoption of a market-determined exchange rate. Other measures include improving and modernising payments system and regulatory framework.

Financial regulation and supervision in Zambia has, over the last decade, been structured around specialist institutions and apart from the Bank of Zambia (BoZ), most were established after the liberalisation of the economy in 1991. The BoZ (country's central bank) regulates and supervises commercial banks, non-bank financial sector and micro-finance institutions; the Securities and Exchange Commission (SEC) regulates securities market and Stock Exchange; and the Pensions and Insurance Authority (PIA) oversees operations of pension schemes and insurance business.

The Bank of Zambia was established in August 1964 although the Act establishing the Bank was passed in June 1965. The BoZ Act and the Banking and Financial Services Act (BFSA) provide a legal framework for central bank to carry out its responsibilities. It is charged with the responsibility of formulating and executing monetary and supervisory policies, with the ultimate objective of achieving price and financial systems stability. The BFSA gives the BoZ power to supervise banks and non-bank financial institutions. It also gives the BoZ power to prescribe, issue regulations and guidelines and to enforce them.

During early 1990s, a number of small-scale commercial banks emerged and set up branches in Lusaka and the Copperbelt. The proliferation of small-scale commercial banks demonstrated

how easy it had become to establish a commercial bank. Many of them could not survive competition and collapsed due to their own inadequacies. Their collapse revealed weaknesses in the regulatory frameworks, and called for strengthening of banking laws. As a result, Zambia made considerable improvements in enhancing bank supervision and regulation of commercial banks by the Bank of Zambia. The Banking and Financial Services Act of 1996 has been amended to bring it into line with internationally accepted standards for licensing, prudential regulation and supervision. In 2001, the Banking Act was amended to accommodate for the regulation of micro-finance institutions.

Improvements in bank and non-bank financial regulatory framework have, nevertheless, not changed the nature of competition. Concentration is high, with the five largest banks controlling vast majority of assets in the system. Commercial banks have maintained high lending interest rates partly due to the perceived risk associated with default and the high volume of non-performing loans on their books. In addition, continued high borrowing by Government from banking system through the issuance of Government securities remains an impediment towards further interest rate reduction.

Prior to the liberalisation era, Zambia had no formal capital market. Firms relied mainly on retained earnings and loans from development financial institutions for sourcing long-term finance. Hence, only firms in certain prioritised sectors and those with close ties (informal or formal) to these institutions were in a position to easily expand their activities. In the reform process, development of capital markets was considered as key in enhancing the rate of capital formation and of importance in facilitating privatisation.

In 1993, the Securities Act was passed to allow for the setting up of an institutional framework for the establishment of a formal capital market and SEC as a regulator. SEC is charged with the responsibility of regulating, supervising and developing the securities market in Zambia. Following the enactment of the Securities Act, the Government, with the assistance of the International Finance Corporation (IFC), established the Lusaka Stock Exchange (LuSE) in February 1994. The capital market in Zambia, however, continues to remain small, both in absolute terms and relative to the size of the economy. Trading on the Lusaka Stock Exchange remains limited, with three largest listed firms dominating the exchange.

Pension schemes in Zambia, until 1996, were unregulated and were only required to register with Zambia Revenue Authority (ZRA) for tax exemption purposes. The scenario changed with the enactment of the Pension Scheme Regulation Act in 1996, which provides for administration and regulation of all pension schemes with the exception of National Pension Scheme, which is run by National Pension Scheme Authority (NAPSA).

In insurance sector, the Government had, in 1970, formed the Zambia State Insurance Corporation (ZSIC) as a monopoly insurer by merging the assets of the then 26 foreign private insurers. This state of affairs remained until 1992 when the insurance market was liberalised. This was followed by enactment of the Insurance Act in 1997 to govern the supervision and regulation of insurance industry. The Act provides for licensing of insurers, brokers and other insurance services providers.

With the enactment of the two Acts to govern pension schemes and insurance industry, the government established the Pensions and Insurance Authority (PIA) in February 1997 as a regulatory and supervisory authority for pensions and insurance industry in Zambia. It draws its authority from the Pension Scheme Regulation Act of 1996 and the Insurance Act of 1997.

Unlike other regulatory bodies, PIA is a semi-autonomous entity under the Ministry of Finance and National Planning, and its registrar reports to Minister through Secretary of the Treasury.

The enactment of Banking and Financial Services Act, Securities Act, Pension Scheme Regulations Act and Insurance Act and related legislations have resulted in distinct and separate regulatory responsibilities for the banking, securities, pensions and insurance sectors. This situation has led to a number of overlaps and areas of conflict in the regulatory environment of financial services in Zambia, leaving room for regulatory arbitrage, which remains an issue to be addressed.

4. Evaluation of Sectoral Regulatory Framework

There are a number of sectoral regulatory bodies in Zambia, most of which were either established or reformed to apply their regulatory mandate during the early 1990s especially after the introduction of liberalisation and structural adjustment programmes. This section evaluates the structure and functioning of sectoral regulatory agencies based on a number of indicators.

4.1 Regulatory Institutional Framework

Table 4.1 Regulatory Institutional Framework in Zambia

Sector	Enabling Legislation	Regulatory Body	Appellate Body	Other Agency and its role	
Telecommunications	Telecommunications Act, 1994	Communications Authority of Zambia (CAZ)	High Court		
Energy (Electricity, Oil & Gas)	Energy Regulation Act, 1995 (amended in 2003)	Energy Regulation Board (ERB)	High Court	Rural Electrification Authority	Enhance access of rural poor to electricity
Water Supply and Sanitation	Water Supply and Sanitation Act, 1997	National Water Supply and Sanitation Council (NWASCO)	Minister (relating to licensing)/ High Court (for all matters)	Department of Water Affairs; Water Development Board	Water resources development, management & administration
Road Transport	Roads and Road Traffic Act (revised in 2004)	Ministry of Communications and Transport		Road Transport & Safety Agency; National Road Fund Agency; Road Development Agency (all under Ministry)	Management of funds, construction & maintenance of roads, enforcement of road traffic & safety regulations
Civil Aviation	Aviation Act 1954	Ministry of Communications and Transport (Department of Civil Aviation)		National Airport Corporation	Airport manager, air navigation services
Seaports		Ministry of Communications and Transport			
Banking	Bank of Zambia Act 1965 (revised in 1996) Banking and Financial Services Act 1996	Bank of Zambia (BoZ)	High Court		

Sector	Enabling Legislation	Regulatory Body	Appellate Body	Other Agency and its role	
Capital Market	Securities Act, 1993	Securities Exchange Commission (SEC)	Minister (when SEC gives direction to a Security Exchange)/ High Court (for all matters)		
Pensions & Insurance	Pension Scheme Regulation Act, 1996; Insurance Act, 1997	Pensions and Insurance Authority (PIA) (under Ministry of Finance & National Planning)			

The Zambian government does not follow a common approach towards establishing sector regulators. Following three approaches are observed:

i) Sectors where regulatory bodies have been established as specialised agencies outside of government i.e. telecom (CAZ), energy (ERB), water supply & sanitation (NWASCO), banking (BoZ), and capital markets (SEC).

ii) Sectors where specialised agency has been established to regulate sector, but is not autonomous and is under line ministry i.e. pensions & insurance (PIA).

iii) Sectors which are regulated by line ministry i.e. transportation (road transport, civil aviation and seaports), which is under the Ministry of Communications and Transport.

A second set of variation is observed in the context of establishing single vs. multi-sector regulators. On one hand there is the Energy Regulation Board, which has been established, from inception, to regulate entire energy sector (electricity, petroleum, coal, etc.). On the other hand, in financial services, separate agencies have been established to regulate banking, capital markets, and pensions and insurance respectively. Similar approach is followed in transport sector, where various statutory bodies have been established, besides government departments, to regulate activities in different sub-sectors.

Another feature that emerges is that, in none of the sectors has the government established specialised appellate authority to hear appeals against decision of regulatory body. In fact, in capital market and water supply & sanitation sectors, in certain cases, appeals can be made to the Minister to whom regulator reports. In all cases, otherwise, appeals lie to the high court.

Among key rationales for setting up regulatory bodies is to separate policy-making and regulation functions. The institutional set-up established by Zambia in water supply and sanitation service sector shows how this principle can be followed in true spirit and offers a model for other developing countries to follow (Box 4.1).

Box 4.1 Separation of Policy-making and Regulation Functions: Zambia shows the way

In Zambia, responsibility for water supply and sanitation service provision is under Ministry of Local Government and Housing (MLGH). Therefore, and in order to follow the principle of separating policy making and regulation functions, the regulator, National Water Supply and Sanitation Council (NWASCO) reports to Government through the Ministry of Energy and Water Development (MEWD), which is water sector's "line" ministry.

The issue of which Ministry NWASCO would report to, had been a bone of contention when WSS Act was passed in 1997. There was a disagreement between MLGH & MEWD on reporting mechanism of NWASCO. Initially, a compromise was made to pass WSS Act in 1997 wi thout specifying to which

minister NWASCO has to report. The dispute of NWASCO reporting was resolved by Cabinet one and a half years after passing of WSS Act by confirming the need to separate regulatory function from policy making function in WSS sub-sector. Thus, it was decided that NWASCO was to report to Ministry of Energy and Water Development (MEWD) and that the Minister of MEWD was to appoint NWASCO Board.

4.2 Management Structure and Selection Mechanism

Table 4.2 Appointments in Regulatory Agencies in Zambia

Regulatory Body	No. of Board Members	Appointing Agency	Agency for determining salary, allowances, etc. of members	Term of Office
Communications Authority of Zambia (CAZ)	9 (part-time) members	Minister of Communication and Transport (appointments ratified by Parliament)	Determined by Board with approval of Minister	3 years (renewable)
Energy Regulatory Board (ERB)	7 (part-time) members	Minister of Energy and Water Development	Determined by Board with approval of Minister	3 years (renewable for one more term)
National Water Supply and Sanitation Council (NWASCO)	16 (part-time) members	Minister of Energy and Water Development	Determined by Council itself	3 years (renewable for one more term)
Bank of Zambia (BoZ)	7 members (Chairman and 6 Directors) + Secretary to Treasury (as ex-officio member without power to vote)	President (appoints Chairman) Minister of Finance and National Planning (appoints 6 Directors)	Determined by Minister	Chairman (5 years, renewable for one more term) Director (3 years, renewable for one more term)
Securities Exchange Commission (SEC)	7 members	Minister of Finance and National Planning	Determined by Minister	3 years (renewable)

There are broadly two approaches followed to appoint regulators in Zambia:

i) Nominations from identified stakeholder groups in case of CAZ, NWASCO, and SEC
ii) Selection of eminent persons in case of ERB, and BoZ

In case of nominations, there is variation with respect to powers enjoyed by a line Minister. For appointments to the Board CAZ, it isthe Parliament that ratifies nominations, and the line Minister has no role whatsoever. In contrast, in the case of NWASCO and SEC, relevant line minister is given power to ratify nominations. In cases where candidates are appointed based on their experience and qualifications (ERB and BoZ), line Minister enjoys considerable power, as there is no selection committee to identify prospective candidates and appointments are done on Minister's discretion. Thus, except for CAZ, line minister concerned has a greasay in appointments in all other regulatory bodies.

Be that as it may, independence from line minister enjoyed by CAZ board is limited only till the issue of appointments. The line minister enjoys great power in removal of a member of CAZ. As per the provisions of Telecommunications Act, minister can remove a member of CAZ by giving one month's notice in writing! Thus, a good practice (of appointment procedure) is nullified by this provision of removal. A similar provision exists in case of NWASCO, SEC, and BoZ. Interestingly, members of ERB enjoy immunity from discretionary removal by Minister.

As per the provisions of Energy Regulation Act, Minister cannot remove any ERB member for no reason. However, this provision has limited impact on ensuring independence of ERB, as appointments to ERB, in the first place, is made at the discretion of line minister.

Thus, line minister plays a decisive role in appointments and removal of regulators and this seriously undermines independence of a regulatory body.

Furthermore, remuneration, allowances, etc of regulators is determined by line Minister in case of all regulatory bodies, except for NWASCO, where it is determined by NWASCO council itself.

The board of CAZ, NWASCO and SEC includes representatives of government institutions, private sector, consumer protection organisations and other agencies. There is a merit in this sort of composition as it facilitates a high degree of stakeholder involvement and ensures that the risk of capture by one particular group is kept at a minimum. Interestingly, the Securities Act goes too far and provides that the Lusaka Stock Exchange (LuSE) would be one of the seven institutions entitled to be represented on the Board of Commissioners of SEC, which regulates and supervises the LuSE. Under this structure, the possibility of a conflict of interest is apparent in having a regulated institution sitting on the Board of its regulator. This undermines the objectivity of the Board especially in matters such as the supervision, regulation and disciplining of the LuSE by the Commission.

4.3 Financial Resources

All regulatory agencies, except the central bank, are resourced through license fees and government grants, and license fees are the most significant source of finances. The Bank of Zambia is allowed to retain a part of its profits to meet own expenses and transfer the balance to the Government.

In terms of financing of a regulatory body, the government of Zambia seems to be moving towards less interference. For instance, as per an earlier provision in the Energy Regulation Act, amount collected by ERB as fees was deposited in the general revenue account of the government. Realising that this provision constrained financial independence of ERB, an amendment was made the Act in 2003 to allow for ERB to retain a certain percentage of amount collected from undertakings as licence fees. Accordingly, ERB is now allowed to retain 80 percent of fees collected and remainder is remitted to Ministry of Finance and National Planning.

The same principle (self-sufficiency of a regulatory body) was applied when NWASCO was established. NWASCO is financed by commercial utilities, which pay one percent of their turnover as licence fees to the regulator. Financing through levying a fees on commercial utilities gives NWASCO considerable financial autonomy, an approach that the regulator adopted from the beginning since government funds were only available during the start-off period.

Regardless of the approach towards ensuring financial autonomy, total funds available with a regulatory body relative to its requirements, seems to be low. This emerges in the case of CAZ and SEC. As per information available, CAZ is not considered to be technically abreast to meet challenges of effectively monitoring telecommunication providers, and the reason lies in it being poorly resourced. CAZ had been requesting Government for funds to procure a spectrum monitoring equipment to improve it's capacity to monitor service providers but to no avail. This

is in an environment where service providers have adopted more advanced technological equipment. Similarly, there is a serious under-funding of SEC with the result that it cannot fully meet its statutory function of supervision and oversight alongside its other mandate of developing securities market. For example, SEC cannot implement its approved staff establishment.

In a similar vein, PIA has not been adequately funded to meet its operational needs, which includes training and consumer education. Instead, PIA is wholly dependent on monthly grants from the Government.

Thus, though the government has taken measures to enhance financial autonomy of regulatory bodies, the amount available with regulatory agencies is not enough to help them implement their mandate effectively.

4.4 Staffing and Training

Table 4.3 Staffing and Training in Regulatory Agencies in Zambia

Regulatory Agency	Number of staff	Training	Power to appoint staff
CAZ	32 (sanctioned 43)	Staff encouraged to participate in capacity building programmes sponsored by regional and international organisations	Controller of Communications (responsible for day -to-day operations), with approval of CAZ Board appoints officers; terms and conditions of staff specified by Board, with Minister's approval
ERB	48 sanctioned (increased from 32 in year 2002)		Board of ERB appoint staff and empowered to determine terms and conditions of staff
NWASCO	13 (7 professional, 6 support staff)	Technical assistance received from foreign governments/agencies. Staff sent for short -term training, study tours	The Council independently recruits personnel from open market that are remunerated a market salary scheme
Bank of Zambia			Board of BoZ appoint staff and empowered to determine terms and conditions of staff
SEC			SEC board empowe red to appoint staff and determine terms and conditions

Except for CAZ, all other regulatory bodies are empowered to appoint their own staff and determine their terms and conditions. This allows them to offer staff market-based salary, already witnessed in the case of NWASCO.

In case of CAZ, the Controller of Communications, who is Chief Executive Officer of the regulatory body and responsible for day-to-day operations is appointed by the line minister. Further, terms and conditions of appointment of other CAZ staff require Minister's approval. This highlights a lot of interference by line minister in the functioning of CAZ.

4.5 Regulatory Mandate and Enforcement

Telecommunications

The Communications Authority of Zambia (CAZ) was established by Government in order to regulate the provision of telecommunication services in the country. The main functions of CAZ are:

- Licensing new operators
- Develop rules and procedures that would promote and safeguard social requirements and competition in the telecommunications sector;
- Protect the interest of users and consumers of telecommunication services;
- Create a fair playing field for operators and investors;
- Administer effective and efficient utilisation of the Radio Frequency spectrum.

Nevertheless, as per the Act, CAZ is subject to the control and direction of the Minister in the exercise and performance of its powers and functions. This provision facilitates Ministerial intervention in the functioning of CAZ. Not surprisingly, questions have been raised about the independence of the regulator, who is seen in the private sector as a government agent and doing nothing when it comes to regulating the state-owned incumbent. There are several cases of restrictive practices by Zamtel, especially complaints made by ISPs, and the regulator is perceived to have failed in curbing such practices.

For instance, ZAMTEL through its subsidiary Zamtel Online provides dial-up and leased line and wireless Internet access. All Internet access calls to ZAMTEL Online are metered as local calls regardless of their origin. This has had the positive effect of reducing call charges, which account for the bulk of monthly Internet access charges, especially for users located outside Lusaka and the Copperbelt. However, through its monopoly ownership of the fixed line access network, this practices gives unfair competitive advantage to Zamtel, which is engaging in cross-subsidization - effectively locking out other ISPs from the distance-independent Internet market across the country. Secondly ZAMTEL uses discriminatory pricing for broadband access in that other ISPs are charged 3-4 times more for the same service compared to ZAMTEL's non-ISPs customers. ISPs accuse that ZAMTEL is using its integrated service nature to sell its Internet services cheaply. They have made presentations before the Zambia Competitions Commission to review this arrangement, as CAZ has not been found to be effective in handling the issue.

Tariff regulation

There is no direct regulation of prices for services offered on the market by the operators. Market players come up with price adjustments according to market demands and these are passed to the regulator for scrutiny. The regulator looks for justification and once satisfied, approves the proposed rates. Information asymmetries between the operators and the regulator, compounded by a lack of skill and experience at CAZ have rendered price regulation futile. At no time has the regulator turned down a price hike by any of the operators be it ISP or Mobil service operators.

Interconnection

The Controller of CAZ is empowered to set out the terms for interconnection between networks where the two operators cannot agree between themselves. This is fundamental to promoting competition because it enables customers of one network operator to contact customers of the other and *vice versa*.

CAZ has been trying to negotiate the regulation of network interconnection between mobile operators and fixed line carrier, ZAMTEL through a number of consultative meetings with the

operators. Since all parties, especially the private companies did not agree to a uniform figure for termination charges, CAZ came up with its own figure (cost-based tariff), in line with international practice. However operators have yet to demonstrate that their tariffs are cost based and the information asymmetries that exist between the operators and the regulators make this difficult to enforce.

The Minister has also established a Telecommunications Users Advisory Committee to consider complaints and comments from users of telecommunication services. The Committee is responsible to the Minister and performs such functions as the Minister prescribes.

Is the CAZ independent?
The establishment of CAZ was to safeguard the market against distortionary practices. The question is, has the regulator delivered on its mandate. In the Government's eyes, the regulator has delivered. In the opinion of the private sector the regulator is only responding to his master's voice. The regulator, being part and parcel of the line-Ministry is seen as carrying out Government instructions.

This concerns stems from the fact that the regulator sits on the board of ZAMTEL. This creates a conflict of interest in that both are players and referee in the telecommunication sector. The separation of policy, regulation and operations between Government, the national regulatory agency and the operator is a fundamental principle of the international reform model to which Zambia has committed itself. The feeling of many stakeholders is that since the regulator was a creation of parliament, it should be independent from the government line ministry and be answerable only to the parliament. The Telecommunication Act of 1994 clearly stated that the regulator should be independent from the line Ministry but this has not been put in practice in the spirit or the word of law.

The CAZ falls under the Ministry of Transport and Communication. This has led to the general belief in the private sector that the CAZ is an extension of the Ministry and carries out Government orders and therefore its independence as a regulator is very much in doubt and biased towards Government thinking especially when it comes to making decisions that might affect the operations of the state owned company in the sector. It is believed that while competition is permitted one cannot fairly compete against the state owned company as the regulators may put in place regulations that will impede such competitions. The ICT Policy that is currently being drafted in Zambia seeks to address this issue.

Energy
The specific functions of the ERB as mandated in the Energy Regulation Act are the following:

- Issue licences
- Monitor the efficiency and performance of undertakings
- Investigate complaints received from consumers on price adjustments by any undertaking and services provided by undertakings, and regulate such price adjustments and quality of services
- Approve location and construction of, and receive and investigate complaints concerning location or construction of any common carrier or any energy or fuel facility or installation

ERB seeks to promote competition and ease of entry into the energy sector as well as safeguarding consumer interest. Its regulatory mandate includes petroleum products, electricity, solar energy and other forms of energy, though oil and electricity sector are key focus areas.

The ERB has since inception scored many successes. It has introduced complaints procedure to resolve consumer complaints, developed standards to monitor efficiency and performance of regulated undertakings, developed inspection procedures and other guidelines. For instance, in petroleum sector, ERB has drawn up guidelines for prospective operators wishing to build a depot or service station. Such measures have helped instilling confidence among investors. Thus, when the ERB came into existence there were five Oil Marketing Companies (OMCs) operating in the country. The number has since gone up to 13.

Be that as it may there are certain provisions in the Act that undermine ERB's decision making power. For instance, as per the provisions of the Act, ERB is required to seek Minister's consent prior to revocation of a licence or refusal to renew a licence.

Tariff regulation

Since establishment of the Energy Regulation Board (ERB), variation of electricity tariffs has been based on Revenue Requirement Approach and Automatic Tariff Adjustment Formula (ATAF). Revenue requirement approach allows a utility to earn enough revenue to recover all costs that are deemed just and reasonable, including a reasonable return on investment. ATAF is meant to restate the approved revenue requirement in real terms. Since 1995, the ERB has handled 10 tariff review applications from ZESCO LTD, Zambia's main electricity utility company. Five of these have been full tariff reviews based on 'revenue requirement' approach while the rest have been based on the ATAF.

The law requires an electricity utility to apply to the Energy Regulation Board (ERB) when intending to alter its tariffs and also requires the utility to give notice to its customers of the intention to alter retail electricity tariffs. The law further provides for objections from the public. In the event of receiving no objections, the ERB can on its own motion review the undertaking's proposal. The ERB decision is final and not subject to appeal. Unfortunately, apart from representatives of industry, very few quality objections are received from the general public.

Consumer protection

The ERB, with the involvement of various stakeholders has prepared an Electricity Consumer Charter aimed at protecting consumers, and ensuring the obligations of energy utilities and consumers are rightly stated. The ERB also receives, investigates and resolves consumer complaints using the Complaints Procedure developed by the ERB. Any person or consumer may seek ERB's intervention if they are dissatisfied with the handling of their complaint by an energy utility.

ERB, CAZ and National Water & Sanitation Council (NWASCO) have recently agreed to form joint consumer Councils or watch groups that will cut across three sectors namely communications, energy and water. These groups will act as regulators' link between consumers and service providers. They would serve as an important contact point to channel consumer complaints, queries and other concerns pertaining to the quality of services or goods. NWASCO already has water watch groups, which would be transformed to represent the three sectors.

Water Supply & Sanitation

The main functions of NWASCO, as established under the WSS Act, are advising government institutions, licensing of utilities, developing guidelines for WSS, establishing and enforcing standards for the design and management of utilities, advising utilities and other service providers, disseminating information to consumers, as well as other activities. NWASCO has powers to enforce its functions through the licensing and tariff setting process and through enforcement notices and penalties.

NWASCO has been involved in a lot of activities to meet its main objective of regulating quality of service and pricing of water and sanitation services to protect consumers from exploitation. These include carrying out on spot as well as intensive inspections on water utilities to monitor their performance. NWASCO has also introduced an information system with the view to improve reporting system and data collection from the Commercial Utilities (CUs). NWASCO facilitates competition amongst utilities by benchmarking, thus creating comparative competition in the absence of market competition. The main tool used is NWASCO's annual comparative sector report. With this, the behaviour and activities of providers have become more transparent and they are more accountable to policy makers and public.

Be that as it may, the conflicting perception of roles by government institutions hampers cooperation in the sector and does not present an image of a united water sector. Government departments have still not fully recognised the legal authority given to NWASCO. Consequently, when the latter instructs providers it is often perceived as interference in the power of the ministries even when the objective of the action is shared. There are certain provisions in the Act, which give powers to the Minister to override a decision of NWASCO. For instance, any applicant for a licence who is aggrieved by a decision of the Council may appeal to the Minister, who in determining the appeal may confirm, vary or set aside the decision of the Council

Tariff regulation

One of the principles of reform was for water supply and sanitation sector to attain full cost recovery through user charges in long run. When CUs started operations, most tariffs in the sector were very low with little or no semblance of costs of providing the service. Therefore, NWASCO tried to increasingly standardise the tariffs.

Tariff adjustments are now no longer dictated by politicians. NWASCO's power with regard to price regulation is based on the WSS Act. Applications for tariff-adjustments by providers go through a number of stages before final approval by the regulator. Before submitting a tariff adjustment proposal a provider has to hold a consultative meeting with customer representatives. The regulator links tariff adjustments to sustainability of systems and to performance of providers. NWASCO prevents consumers from paying for the inefficiencies of service providers and seeks to ensure that social interests are taken into account. The CUs are allowed to charge tariffs that allow them to at least cover current operational costs. Consequently, regulation not only serves the interests of consumers and public but also service providers.

The autonomy of the regulator NWASCO was demonstrated in 2002, when a few months before general election, tariff increases of up to 100 percent were approved.

Consumer Protection

NWASCO has established water watch groups (WWGs), which encourages consumers to resolve their complaints directly with providers. WWGs are composed of volunteers from consumers responsible to deal with unsolved disputes between customers and service providers before the regulator is engaged.

WWGs, as a sub-structure of NWASCO, are a very good example how customers can be mobilised to solve disputes between consumers and providers. They are an appropriate means to extend regulation on the ground in order to reinforce consumer protection and at the same time limit cost of regulation. The WWGs not only involve customers in resolution of conflicts with providers but also help to sensitise customers about their responsibilities such as taking care of the infrastructure and paying bills on time. The WWGs also advise on adjustments to regulations

and guidelines and educate consumers on the role and functions of NWASCO. The pressure created by NWASCO and the WWGs have made commercial utilities decide that customer complaints are an issue for top management at head quarters and can no longer be left to sub-ordinates at regional level. The Water Watch Groups (WWGs) concept has proven to be very successful in establishing the regulator's presence on the ground.

NWASCO has tried to give special consideration to poor in all its regulatory tools. Through the definition of service coverage areas in licence agreement, the regulator obliges CUs to provide services to low-income urban areas as well. Recognising the challenges for CUs to fully meet coverage targets, NWASCO issues guidelines on service provision to urban poor through water kiosks, which have been successfully implemented for the past one decade. The regulator has also put in place Devolution Trust Fund (DTF), a basket-financing instrument that provides funding to CUs to extend their services to urban poor.

Banking

The Bank of Zambia (BOZ), the Central Bank reports to the Ministry of Finance, supervises and regulates the Banking Sector. The BoZ has also been responsible for controlling inflation though it is not fully independent from the government.

The principal Act governing the functioning of BoZ was amended in 1996. Consequently, the BoZ, which had the primary responsibility of formulating and implementing monetary and financial system policies, witnessed its functioning confined to ensuring price and financial system stability. Accordingly, among the key functions of BoZ are to license, regulate and supervise banks and financial service institutions to ensure a safe and sound financial system.

The Bank of Zambia also has regulatory responsibility of supervising Non-Bank Financial Institutions (NBFIs) in the country. The Regulatory Policy Division of BoZ regulates and supervises NBFIs under the Banking and Financial Services Act in order to promote a competitive, safe and sound financial system.

Under the current legal framework, the independence of the BoZ in executing its duties is compromised. The BoZ Act provides that *"The Minister may convey to the Governor such general or particular Government policies as may affect the conduct of the affairs of the Bank and the Bank shall implement or give effect to such policies.*" The mandatory tenor in which this provision is couched leaves little doubt of the overriding influence that the minister may wield over the BoZ on some policy matters. The lack of central bank independence has, in fact, resulted in recommendations and decisions made by the BoZ being overridden by the Ministry of Finance and National Planning.

4.6 Interface with Competition Authority

The law on competition and fair-trading seeks to control or eliminate restrictive business practices including agreements on mergers and acquisitions or abuse of dominant positions, which may limit access to markets or otherwise unduly restrain competition. Therefore, the interface between ZCC and sector regulators requires strengthening at policy and operational levels. There are some visible examples of regulatory co-ordination in some of the sectors in Zambia. For instance the ERB and CAZ co-operate with the Zambia Competition Commission (ZCC) in dealing with competition concerns affecting their respective sectors. The Banking sector is the weakest in terms of interface with other agencies such as competition commission.

The Communications Authority has links with the ZCC at board level and is equally empowered to address competition concerns. It has been working together with the ZCC to restructure the Zambia Telephone Company in advance of privatisation by unbundling internet, landline and mobile services into separate companies.

The Energy Regulation Act also deals with competition issues and the Act specifies functional co-operation with ZCC and other agencies. As per the Act, ERB is required to work in conjunction with the Zambia Competition Commission to monitor levels and structures of competition within the energy sector and develop and implement appropriate rules to promote competition.

The Executive Director of ZCC sits on the Water and Sanitation Council, which helps to address competition issues in the sector. However, the banking sector has not emulated the spirit of competition in the market and there is need to look at anti-competitive behaviour of banks in Zambia.

The relationship between ZCC and other sector specific bodies is still evolving. At present close relations exist with Energy Regulatory Board at committee level. In practice, ZCC refers relevant cases to sector specific regulatory bodies where this applies. A good example of co-operation between the Zambia Competition Commission and sector specific regulatory body is the case of the oil-marketing cartel (see Box 4.2).

Box 4.2 Zambia's Competition Authority and Energy Regulator collaborate to check oil cartel

All oil marketing companies (OMCs) in Zambia buy their petroleum requirements from Indeni Refinery, which processes imported crude oil and sells refined petroleum at wholesale prices. In May 1999, the Indeni Oil Refinery was gutted by fire and oil marketing companies (OMCs) were allowed to import refined petroleum products. The Government reduced customs duty from 25 to 5 percent. Despite importing from different sources and facing different operating cost, pump prices for petroleum products remaine d the same. The ERB and ZCC observed that OMCs acted collusively in price adjustment since 1997. The OMCs selected one company to apply for price adjustment to the sector regulator and all parties implemented the decision of the regulator uniformly and at the same time. It was further observed that OMCs had regular meetings where exchange of information on sales volumes and prices were discussed. When small OMCs attempted to charge lower prices on the basis of their cost structures, cartel leaders immediate ly reacted by reducing pump prices at service stations in the vicinity of service stations of defiant operators until they complied with standard behaviour on prices. In this context, the ZCC and ERB collaborated to initiate prosecution of the firms for ca rtel behaviour.

4.7 Decision-making Process

Table 4.4 Decision-making Process in Regulatory Agencies in Zambia

Regulatory Body	Decision-making process
CAZ	• Licences issued based on pre -determined guidelines and qualifying criteria that applies to all service providers
ERB	• Public hearings in certain cases (e.g. tariff changes)
NWASCO	• Developed a National Information System as a support tool in decision making • All interest groups involved in decision -making process
BoZ	• Consults the Ministry of Financ e and National Planning, commercial banks and NBFIs on monetary policy • Interference of Minister on monetary policy matters

Among the regulatory bodies, only ERB and NWASCO are known to involve various stakeholders in decision-making. This is true for ERB in a limited sense. ERB invites comments from public on proposals of tariff increases by regulated entities. Public hearings are held and decisions communicated to public through media and scripts made public.

The decision-making process followed by NWASCO is quite wide ranging as it seeks to involve various stakeholders at all levels of decision making. It has developed a national information system (NIS) on urban water supply and sanitation, which enables it and other stakeholders to observe developments in the sector. The information gathered in the NIS serves as a support tool in decision-making.

From the beginning of reform process in WSS sector, particular emphasis was put on stakeholder participation. The advantage was that stakeholders and public were aware of reforms and its principles. Particularly the process of commercialisation involved considerable consultation at all levels, in order to sensitise them on the new legal and institutional framework and the coming new water management approach. Media was regularly briefed to sensitise stakeholders. As a result water issues became high on national development, social and political agenda with politicians and other decision makers being well informed of the progress and developments in the sector.

Consumer involvement in tariff setting process is guaranteed through consultative meetings, which the commercial utilities are obliged to hold with consumer representatives before applying for tariff adjustments. The minutes of meeting of these consultations are part of tariff adjustment proposal submitted to NWASCO. Decision making is separated from political constraints and a high degree of transparency and control is ensured through the supervision of the regulatory management by a Board with representatives from all key stakeholders. This makes the secretariat of the regulatory body accountable for all their actions.

4.8 Accountability Mechanism

Table 4.5 Accountability Mechanisms for Regulatory Agencies in Zambia

Regulatory Agency	Minister/Parliament	Appellate Body
CAZ	Annual report of activities submitted to Minister, *who tables it before Parliament*	Judiciary
ERB	Annual report of activities submitted to Minister, *who tables it before Parliament*	Judiciary
NWASCO	Annual report of activities submi tted to Minister, *who tables it before Parliament*	Minister (relating to licensing)/ High Court (for all matters)
BoZ	Annual report of activities submitted to Minister, *who tables it before Parliament*	High Court
SEC	Annual report of activities submitted t o Minister, *who tables it before Parliament*	Minister (when SEC gives direction to a Security Exchange)/ High Court (for all matters)

As observed, all regulatory bodies are required to submit their annual reports to line minister concerned, who then tables these before parliament. Further, parties aggrieved by a regulator's decision can appeal to the high court. There is no specialised appellate authority established to hear appeals against decision of regulatory body, as is the case in several other countries.

The situation in water supply & sanitation sector and capital markets is of concern. In specific circumstances, parties aggrieved by a regulator's decision, can appeal to the line minister concerned, with the High Court being the final arbiter. This adds to powers already enjoyed by line minister with respect to functioning of regulatory bodies. Allowing aggrieved parties appeal to line minister against regulator's decisions, undermines credibility of regulatory framework in both these sectors.

5. Concluding Remarks

Zambia embarked on its reform programme with a view to transforming state-led, economy into a market driven economy. Realising the importance of private investment in enhancing economic growth, government enacted suitable policies and legislations. Sector regulators have been established which seek to ensure orderly and stable development of a sector by promoting investment as well as ensuring fair competition and fair treatment of consumers.

All sector regulatory laws in Zambia seek to follow the principle of separation of policymaking, regulatory and operational functions in a sector. Zambia has come a long way from the times when same agency performed policy-making, regulatory and service provision functions. The Minister's role is now primarily related to policy-making; a specialised body performs regulatory functions; and state-owned entities and other private operators provide services.

Nevertheless, the situation is far from rosy. In most cases, line ministers, though have relinquished regulatory functions to sector regulators, continue to oversee functioning of regulatory body and state-owned service provider, thus belying the principle of separation of functions. This is true for telecommunications and energy sector. The structure in capital market presents an interesting scenario, where the regulated (Lusaka Stock Exchange) is on the board of regulator (Securities Exchange Commission). In either case, possibility of a conflict of interest is apparent which undermines functioning of regulatory regime.

In contrast, the institutional structure adopted in water supply and sanitation sector shows how this principle can be followed in true spirit. Ministry of Energy and Water Development (MEWD) has been made line ministry for NWASCO, the sector regulator, whereas responsibility for water supply and sanitation service provisions lies with Ministry of Local Government and Housing. This arrangement in one stroke addresses conflict of interest issues. There is need for Zambia to address these variations in approaches towards sectoral regulation and apply good practice in one sector to other sectors as well.

There are several other variations observed in regulatory regime that has been established in Zambia, and there seems to be no sign of coherence in regulatory law making. For instance, NWASCO and the pensions & insurance authority (PIA) were established in the same year i.e. 1997. But while NWASCO has been set up as autonomous agency outside of government set-up, PIA has been set up as a semi-autonomous entity under the Ministry of Finance and National Planning, its line ministry.

Similarly, while on one hand there is the Energy Regulation Board, which has been established, from inception, to regulate entire energy sector (electricity, petroleum, coal, etc.). On the other hand, in financial services, separate agencies have been established to regulate banking, capital markets, and pensions and insurance respectively.

There exist a number of overlaps and areas of conflict in regulatory environment of financial services leaving room for regulatory arbitrage. Further, technological improvements and globalisation have resulted in emergence of complex financial structures which have blurred the traditional product boundaries among banking, securities and insurance sectors. In the light of these changes, there is a view that a single integrated body responsible for overall supervision would create an enabling environment for better convergence of policies by bringing all regulatory functions together in a harmonious manner. The issue of whether to have separate specialist bodies or a unified supervisory agency and manner in which integrated regulatory body would be structured, and how to implement and manage the integration process continues to be debatable, and Zambia should start the deliberation process.

Though the thinking in Zambia has been to distance regulatory functioning from line ministers, sector regulatory laws empower line minister to play a decisive role in appointments/removal of regulators. This seriously undermines independence of a regulatory body. Here again, as observed in the paper, good practice at one stage (either in appointment or removal procedure) is nullified by a bad practice in other stage.

Similarly, while government has taken measures to finance regulatory agencies from sources independent of government budget, total funds available with a regulatory body relative to its requirements, seems to be low. This affects the capacity of a regulatory body to implement its mandate and to appoint skilled persons based on a market salary scheme.

There are similar cases of provisions that nullify a good practice. For instance, the board of CAZ includes representatives of various stakeholders that facilitates a high degree of stakeholder involvement and ensures that risk of capture by one particular group is kept at a minimum. However, Telecommunications Act makes CAZ's functioning subject to the control and direction of line Minister. Therefore, irrespective of what decision this multi-stakeholder group takes, it could be subject to Minister's discretion. Same is the case with Bank of Zambia where Minister has been empowered to override decisions of BoZ on policy matters. Such provisions have raised questions about credibility of regulatory agency.

What emerges is that the government of Zambia has sought to establish sectoral regulators in a half-hearted manner. There are certain good practices followed, but the issue has not been looked at in a holistic manner. The government needs to develop a coherent approach towards establishing sector regulators and provide them with required power and resources to implement their mandate. At the same time, government needs to strengthen mechanisms to make regulatory bodies accountable. The practice followed by NWASCO of establishing water watch groups is a good example to ensure participation of public in regulatory process and enforcement of regulation at ground level. It is good to see the practice being expanded to include energy and communications sector. Similar measures are required to ensure credibility of regulatory regime in Zambia.

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Chapter V
Regulatory Environment in India

1. Introduction

India is located in South Asia bordering Bangladesh and Myanmar to the east, Pakistan to the west and China to north and the north-east.

INDIA COUNTRY PROFILE	
Population:	1.1 billion ***
GDP (Current US$):	599 billion ***
Per Capita Income: (Current US $)	530 (Atlas method)*** 2,670 (at PPP.)**
Surface Area:	3.3 million sq. km
Life Expectancy:	63.7 years
Literacy (%):	61.3 (of ages 15 and above)**
HDI Rank:	127 ***

Sources:
- World Development Indicators Database, World Bank, 2004
- Human Development Report Statistics, UNDP, 2004

(**) For the year 2002
(***) For the year 2003

The entire country is divided in 29 states and 6 union territories. Democracy is deep rooted in the political system. India's richness and diversity of culture, geographic and climatic condition, natural and mineral resources are matched only by few other countries in the world.

India has strong institutional base for higher education and some of the institutions of technical and management education are considered amongst the best in the world. Yet early dropouts from schools still remains a major concern. India is the second most populous country in the world, of which nearly one-fourth live below poverty line.

After independence, India followed the Soviet styled industrialisation that required extensive State intervention along with import substitution. Since July 1991, it has radically liberalised its economy and, today, actively engages in the promotion and protection of competition in its markets. A new spirit of economic freedom is now steering the country. A series of 'second generation reforms', aimed at further deregulation and stimulating foreign investment has moved India firmly into the front ranks of growing economies.

With a gross domestic product (GDP) of about US$530bn in year 2003, India is emerging as a promising economy and one of the largest markets in the world. It is the fourth largest economy in terms of Purchasing Power Parity. The economy has posted an average growth rate of 6 percent during 1990s.

India's economy encompasses traditional village farming, modern agriculture, handicrafts, a wide range of modern industries, and a multitude of support services. Agriculture, which contributes 22 percent to the GDP, continues to be the mainstay for nearly 65 percent of the population. The contribution of industry has come down to 26 percent, while that of services has increased to approximately 51 percent. The country is capitalising on its large numbers of well-educated people, skilled in the English language, to become a major exporter of software services and software workers.

Tea, minerals, garments, Information Technology and services are the major exports for India. The proportion of IT services in the export portfolio of India is increasing at rapid pace. Petroleum crude and derivatives, heavy machinery, and steel are among the major commodities which India imports.

2. Evolution of Economic Policy Regime

Prior to independence in 1947, India's economy was stagnated and industrial development was restrained by the colonial regime. After independence, democratic government was sworn in and a mixed economy approach was adopted with an inclination towards socialism. Policies were skewed in favour of Soviet Model where role of market was undermined and the State assumed increased responsibility of overall development of the country.

The new leadership of India decided to direct economic growth and invested heavily in core sectors. Public sector enterprises were set up to dominate heavy industry, transport, energy, telecommunications etc. The Industrial Policy Resolution of 1956 aimed at achieving a socialistic pattern of society through adoption of economic policies that promote equitable distribution of wealth and economic power. Private sector was restricted to produce selected goods and licensing was used as one of the policy instruments to channel private investment. Import substituting development strategy was followed to attain self-reliance. Cross-border trade was not encouraged and strict restrictions were imposed on imports.

Many enterprises, including commercial banks, were nationalized and license and quota regime was adopted to direct and control economic activities. Bureaucracy was commanding control over decision-making on economic issues and lack of transparency roped in corruption. Several goods were included into restricted lists which private sector was not allowed to produce. Similarly, small-scale industries were also given protection by not allowing large-scale industries to compete with them.

These measures created distortions in allocative efficiency, and constricted domestic production and competitiveness in Indian industry. By mid 1980s, adverse outcomes of excessive reliance on government and under-utilization of private resources started surfacing and Indian economy continued to stagnate with a lower order of growth. Reliance on borrowings from foreign sources increased substantially. The gulf war in 1990 and its impact on oil prices compounded the problem and led to a severe balance of payment crisis in 1991.

Responding to the crisis, India embarked on a series of economic reforms. Reform measures consisted of liberalising foreign investment and exchange regimes; reduction in tariffs and other trade barriers; modernisation of financial sector; lowering state regulations on private sector; and adjustments in monetary and fiscal policies. With every passing year a general consensus on reforms has emerged among major political parties. Subsequent governments have continued with the reforms, though at varying pace.

The economic reforms have resulted into several favorable outcomes such as higher growth, lower inflation, and significant increase in foreign investment. Foreign portfolio and direct investment flows have risen significantly since reforms began in 1991 and have contributed to healthy foreign currency reserves and a moderate current account deficit. Significant liberalisation of investment regime since 1991 has made India more attractive destination for foreign direct and portfolio investors. Foreign investment is particularly sought after in power generation, telecommunications, ports, roads, petroleum exploration and processing, and mining.

The slow but steady implementation of the economic reform agenda has driven the growth of the country and market forces are increasingly allowed to play significant role. The economy has shifted its focus from inward looking import-substituting growth strategy to an outward-looking export-led one. The social and economic infrastructure sectors have been opened up for private

participation. The benefit arising from privatisation and competition in sectors like telecommunications, transport, health, education etc has given sufficient backing to the changing mind-set of people.

3. Evolution of Sectoral Regulation

As has been the case in most developing countries, Government of India traditionally performed multiple roles of policy maker, regulator, and service provider in most infrastructure services. During early nineties, occurrence of an economic crisis forced the government to revisit this role. Contribution of private sector has been realised to supplement the efforts of the State and allow market to play greater role.

Over the years, especially after economic reforms were initiated in early 1990s, a number of sectoral regulatory authorities have been formed. For telecom, there is the Telecommunications Regulatory Authority of India (TRAI). For electricity, there is Central Electricity Regulatory Commission (CERC) at the federal level and State Electricity Regulatory Commission (SERC) in most states. Securities and Exchange Board of India (SEBI) looks after the operation of the capital market while the banking and the financial sectors are regulated by the Reserve Bank of India, the central bank. Insurance Regulatory & Development Authority (IRDA) has been created to regulate the newly opened insurance sector. There are other statutory bodies for regulating some other sectors and some more are in the offing (e.g. oil & gas).

Independent regulatory regimes have been set up with the expectation that insulation of economic decision making from political establishment would contribute towards consistent and rational policy environment, provide level playing field to competitors and reduce perceived regulatory uncertainty amongst private investors. Regulators were also entrusted to ensure access to common carriers in network industries.

Following is a brief discussion on evolution of regulatory regime in selected sectors in India.

3.1 Telecommunications

Till the 1980's, India's telecommunications industry was almost entirely controlled by the government, which performed all roles including licensing, policy-making, regulations and operation of services.

With the introduction of several new electronic communications services in early 1990's, the Government allowed private sector to provide the new "value-added services". Rather unusually, cellular mobile services were classified as value added services. In effect, the opening of cellular services to private sector operators heralded the beginning of network creation by private entrepreneurs.

The National Telecom Policy (NTP-94) outlined the basic policy framework for the development of the telecommunication sector. It allowed private sector, including foreign companies (subject to equity participation upon 49 percent) to provide all services and referred to the large investment (INR 230bn) required to meet the telephony targets spelt out in the policy as the main reason to invite private sector participation.

With the entry of private sector players in the cellular market, India's telecom sector, for the first time experienced competition in the provision of telecom services. The Telecom Regulatory Authority of India (TRAI) was set up in 1997; well after mobile services had begun in 1995.

The government players, Mahanagar Telephone Nigam Ltd. (MTNL) and Department of Telecommunications (DoT), initially opted out of the mobile market. It was felt that fixed line demand needed to be addressed first and highly priced mobile services had a little role in a poor country like India. However, the two operators soon realised the potential, mobile telephony had in India, and resorted to actions that were objected by TRAI. This led to turf war between the government and the TRAI that went to the courts, which ruled against TRAI (see Box 5.1).

The private operators felt that the regulatory regime did not provide sufficient incentive or security to new investors. Faced with the dilemma of allowing the private operators to die and face the resulting bad publicity or changing its approach, the government chose the latter. It announced a change in policy through the formulation of New Telecom Policy 1999. Creation of a competitive telecommunications sector was for the first time recognized as an objective, as was the need for a level playing field.

The same year, government issued an ordinance to amend the TRAI Act and reconstituted the regulatory body (see Box 5.1). The amendment gave TRAI exclusive mandate to fix and regulate tariffs and interconnection and removed all government say in these two functions. It also mandated the government to seek advice from TRAI before it licensed a new operator, although such advice would not be binding. TRAI was reconstituted and the Telecom Dispute Settlement and Appellate Tribunal (TDSAT) created to which inter operator disputes, operator-government disputes, and appeals against TRAI's decisions could be made.

The operating company Bharat Sanchar Nigam Limited (BSNL) was carved out of the DoT in 2000, leaving a smaller DoT to deal with policy making and related government functions including licensing and spectrum management.

Presently, the government is policymaker and seller of telecom operating licences. It also owns all the equity in India's biggest telecom company called Bharat Sanchar Nigam Ltd (BSNL). The TRAI is supposed to regulate BSNL, however both of them report to the Department of Telecommunications!

The competitive pressure following the entry of two more mobile players in 2001 led to a considerable fall in prices and expansion of services. However, there is limited competition in the fixed line business, as BSNL and MTNL between them control almost 95 percent of the fixed line subscribers. Private sector companies Reliance and Bharti lead the market shares in the mobile business with BSNL, a close third.

Competition in the long distance market has led to over 75 percent fall in long distance rates both nationally and internationally. Internet market too has begun to show the fixed line incumbents as the likely winners.

At present, the sector is on high growth trajectory with a phenomenal growth in mobile segment. The number of mobile subscribers has surpassed that of fixed line. The market is competitive and at least three operators are present in most of the circles[20]. In the case of fixed line services, which are still the mainstay of most rural consumers, the situation is problematic. In most cases, only one operator, BSNL, serves rural areas. Most rural consumers in India still do not have

[20] The entire country is divided in 20 circles, categorised as A, B and C based on their revenue potential. Licences are awarded separately for each circle. The telecom regulator has recommended moving to a unified licensing regime, which includes issuing one all-India license rather than circle-wise licences.

access to competition and its consequent benefits through more attractive prices, quality as well as actual choice.

Box 5.1 The TRAI Fiasco: An Account of Difficult Times faced by Indian Telecom Regulator

In 1999, the tussle over turf issue between the government and the Telecom Regulatory Authority of India (TRAI) reached such a level that the government amended the TRAI Act 1997 and in the process reconstituted the TRAI. Since the Act protected the Members of the authority, as their removal was subject to proven guilt in a judicial probe, there was no other way through which the government could get rid of the then members of TRAI.

The spate began in 1999 when DoT announced a tariff hike for calls made from fixed lines to mobile phones. Soon after, MTNL announced plans to enter the mobile market. Mobile operators were soon knocking the doors of the newly created TRAI, which provided them quick relief and quashed the DoT's tariff proposals. Later, it disallowed MTNL from entering the mobile market on grounds that the terms and conditions of its licences were unavailable and the government had not sought TRAI's prior approval when it licensed MTNL to provide mobile services. TRAI also came out with directions to move mobile operators to a 'Calling Party Pays' (CPP) regime where mobile users, like the fixed one, would pay only to make outgoing calls

The government-owned Department of Telecommunications (DoT) and the Mahanagar Telecom Nigam Ltd (MTNL), the two largest service providers appealed to the high court (provincial court) against TRAI's decisions, challenging its jurisdiction over matters relating to licensing and tariff. The DoT won its appeals against TRAI. The Government, according to the High Court, did not need to consult the TRAI on any licensing decisions. The TRAI did not also have the right to alter revenue sharing arrangements, i.e. interconnection terms of operators, since this function stemmed out of the operators licences and the TRAI's role in licensing was only limited.

Subsequently, the government of India decided to rewrite the TRAI law and sacked existing heads and members. All but one member of the erstwhile TRAI were removed and replaced by a team, which in the new dispensation enjoyed no legal protection, beyond a right of being heard, if the government wished to remove them from office. The earlier TRAI members could only be sacked after a successful reference to the Chief Justice of India. Almost all newly appointed full-time members were former government bureaucrats with little demonstrated expertise in the sector.

3.2 Energy

3.2.1 Coal

Coal contributes nearly 50% of the total indigenous primary energy supply in India. The sector has been dominated by public sector enterprises (PSEs), though private sector is gradually being allowed to make in-roads in various segments.

In year 1973 the Coal Mines (Nationalisation) Act was introduced and facilitated nationalisation of the sector. Since than the sector has been dominated by public sector enterprises. In year 1976, the legislation was amended to allow captive mining by private sector. Since 1996, gradual de-regulation of pricing has also been initiated.

The Colliery Control Order 2000 paved the way for full deregulation of coal pricing in India, leaving no power with the Central Government in this regard. Although pricing freedom has been given to the coal producing companies, the distribution of coal is still managed or mediated by government agencies, and only government-owned coal companies are allowed to sell coal directly to consumers.

Allowing private investors, only in mining, without allowing them to sell directly to consumers, is least likely to attract private miners, as they virtually face single buyer, i.e. Coal India, who would then, in turn, allocate to consumers. The Government attempted to introduce the private sector in non-captive mining, which could have introduced competition in the sector. The Coal Mines (Nationalisation) Amendment Bill 2000 aimed at amending the provisions of the relevant Act and permit private sector in non-captive mining is still pending in Parliament. However, coal being a labour intensive industry, doing that would need strong political commitment and would involve taking trade unions on board.

3.2.2 Oil and Gas

Oil and Gas is other important sector that meets nearly 45 percent of India's overall energy requirements. The sector is being governed by the Petroleum Act 1934 and the Oilfields (Regulation and Development) Act, 1948 and the ministry concerned has framed several sets of rules and regulations over the years.

The upstream activities (i.e. exploration, and production of oil & gas) are regulated by Directorate General of Hydrocarbons (DGH). In 1999, the government announced the New Exploration Licensing Policy (NELP), which allows exploration of new oil fields. Private sector companies including foreign companies are allowed to bid for exploration and exploitation of oil and gas fields.

However, private investors still have some concerns related to protection offered to refineries, rights to market petroleum products, and the need for a level playing field with public sector enterprises. As an attempt to address these concerns the government had proposed a framework for independent regulation of the down-stream of petroleum and natural gas sector. Accordingly, the Petroleum Regulatory Board Bill has been drafted and in under consideration of the Indian Parliament. The bill seeks to set up an agency to regulate the down stream sector in oil & gas. Meanwhile, the government plans to install a pipeline grid across the country; access to which would be regulated by the proposed regulatory agency.

As far as retail and marketing segments are concerned, in year 1993 private companies were allowed to and they are gradually making their presence felt.

3.2.3 Electricity

The electricity sector in India is in the Concurrent List of the Constitution hence the union and the provincial governments are both responsible for its development. The Electricity Act 1910, providing for granting of licenses to local governments was in force until it got replaced by the Electricity Act 2003. The Electricity (Supply) Act 1948 was enacted to facilitate regional coordination in the development of electricity sector in India and the Central Electricity Authority (CEA) was created.

By late fifties all state governments had established State Electricity Boards (SEBs), as public sector enterprises responsible for generation, transmission and distribution of electricity. In 1976, the union government also started setting up power generation plants.

Over the years, the gap between demand and supply went up and the government was unable to put investment of the order required. This led to a major shift in the policy in year 1991 when the government opened up the sector for private investment including for foreign investment. 100 percent foreign investment is now allowed in electricity generation. However, this could not yield favorable result as proper market structure was not in place and private generators were compelled to supply only to the SEBs, who's credibility to pay was under suspicion. Later, the transmission segment was also opened up for private players in year 1998. However, again poor financial condition of SEBs (at the distribution stage) could not spur any substantial activity in this segment as well.

Introduction of the Electricity Act 2003 has provided a framework for private investment in almost all segments of the industry. The Act mandates the states to un-bundle the SEBs and set up SERCs in a time bound manner. By now two of the states i.e. Orissa and the national capital New Delhi have privatised electricity distribution and the outcomes are not encouraging. Orissa was the first state to set up an independent regulatory commission in 1995. However, the outcome of restructuring has been far from satisfactory and tariffs have been raised manifold without commensurate improvement in services.

Several of the other states in India have followed a similar approach towards restructure their power sector. The Electricity Regulatory Commission Act 1998 enabled creation of Electricity Regulatory Commissions (ERCs) at the centre and in some of the states. The Central Electricity Regulatory Commission (CERC) regulates tariffs for central power generating units, inter-state transmission tariffs, and issues licenses to private investors for inter-state transmission. The State Electricity Regulatory Commissions (SERCs) determine tariffs to be charged to customers and regulate other activities relating to intra-state transmission and distribution.

The present situation is that, the role of the Ministry is confined to formulate macro policies. Formulation of micro policies and implementation is left for the regulatory agencies. ERCs are considered to be provided with sufficient functional autonomy. However, credibility of the institution is being questioned for the reason that performance of most utilities has not improved significantly. Private investment in generation, though has picked up, however is below expectations. 'Open-access' to transmission and distribution infrastructure is being implemented. However, a very high level of Transmission and Commercial (T&C) losses continues to impede performance of distribution companies which is the most crucial component in the entire value chain.

Presently, the per capita consumption of electricity is 606 KWH/year in India. 44 percent of the households have been electrified though the quality and availability of electricity is not satisfactory by and large. The government of India has set a target to provide electricity to every household by year 2012. This would be difficult to meet without substantial investments from the private sector, which calls for a proper regulatory regime.

Box 5.2 Dabhol Power Company Case - Failure of Governance?

In 1992, India opened up its power sector for foreign i nvestment. Enron Inc along with other promoters signed an MoU with the provincial government of Maharashtra to set up a thermal generation plant of a capacity of 2000 -2400 MW. The project facilitated biggest ever inflow of foreign direct investment to India.

The Power Purchase Agreement (PPA) was signed between Dabhol Power Company (DPC), Indian subsidiary of the Enron Corporation, and Maharashtra State Electricity Board (MSEB). Notably, the

investor virtually passed on every possible business risk to the MSEB. MSEB was obliged to buy power for 24 hours a day at inflated price and fluctuations in the dollar-rupee exchange rate was provided to factor into the cost.

This evoked resentment among public and became a major political issue during the then elections. The government that was sworn in, scrapped the contract. The PPA was re-negotiated and the rate at which power was to supply to MSEB was brought down. The Federal government on its part extended a counter-guarantee to cover any defaults by the state utility to the DPC.

The cost of power was still considered high. In year 2001, MSEB defaulted on its payment to DPC which led to Enron issuing a notice of arbitration to the Indian government to pay the bill. Enron invoked political *force majeure* clause in its contract with MSEB.

The project suffered heavily. An array of suits were filed from both sides and several committees were set up to resolve the matter amicably which did not succeed. Re-negotiating PPA also did not help and the project was put to a stand still. Despite all efforts of the state and the central governments the matter could not resolved and assets worth billions of rupees remain idle till date.

The entire episode contributed to raising the risk perception about India and adversely affected FDI flow. The case highlights the need of a predictable and consistent regulatory regime to have sustained inflow of private investment, absence of which cannot be compensated by out-of-proportion incentives.

3.3 Transportation

3.3.1 Highways

The sector comes under the supervision of the Ministry of Shipping, Road Transport & Highways. In 1988, the National Highway Authority of India (NHAI) was constituted by an Act of Parliament and made responsible for the development, maintenance and management of National Highways. However the NHAI could become functional only in 1995 due to delay caused by bureaucracy. NHAI works under the ministry and has been instrumental in facilitating private investment in construction and management of highways in India.

The NHAI is responsible for implementing the National Highway Development Programme (NHDP) a massive programme government has initiated to develop highways in the country. Several of contracts under this programme have been awarded to private companies.

Recently, the Control of National Highways (Land & Traffic) Act, 2005 came into force empowering Highway Administrations to pass orders to regulate access to National Highways. The government has already notified constitution of 192 numbers of Highway Administrations in different parts of the country. The law provides for a party aggrieved by the orders of the Highway Administrations to approach the National Highway Tribunals for redressal. The initiative has been taken recently hence its evolution is yet to be observed.

3.3.2 Aviation

Aviation oversight functions are currently distributed between the Ministry of Civil Aviation (MoCA), Airports Authority of India (AAI), Directorate General of Civil Aviation (DGCA) and the Bureau of Civil Aviation Security (BCAS).

Ministry of Civil Aviation is the nodal Ministry responsible for the formulation of national policies and programmes for development and regulation of Civil Aviation and for devising and implementing schemes for the orderly growth and expansion of civil air transport. Its functions also extend to overseeing airport facilities, air traffic services and carriage of passengers and goods by air. The Ministry also administers implementation of the Aircraft Act, 1934. DGCA

and BCAS are subordinate organisations to the Ministry, responsible for aviation safety and security respectively. Airports Authority of India (AAI) is a public sector undertaking coming under the administrative purview of the Ministry.

So far, economic regulation of the aviation sector has been, at best, an informal exercise, with the AAI combining the functions of operator and regulator of airports and air traffic control services. These multiple roles obviously create serious conflicts of interest.

As far as market scenario is concerned, public sector airlines i.e. Air India and Indian Air Lines (renamed as Indian) remain big players. However, their market share in domestic services is gradually coming down. The repeal of the Air Corporations Act 1953 in the year 1994 enabled private operators to provide scheduled air transport services. With the entry of private operators, competition has increased. There has been an improvement in the quality of services and sharp reduction in airfares.

However, the entry of new airlines and expansion in their services has put a strain on existing airport facilities. Considering this, the government has got on the path to restructure and modernize airports. Recently the government invited private sector to invest into modernizing the Delhi and Mumbai airports, the two busiest airports in India. The bidding process, however, ran into problems before being finally cleared and seems to be on course now.

3.3.3 Ports

In India the major ports are placed under the Federal List of the Constitution and are administered under the MPTA (Major Port Trusts Act) 1963 by the government of India. The other ports (minor ports) are placed in the Concurrent List and are administered by the states under the India Ports Act, 1908.

Under the MPTA a port trust organisation is established to manage and operate country's major ports and the central government appoints the board of trustees to each of them. At the state level, the department in charge of ports or the State Maritime Board (SMB) - a legislative body – is responsible for regulating and overseeing the management of state ports.

India has 12 major ports and 185 minor ports. The major ports handle around 75 percent of the over all seaborne trade. During nineties, general cargo volume witnessed significant increase which was a reflection of adoption of trade liberalisation policy by the government of India.

The port system was not rational in India as the major ports were handling more cargo volumes than their capacity. This resulted in pre-berthing delays and longer ship turnaround time. As compared to world standards Indian ports continue to show lower productivity in terms of labour and equipment. With the view to address the referred issues, in year 1996 the government of India released guidelines to facilitate private sector participation in ports sector. A number of existing facilities have been taken over by private players and many new facilities have also been set up at existing ports. As a result, container terminals at Jawaharlal Nehru, Chennai, Tuticorin and Visakhapatnam Ports are managed by private operators. Two new ports (Mundra and Pipavav in Gujarat) have also been constructed in the private sector.

With privatisation, the role of Indian ports is changing from a service port model to a landlord port model, where the port authority retains the port infrastructure and regulatory functions, whereas private operators provide the port services. Ennore Port is one such example.

The MPTA 1963 and the IPA 1908 were amended in 1997 to create the Tariff Authority for Major Ports (TAMP), to regulate tariffs, both vessel related and cargo related, and rates for lease of properties in respect of Major Port Trusts and the private operators located therein. However it has no jurisdiction over the minor/private ports.

3.4 Financial Services

3.4.1 Banking

The Reserve Bank of India is the central bank of the country set up by the colonial government. The Reserve Bank of India (RBI) Act 1934 provides the statutory basis of the functioning of the Bank, which commenced operations on April 1, 1935.

RBI was constituted to regulate issuance of bank notes, maintain reserves with a view to securing monetary stability and operate the credit and currency system of the country. The RBI began its operations by taking over the functions of the Controller of Currency and the Imperial Bank of India. The Bank, which was originally set up as a shareholder's bank, was nationalised in 1949.

With liberalisation, RBI's focus has shifted to core central banking functions such as Monetary Policy; Bank Supervision and Regulation; and Overseeing the Payments System and developing the financial markets. The Reserve Bank's affairs are governed by a central Board of Directors which is appointed by the government of India.

The Reserve Bank is vested with regulatory and supervisory authority over commercial banks and urban cooperative banks (UCBs), development finance institutions (DFIs) and non-banking financial companies (NBFCs). As a regulator of the banking systems in India RBI is responsible to prescribe broad parameters of banking operations within which the country's banking and financial system functions.

3.4.2 Capital Market

In year 1988 government of India set up the Securities and Exchange Board of India (SEBI) with the objective to regulate the security markets in India, which was evolving at that time. SEBI was initially set up through an executive resolution and was upgraded subsequently as an autonomous body in the year 1992, through the Securities and Exchange Board of India Act (SEBI Act). Paradoxically, conferring a legislative status to SEBI was an outcome of a massive securities scam that took place in 1990-91.

SEBI is an autonomous statutory body responsible to cover both development & regulation of the securities market in India. In 1999, an amendment was made to the Securities Contracts (Regulation) Act, 1956 to allow SEBI to regulate trading in derivatives. SEBI is required to abide by the directions given to it by the government on questions of policy.

In year 2002, an ordinance was promulgated empowering SEBI with powers to investigate, bringing in larger penalties and better defined concepts such as insider trading and market manipulation.

3.4.3 Insurance

Insurance is a federal subject in India. The first of the insurance companies was started in India in 1818 and a number of foreign and Indian insurers operated till the nationalisation of the industry took place on the ground of adoption of unethical practices by some of the players. The Insurance Act 1938 and the Insurance Regulation & Development Agency Act 1999 presently governs the sector.

Nationalisation in the decade of seventies lent the industry solidity, growth and reach. However, state owned corporations were having monopoly in life as well as general insurance. In line with the general liberalised economic policy environment, and with a view to induce competition and provide a choice to the consumers, entry for private sector was allowed and Insurance Regulatory & Development Agency (IRDA) was constituted in year 2000 by enacting the IRDA Act, 1999. The IRDA Act facilitated entry of private players in the insurance market. The Indian insurance regulator follows the general pattern of keeping the life insurance and general insurance companies separate.

IRDA has so far granted registration to 12 private life insurance companies and 9 general insurance companies. Nevertheless, public sector corporations still dominate the market though private players have started making their presence felt.

In brief…

Regulatory agencies in various sectors in India are created by separate pieces of legislation. Significantly, creation of regulatory bodes in most sectors was in response to prevailing dynamics in the sector rather being a part of overall strategy to liberalise. With the exception of insurance and banking, the dominant approach is of establishing a regulatory body after allowing entry to private sector. This is true for the proposed Petroleum regulator, as well as the civil aviation regulator, which is being talked about.

The basic premise to set up regulatory agencies is to achieve following objectives:

(i) Separate policy formulation function from that of regulation to provide consistent regulatory environment through achieving insulation from politics
(ii) Stimulate investment through offering a level playing field to private operators with state-owned incumbents
(iii) Provide measures for accountability

The attainment of these objectives would depend upon the actual working of the regulatory regime, an issue to which we turn next. We make an assessment of the working of regulatory system in India on the basis of certain parameters (regulatory autonomy, accountability, interface with government, etc.).

4. Evaluation of Sectoral Regulatory Framework

Box 5.3 Indian Prime Minister on Need for an Enabling Regulatory Structure

In 2004, the Prime Minister of India, Dr. Manmohan Singh expressed that his government is working towards developing a proper regulatory framework in infrastructure sector.

He assured that the government would ensure a regulator y framework that is transparent, independent, provides impartial balance between public and private sectors and is based on international best practices.

The Prime Minister had asked the Planning Commission to prepare a policy paper indicating the regulatory structures for different areas such as power, roads and ports. The paper will look into the gaps in the existing system, comparing them with international best practice and recommend changes in the existing policies, if necessary. (The paper is still u nder preparation)

4.1 Regulatory Institutional Framework

Following is a review of institutional and organizational features of the regulatory framework of various sectors in India.

Table 5.1 Regulatory Institutional Framework in India

Sector	Enabling Legislation	Regulatory Body	Appellate Body	Other Agency and its role	
Telecommunications	Telecom Regulatory Authority India1997 (Amended 2000)	Telecom Regulatory Authority of India (TRAI)	Telecom Dispute Settlement and Appellate Tribunal (TDSAT)	Department of Telecommunications	Policy formulation, licensing, administrative monitoring of PSUs,
				Wireless Planning Commission (within DoT)	Advise DoT on spectrum allocation and management
Electricity	Electricity Act 2003	Central/State Electricity Regulator Commissions (ERCs)	Appellate Tribunal for Electricity	Central Electricity Agency (CEA)	Macro planning along with Ministry
Oil & Gas	The Petroleum and Natural Gas Regulatory Board Bill, 2005*	Petroleum and Natural Gas Regulatory Board (PNGRB)	Appellate Tribunal for Electricity	Directorate General of Hydrocarbons	Regulate upstream sector (exploration and production)
Highways	National Highway Authority of India Act 1988	Ministry of Shipping, Road Transport and Highways		National Highways Authority of India (NHAI)	Facilitate highways construction and development
Civil Aviation	Air Craft Act 1934, Airport Authority of India Act 1994	Ministry of Civil Aviation		Airports Authority of India (AAI)	Regulation, operation and management of airports and providing air traffic services
				Directorate General of Civil Aviation	Maritime Administration, Education and Training, development of Shipping Industry
Seaports	Indian Ports Act 1908; Major Port Trusts Act 1963	Tariff Authority for Major Ports (TAMP)	Judiciary	Directorate General of Shipping	
Banking	Reserve Bank of India Act 1934	Reserve Bank of India (RBI)			
Capital Market	Securities and Exchange Board	Securities and Exchange	Securities Appellate		

Sector	Enabling Legislation	Regulatory Body	Appellate Body	Other Agency and its role	
	of India 1992	Board of India (SEBI)	Tribunal		
Insurance	Insurance Act 1938, Insurance Regulation and Development Act 1999	Insurance Regulatory and Development Authority (IRDA)	-		

* the bill has been tabled in the Parliament and is under consideration

Broadly three approaches are being followed in India:

- One, where independent regulatory bodies have been set outside of the line ministry (e.g. in telecom, electricity, seaports, banking, insurance, capital market, and as proposed in oil & gas).
- Second, where regulatory function is performed by the line ministry concerned, and specialized agencies within the ministry have been constituted to perform these tasks (e.g. civil aviation, highways)
- Third, where the line ministry is performing multiple tasks that of policy maker, service provider and regulator (e.g. in Railways).

Highways, water supplies, railways are the sectors that continue to be regulated by related government departments. The state government of national capital Delhi is in the process of setting up regulatory agency for water supplies. Petroleum & Gas sector is likely to see an independent regulatory body soon and discussions are on to set up another regulator for aviation industry.

Electricity being the joint responsibility of both the federal and provincial governments, separate regulatory bodies have been set up at the centre as well as the states.

Except for seaports, insurance and banking, appellate tribunal has been set up with all other regulatory agencies that perform quasi-judicial functions (i.e. TRAI, ERCs, TAMP, and SEBI). In case of seaports, appeals can be made to the judiciary. In the case of insurance, discussions are on to either set up an insurance appellate body or entrust the responsibility to the already existing securities appellate tribunal. The latter is an emerging trend in India. For instance, the proposed Petroleum and Natural Gas Regulatory Board Bill provides that the appellate tribunal established under the Electricity Act, 2003, would be the appellate tribunal to hear appeals against order or decision of the proposed Regulatory Board. This is a welcome development and would serve to limit the mushrooming of appellate bodies in India, and at the same time ensure coherence in the application of regulatory laws.

4.2 Management Structure and Selection Mechanism

Selection and appointment of regulator is one of the potential sources to influence regulatory activism and outcomes, indirectly. In India, there is lack of transparency in the selection and appointment of regulators, and line ministries have a great say. For instance, in telecom, regulators are selected by the Government of India (represented by the Ministry of Communications), without issuing any public notice thereof. In electricity sector a selection committee (constituted separately at the central level as well as state levels) identifies appropriate candidates and recommends the case to the government.

In practice, regulatory agencies are used as parking ground for retired bureaucrats from the government. For instance the Central Electricity regulatory Commission remained head-less for nearly one and half year as a suitable candidate could not be identified until the then secretary in the Ministry of Power got retired and appointed as the next chairperson. What's more, the TRAI Act specifically mentions of acting bureaucrats being eligible for appointment as regulator which has not been provided in other laws.

Several regulatory legislations such as that of telecom provides for appointment of a person who is representative/expert on consumer issues as regulator however this has not been exercised so far. In general, the upper age limit for serving, as a regulator is 65 years. There are of course, variations in some sectors, such as the age limit for insurance regulator is 62 years. Usual term for appointment is five years with an exception in telecom sector where it is three years.

The regulatory legislations in telecom, capital market, and insurance provide for appointment of part-time members in regulatory agencies. Provisions with respect to reappointment are not uniform. For instance, regulators in electricity sector are not eligible for reappointment.

Further, there are variations in the minimum 'cooling period' between retiring from regulatory position and joining the same industry. Thus, whereas regulators in telecom face a restriction of one year, the Electricity regulators face a restriction of two years before accepting any commercial employment after ceasing to hold office.

The related line ministries determine salaries and allowances for regulators, which is usually comparable with those of upper-middle level bureaucrats.

Provisions related to removal of regulators also vary across sectors. In electricity sector, a regulator cannot be removed unless proven guilty in a judicial probe. In banking, government retains the power to suspend the Board of the Reserve Bank of India in certain circumstances. In such an event, government has to cause a full report of the circumstances leading to such action and lay it before the Indian parliament. However, in telecom, regulators enjoy no legal protection, beyond a right of being heard, if the government wishes to remove them. Some board members of SEBI can be removed with a prior notice of 3 months.

4.3 Financial Resources

Lack of financial autonomy may substantially curtail functional autonomy of a regulatory agency. Capacity of a regulatory agency to attract best available talent is determined by the availability of funds and authority to use the same.

Table 5.2 Funding Arrangements for Regulatory Agencies in India

Regulatory Agency	Mode of Financing	Approving Agency
Telecom Regulatory Authority of India (TRAI)	Grants from the government (Though law provides for regulator to raise funds through imposing levy etc)	Line Ministry
Electricity Regulatory Commissions (ERCs)	Grants from government (Though law provides for regulator to raise funds through imposing levy etc)	Line Ministry
Tariff Authority for Major Ports (TAMP)	Grants from the government	Line Ministry
Reserve Bank of India (RBI)	Return on invest ments it had made, interests etc	Self approval
Securities and Exchange	SEBI Fund comprising of grants, fee,	Self approval

Regulatory Agency	Mode of Financing	Approving Agency
Board of India (SEBI)	charges received, and sums received from other sources	
Insurance Regulatory and Development Agency (IRDA)	IRDA Fund comprising of grants, fee, charges etc	Grant amount determined at the discretion of government

The provisions made in Indian sectoral regulatory laws to finance regulatory bodies are not consistent across the sectors. More over, some of the provisions of the law are not being implemented. For instance, the enabling legislation in telecom and electricity provide for the setting up of separate funds in which grants received from the Government and other receipts in the form of fees and charges, etc. are to be credited. However, these provisions have not been implemented as yet. Instead, regulators are made to rely on line ministries for budget, which is often not enough to meet the increased requirements of the regulator.

TRAI, for instance, has been complaining of limited resources at its disposal that severely curtail it's functioning. Accordingly, the telecom regulator sought government's permission to allow it to share a part of the license fees, as its independent source of funding. However, the Ministry of Finance shot down the proposal. Interestingly, regulatory agencies in the financial sector are allowed to raise revenues through fees, charges, etc. as available to the insurance regulator (IRDA) and capital markets regulator (SEBI)

Be that as it may, raising revenue is just a part of the story. More important is to be allowed the freedom to spend it. Unfortunately, this does not seem to be the case with the insurance regulator which is currently having a dispute with the Ministry of Finance (see Box 5.4).

Box 5.4 Insurance Regulator: Struggling for power to retain funds

In February 2002, the Ministry of Finance decided to place the receipts of the IRDA in the Public Account. The decision was taken in the background of similar practice being followed by constitutional/statutory authorities, which are autonomous in their functioning, and also keeping in view the fact that the receipts of IRDA were likely to rise to substantial levels. It was also stipulated that IRDA could withdraw a specified amount once every year from Public Account with the approval of Financial Adviser (Finance) and Secretary (Expenditure) and keep it in their bank account for meeting their annual expenditure. The intention behind seeking this approval was to put a cap on its expenditure.

IRDA, however suggested that legal opinion should be sought on the operation of its fund. Despite being informed by the Ministry of Finance that the Department of Legal Affairs had also opined that IRDA receipts had to be credited to the Public Account of India, IRDA continues to retain the receipts in contravention of Ministry's orders.

In December 2003, IRDA again took up the matter with the Government to allow it to continue retaining the IRDA fund except the penalties/fines levied by them which could be credited to the Consolidated Fund of India. The Ministry however stated that the Government had not agreed with the position taken by IRDA. The matter is still unresolved.

The struggle of telecom regulator and insurance regulator shows the general apathy towards awarding financial autonomy to regulatory agencies in India. The curbs placed on their financial resources is primarily to put a check and cap on their expenditures.

4.4 Staffing and Training

Table 5.3 Staffing and Training in Regulatory Agencies in India

Regulatory Agency	Number of staff	Training	Power to appoint staff
Telecom Regulatory Authority of India (TRAI)	120	Staff is occasionally sent for training	Regulator
Central Electricity Regulatory Commission (CERC)	47	Members and top-level staff get training exposures, occasionally	Regulator with approval of line ministry
Tariff Authority for Major Ports (TAMP)			Regulator
Reserve Bank of India (RBI)	22,500	RBI has got its own infrastructure to train its staff	Regulator
Securities and Exchange Board of India (SEBI)	467	Staff exposed to training. Plan to set up its own institute for training	Regulator
Insurance Regulatory and Development Authority (IRDA)	48	Staff is exposed to training	Regulator

Regulatory agencies in telecom, electricity, ports, securities, banking, insurance sectors are empowered to appoint their staff. However, in general, salaries and other terms and conditions of service of regulator's staff are prescribed by the government of India. For instance, in electricity sector line ministry not only approves the number and nature of the regulator's staff but also their emoluments. In contrast, RBI and SEBI are empowered to take decisions on these matters, independent of the government. But still, their compensation package is not market-related (see Box 5.5).

Box 5.5 Poor Salaries Harming India's Central Bank

The 600-odd executives (of the rank of deputy general manager and above) who run the show at the RBI do not get either market-related remuneration or performance-linked pay. This is at a time when even the PSU banks regulated by the RBI have found ways to provide incentives to their employees.

Unlike some of the central banks across the globe, salary of RBI-tes is not market related. What is worse, the RBI employees' pay packets are even less than those of government employees -- this was not so earlier, but following the implementation of the Fourth and Fifth Pay Commissions' recommendations, this has happened.

Apart from the poor compensation package, the RBI's pace of promotion is also quite slow -- it doesn't help that there are very few vacancies at the top. For instance, there can only be 23 regional directors and another 23 department heads (all of chief general manager rank).

In most cases, staff in regulatory bodies are on deputation from various government departments. Some regulators, such as the TRAI appoint experts as consultants to assist them in their work.

Staff of regulatory authorities are exposed to training. For instance, members and senior staff of electricity regulators have attended a few training programme overseas. Most of these programmes were embedded in the assistance package which donors such as the World Bank,

USAID, Asian Development Bank extended to some of the state governments in India to reform the sector.

4.5 Regulatory Mandate and Enforcement

Telecom

The mandate of TRAI can be divided in two broad categories:

- To advise the government and submit its recommendations on issues including issuance and revocation of licenses, promote competition, measures to develop telecom sector in India, spectrum management. On these issues, TRAI can submit its views to the government either *suo moto* or on a request made by the government. The recommendations are not of binding in nature hence entirely subject to government's discretion.

- The other role that TRAI is mandated for is to regulate the Indian telecom industry in certain aspects including ensuring compliance of terms for licenses, inter-connection related matters, tariffs, prescribe standards for quality of service and measure compliance, ensure compliance of universal service obligations.

With respect to tariffs TRAI follows light-handed approach. The only tariff order that TRAI had issued was in year 1999. Thereafter market has become far more competitive hence tariffs have gone down. The major role that TRAI plays now is to keep a watch on various offers in the market and see that competition is not being debarred.

TRAI is considered to be not so successful in regulating the public-sector incumbent service providers. For instance, BSNL has successfully resisted sharing its infrastructure, acquired since the days of it's being a public owned monopoly, even though regulations demand it. The fact that in several regulatory matters TRAI can only submit its recommendations to the Department of Telecommunications (DoT) to which the public-sector service providers reports, explains the practical difficulties. Further, temptation to command and control these autonomous institutions still prevails within line-ministries, often leading to turf wars.

To cite an instance, the Department of Telecom (DoT) in 2006 announced certain proposals for restructuring the tariff regime in telecommunications, considering these as policy issues. However, TRAI resisted these proposals. After TRAI's objection, the DoT contemplated exercising its powers under the Act to issue 'policy directives' to the regulator. Although the Ministry finally refrained from doing so this event highlights the need to clearly demarcate policy and regulatory issues.

In yet another instance, the ministry of communications recently announced its intentions to implement a one-India call rate abolishing the prevailing differential tariff regime where charges are based on distance to which a call is made. Though a good move, keeping in view the technological developments, however, the telecom regulator, which has a jurisdiction over tariff related matters, was once again kept out. The example explains how line ministry encroaches upon the jurisdiction of regulatory bodies.

The TRAI Act provides that the regulator is not entitled to handle disputes between stakeholders, rather have to be referred to the Telecom Dispute Settlement Appellate Tribunal (TDSAT). This provision has tied the hands of the regulator in several matters, as almost any issue can be presented as a 'dispute' between interested parties. This is one of the reasons for

TRAI not being able to ensure effective interconnection among various service providers (see Box 5.6).

Box 5.6 Interconnection in Telecom, particularly with SOE's network unresolved

In recent times there has been an exponential growth in cellular mobile services. However, the provision of interconnection has not kept pace with this growth le ading to increase in inter -network congestion and poor quality of service to the customers. A recent study paper by TRAI highlights that the problem is escalating and unless immediate remedial measures are taken, the situation will only worsen.

In order to ensure efficient interconnection between service providers, TRAI issued Interconnection (Reference Interconnection Offer) Regulation, 2002. BSNL challenged this Regulation before TDSAT which ruled that the power of TRAI to fix the terms and conditions of interconnection are subject to licence conditions and the existing interconnection agreements between operators.

Ideally, the regulator should have had full authority to get on with the task of getting all networks to hook up with one another in a timel y and transparent manner. However, with the TDSAT clipping TRAI's wings and leaving interconnection to mutual negotiation between operators, the regulator has been left with no teeth to enforce its directives. TRAI has appealed against this ruling at the S upreme Court, and the matter is subjudice.

The problem of interconnectivity is extremely acute with BSNL, whether it is interconnection to their fixed network or the mobile network. The Interconnect Agreements between BSNL and other mobile service provide rs provides for provision of interconnect capacity within 12 months of making the payment for the required capacity. However, there are large number of cases pending where even after 12 months, the required junctions have not been provided by the BSNL.

If interconnection issues are left for mutual negotiations, the incumbent operator and operators with significant market power always try to delay interconnection to other players leading to inconvenience and high cost to subscribers and deterioration of net work conditions. This is evident from the delay in providing interconnections by BSNL and recent dispute on interconnection between Reliance Infocom Ltd. and Tata Teleservices Ltd. where Reliance delayed provision of interconnection to Tata Teleservices Ltd.

In 2005, TRAI facilitated getting the service providers agree on adoption of a consumer charter on voluntary basis and comply with the same within next six months. However, most service providers have still not complied with the charter though it is almost one year. In the absence of penal powers, TRAI finds itself helpless to ensure proper quality of services. Instead, its reaction is confined to issuing periodic quality of service (QoS) reports to monitor compliance with QoS standards framed by the regulator. Recently, the regulator has taken up with the government, the issue of granting it penal powers for non-compliance of QoS standards, and the matter is still to be decided.

Electricity

In India, as per the constitution, both the central and provincial governments are responsible for electricity sector. The regulatory commissions at the centre and in provinces have specific responsibilities of which many are similar.

The regulators are responsible to issue licenses for transmission, trading, and distribution of electricity; regulate tariffs of generation, transmission, and distribution utilities; set up performance benchmarks; monitor compliance of quality of standards; adjudicate disputes; enforce licensing conditions; set up mechanisms to redress grievances; promote and ensure competition. Whereas, provincial regulators are responsible for all these matters in respective provinces, the Central Commission, is responsible in the context of inter-province transactions.

Further, the regulatory commissions are responsible to advice respective governments and provide them with relevant information on specified matters including formulation of policies; promotion of competition and efficiency; promotion of investment etc.

The government owned utilities have been corporatised in most provinces, and in case of two provinces, the distribution segment has been privatised. However, the experiences with privatisation and restructuring have not been encouraging. High level of operational losses is a major problem in almost all provinces and despite consistent regulatory interventions not much has been achieved. The burden of such inefficiency is being passed on to honest consumers.

The Electricity Act 2003 entrusts the regulators to phase-out the cross-subsidy regime and let the government bear the burden of subsidised supplies to certain categories of consumers, should it wish to continue with the arrangement. Nevertheless, electricity continues to be supplied to domestic and agriculture consumers at a price that is below the cost, for social and political reasons (see Box 5.7). The loss accrued on this account is partly compensated through charging a premium to industrial and commercial consumers, and through subsidies provided by respective governments.

Among the key challenges faced by the electricity sector are: bankrupt distribution utilities, rationalising of tariffs for domestic and agriculture consumers, achieving reduction in operational losses, and improving reliability and quality of supplies.

Box 5.7 Policy Directives to Supply Electricity at Free of Cost

The provincial government of Tamil Nadu in India, issued a policy directive to the Tamil Nadu Electricity Regulatory Commission (TNERC) in year 2004.

Through a letter written to chairperson o f the TNERC government directed the TNERC to allow electricity distribution utility, which was a state -owned enterprise, to supply to domestic consumers at reduced tariffs and extension of free supply of electricity to agriculture and Hut consumers. The mo ve was in exercise of the Section 108 (1) of the Electricity Act 2003 which provides for the government to issue 'policy directives' to the regulator.

The government also announced to compensate the utility for the shortfall in revenue that would occur on implementation of the policy directives, which is mandatory as per the law.

The incident demonstrates relevance and effectiveness of independent institutions, despite the government being sole owner of the distribution utility it had to protect commerc ial interests of the utility.

Considering the poor performance of regulatory regime in the electricity sector, the government is reportedly mulling a plan to remove all electricity regulators at the Centre and in certain provinces (ruled by political allies of Federal government). This forms part of a plan to institute a new regime.

However, the poor regulatory environment in power sector is not due to the inefficient functioning of power regulators, but primarily because of government's continuous interference in their functioning. How can more investment come in power plants in a situation where the principal buyers, the state electricity boards, are bankrupt? The Electricity Act 2003 sought to introduce 'open access'. However, despite the legislation, the situation on the ground hasn't changed, as the state governments are delaying the process.

The plan to replace the regulators would have an adverse impact on the regulatory process in India and set an unhealthy precedent.

Seaports

Determining tariffs for major ports is the sole mandate given to the Tariff Authority for Major Ports (TAMP). The Authority is empowered to notify rates and conditionalities governing application of the rates. Although terminal handling charges by private operators may constitute a significant proportion of the total cost of moving cargo through the ports, there is no explicit provision in law, empowering TAMP to regulate tariffs for terminal handling charges by private operators.

Till very recently, TAMP used to set floor prices below which the ports were not allowed to compete. Now, the government has asked TAMP to fix tariff ceilings instead. In any case, under the 1997 amendment, government has retained the power to order remissions from and even alter the rates approved by TAMP.

TAMP has no power to summon data, records etc, to prescribe time frame for compliance of its orders/directions, and monitor compliance of such orders/directions. It has no power to levy fines and charges for non-compliance or violation of its orders/ directions. The orders issued by TAMP are not final, and can be changed by the government.

Banking

The mandate given to RBI is that of 'monetary stability of India' which is very comprehensive. Functions that RBI performs are diverse ranging from formulation of credit and monetary policies, issuance of bank notes, to regulating the banking sector. Non-banking finance companies too fall within its regulatory preview. RBI has no mandate over stock market yet being the largest issuer of bonds it is empowered to supervise the bond market in India.

The enforcement powers given to the RBI to regulate the banking sector are considered fairly comprehensive. While deciding on monetary and credit policies RBI consult with the ministry concerned in the government though the law does not mandate such consultations.

Be that as it may, time and again, conflicts have arisen between the government (represented by the Ministry of Finance) and the RBI. For instance, in its quarterly review of monetary policy announced in January 2006, the RBI hiked interest rates much to the displeasure of the Finance Minister, who hoped that the move would soon be withdrawn. Differences between the RBI and Ministry over economic policies have continued since its establishment, with interest rate policy identified as an area of potential conflict. Finance Minister's have often interfered, which highlights the fact that overall macroeconomic policy continues to be dominated by the fisc, and the recent action by the RBI seems to challenge this notion.

Caught in the crossfire between the ministry and the RBI are public sector banks who constitute a third of the banking industry. They have no choice but to hike their deposit rates to be in sync with the market and at the same time, they are not in a position to hike their lending rates, as that would displease the ministry. So, their net interest rate margin is under pressure and profitability is being hit.

Capital Market

SEBI was constituted to protect the interests of investors in securities and promote development of and regulate the securities market in India. The SEBI Act governs all Stock Exchanges and

the Securities Transactions in India. The legislation empowers SEBI to register and regulate working of stock brokers, sub-brokers, share transfer agents, bankers to an issue, trustees of trust deeds, registrars to an issue, merchant bankers, underwriters, portfolio managers, investment advisers, etc.

The responsibilities of SEBI also includes to register and regulate the working of collective investment schemes including mutual funds, to prohibit fraudulent and unfair trade practices and insider trading, to regulate takeovers, to conduct enquiries and audits of the stock exchanges, etc. For non-compliance of its directives SEBI can impose penalties. The magnitude of such penalties is prescribed in proportion of severity of offence. Repeated violation attracts heavy penalties.

SEBI has the powers of civil court for the purpose of summoning; asking for production and investigating documents and so on. It can appoint an investigating agency if required and can cease or desist any person for committing or causing violations of rules. Decisions given by SEBI can be contested before the Securities Appellate Tribunal (SAB).

Box 5.8 Capital Market Regulator Challenges Government's Decision in Court

During its early days, the Securities Exchange Board of India (SEBI) imposed a huge penalty on the Hindustan Lever Limited (HLL) for the latter's alleged involvement in 'insider trading'. HLL is a subsidiary of the transnational corporation Lever Limited, and one of the largest corporate in India.

HLL contested SEBI's decision and filed a petition before the Ministry of Finance that was the appellate authority at that time. The Ministry revoked th e order issued by the regulator. However, SEBI maintained its stand and decided to protest.

Dissented with the decision of the Ministry, SEBI filed a Public Interest Litigation (PIL) in the Bombay High Court arguing that the decision of the Ministry was not based on merit and likely to affect the interests of millions of small investors. Though the SEBI Act does not provide for filing a PIL, still the judiciary in India usually entertains matters, which have potential to affect public interest.

The step taken by SEBI was unprecedented and no other parallel exists, in which a regulatory agency pulled the government to the Court on the ground of acting against 'public interest'. Nevertheless, the matter is still lying in the Court though several years have passed since the petition was filed.

The case demonstrated the extent to which a regulator can exercise the autonomy given, in letter or sprit. However, the fact that the matter is still lying in court and remains unresolved even after several years does reflect on the pace at which the judicial system works in India.

Insurance

The Insurance Regulatory and Development Agency (IRDA) was constituted with the broad objective of regulating and promoting orderly growth of the industry; and protect interests of insurance policy holders. The mandate of the Agency is inclusive of regulation, promotion and ensuring orderly growth of insurance and re-insurance business in India.

To achieve the stated objectives the Authority can issue licenses; prescribe standards of performance; levy fees and other charges; regulate investments in the sector; adjudicate disputes between insurers and intermediaries or insurance intermediaries; etc. The Authority may suspend or cancel a license of player, if required.

4.6 Interface with Competition Authority

Addressing competition concerns in regulated industries has always been challenging for the reason that possible overlaps between the jurisdictions of sectoral regulator and competition authority exist which may lead to turf war and forum shopping. Lack of clarity in related laws often adds to confusions, and India is a typical example.

On the one hand, we have a very clear statement in the TRAI Act that it will be subject to the rulings of the competition authority and its power to determine entry, mergers or other matters relating to competition are primarily recommendatory. On the other hand, the Electricity Act creates ambiguities as the preamble clearly talks about the objective of promoting competition in the electricity market. The commission (central or state) is empowered to regulate production, supply or consumption to promote competition and is further allowed to regulate distribution to prevent abuse of dominance. Thus in its regulatory functions the law clearly directs the regulator to act in a manner so as to promote competition and efficiency. Further they are also required to advise the government on measures to promote competition. In a similar manner we see that in the financial sector the RBI is authorized on all matters relating to bank licensing, mergers and practices.

On the other end, the nature of the competition authority's power vis-à-vis statutory regulators is ambiguous. The law implicitly recognises that sectoral regulators have a role to play in competition matters and says that statutory regulators may refer competition matters to the competition authority but to what extent the competition authority can influence the regulators in the absence of such requests is not clear. This ambiguity runs the risk of creating either gaps or conflicts in the functioning of the respective agencies.

To add to this ambiguity, the Department of Telecommunications has come out with its own guidelines to regulate intra-circle M&As, despite there being merger regulation provisions in the competition law of the country. These guidelines have so far not created any problems, because presently the competition authority is in a limbo due to a legal imbroglio, however, when the latter becomes active, the DoT guidelines would add to further confusion and turf wars.

4.7 Decision Making Process

Telecom

The Telecom Regulatory Authority of India (TRAI) follows a consultative approach and the process is fairly transparent and participatory. TRAI usually issues a consultation paper to invite comments and publish it widely through multiple mediums. The comments received are debated and discussed in an 'open house' to which all major stakeholders are invited.

In important maters, TRAI is required to submit its recommendations to the line ministry and acceptance of the recommendations is subject to latter's discretion. In practice, consumer groups in India by and large lack in capacity and resources to effectively put forward their concerns.

Electricity

The law provides for ERCs to follow consultative process to decide on substantive issues. Accordingly, comments/objections from stakeholders are invited and debated prior to taking decisions on substantive issues including determination of tariff, setting performance standards. However, in practice, under-representation of consumers remains a concern as they lack in capacity and resources to represent their interests.

Ports
The Tariff Authority for Major Ports (TAMP) invites comments from stakeholders and organises 'hearings' prior to take decisions. The law provides for keeping a copy of every notification, declaration, order and regulation released by the regulator in the office of the conservator and the custom-house for inspection by interested parties.

Banking
The governor of the RBI convenes meeting of the Central Board at least six times in a year and at least once each quarter. Decisions are made through consensus and there are no instances to quote when the Board could not reach consensus. The law empowers the RBI to decide on monetary policy in independent manner, however, widespread perception is that the RBI always consults the government.

Capital Market
SEBI takes decisions based on consensus among members of the Board. In case need arises, the Board decides by majority vote with the Chairman having a second or casting vote. A member having different opinion from that of majority can get his dissent registered on the record, though there is no instance to quote as yet.

Insurance
The Authority decides with majority of votes of members presenting and voting. In the event of an equality of votes the chairperson has a second or casting vote. Stakeholders can submit their viewpoints, though the regulator is not known to reach out to wider audience.

4.8 Accountability Mechanism

The approaches towards holding regulatory agencies accountable in India are by and large uniform across the sectors. Though the effectiveness of these mechanisms is debatable.

Table 5.4 Accountability Mechanisms for Regulatory Agencies in India

Regulatory Agency	Minister/Parliament	Appellate Body
Telecom Regulatory Authority of India (TRAI)	The regulatory agency submits its annual report of activities and audited financial accounts to the minister, which is then tabled in the parliament. Comptroller and Accountant General (CAG) of India carries out audit of accounts	Telecom Dispute Settlement and Appellate Tribunal (TDSAT).
Electricity Regulatory Commissions (ERCs)	Annual report of activities with audited accounts submitted to Minister, *w*ho tables it before the parliament (CERC)/legislative assembly (SERCs)	Appellate Tribunal for Electricity
Tariff Authority for Major Ports (TAMP)	The Authority has to submit annual report to the line ministry	Judiciary
Reserve Bank of India (RBI)	The Authority is required to submit annual report to the line ministry	-
Securities and Exchange Board of India (SEBI)	The Board has to submit a report to the line ministry on yearly basis.	Securities Appellate Tribunal (SAT)
Insurance Regulatory and Development Agency (IRDA)	The Agency has to submit a report to the line ministry on yearly basis.	-

In most cases regulatory bodies in India have to submit an activity report and audited financial accounts to the related line ministry every year. The Comptroller and Auditor General (CAG) of India is authorised to perform financial audit of regulatory bodies.

The line ministries concerned then table these reports in the parliament, though parliament is not known for analysing and debating such reports. In some cases, annual reports are not even submitted on time. For instance, the Committee on Paper Laid on the Table of the Lok Sabha thus observed, "TRAI has been a habitual defaulter in the matter of timely laying of their Annual Reports and Audited Accounts". These realities reflect on the effectiveness of the entire mechanisms.

Appellate tribunals have been set up in telecom, electricity, and capital markets. The laws related to insurance and banking sectors do not provide for such an arrangement. In case of insurance, setting up of an appellate body or making SAT as the appellate body is being discussed.

In telecom sector the role of the appellate tribunal, TDSAT, is quite wide. The telecom regulator is not empowered to settle disputes, rather the TDSAT has been assigned with the responsibility. This division of labour has adversely affected the performance of the telecom regulator, as any issue can be presented as a 'dispute'. Decisions given by appellate tribunals are contestable in the Supreme Court, but only on points of law.

Box 5.9 Telecom Regulator vs. Comptroller and Auditor General of India

As per the provisions of the TRAI Act 1997 the Comptroller and Auditor General (CAG) was authorized to audit the financial accounts of the TRAI.

In year 1999, TRAI recommended tariff structures for the industry through which tariffs were curtailed significantly which affected the revenue flows of the government -owned incumbent service providers as well.

On that, the CAG had asked the TRAI to justify its rationale for recommending tariff rates and alleged that the TRAI had unduly favoured the private operators. The CAG had demanded the justification to question TRAI on grounds that tariffs have financial and revenue implications, which are the domain of the CAG. This had led to a spat between the two autonomous institutions over turf issues.

Consequently, the TRAI had demanded that it be exempt from interrogation by the office of the CAG on issues of laying down tariffs and that the jurisdiction of the latter should be confined to investigate into the accounts only.

The issue was resolved only when the government brought an ordinance in year 2000 to amend the TRAI Act 1997. Now, the administration expenditure undertaken by the TRAI and several other directions made by it remain under the purview of the CAG. However, as per the provisions in the amended TRAI Act the orders of the regulator relating to revenue sharing between telecom companies and tariff fixation are not subject to CAG audit. Rather, the same is subject to an appeal to the Appellate Tribunal and a further appeal to the Supreme Court.

5. Concluding Remarks

The institutional structure of regulatory regimes in India especially within infrastructure services varies to significant extent. Regulatory objectives, autonomy, mandate, accountability, interface with government, etc are some of the parameters on which regulatory structure vary from sector to sector. This is primarily because a coherent approach towards the framework of regulatory

structure has not evolved as yet. As a result, good practices in one sector have not been followed in other cases.

Though several autonomous regulatory bodies have been set up and several more are likely to be established soon, the line ministries find it difficult to share their powers of regulation. In telecom, ports, and banking, government has retained the powers to supersede the regulatory agency. Further, it has retained the power to issue directives to regulators on policy matters. Notably, in case of insurance consultation with the regulator is mandatory prior to government issuing policy directives. This should have been provided in rest of the sectors as well. Similarly, appointment of regulators is left on preference and choice of the ministry concerned.

Lack of capacity among regulatory staff and stakeholders can be observed across sectors. In most cases an institutional arrangement has not been made so far to address that. Given the fact that institutional framework cannot compensate for individual's incompetence, the government needs to address this issue up front. Imparting powers to regulators to recruit competent staff and decide on their salaries are other crucial issues.

The current provisions of accountability are not very effective in practice. Pragmatic approach needs to be adopted to ensure that regulatory agencies work in proactive manner and maintain consistency. Perhaps, emergence of strong consumer advocacy would address that effectively. Provision for interface between competition authority and sectoral regulators is ambiguous and inconsistent.

Given this scenario, the Planning Commission of India is working towards developing a comprehensive framework for sectoral regulation in infrastructure sectors. One can hope for shortcomings and inconsistencies getting addressed soon.

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Chapter VI
Regulatory Environment in Cambodia

1. Introduction

Situated in the tropical region of South-East Asia, Cambodia covers a relatively small land area of 181,035 square kilometers, bounded by Thailand to the west and northwest, by Laos to the north, and by Vietnam to the east. The country is bordered to the southwest by the Gulf of Thailand. The capital city of Cambodia is Phnom Penh with a population of around 1 million people.

CAMBODIA COUNTRY PROFILE	
Population	13.4 million***
GDP (Current US$)	4.3 billion US$***
Per Capita Income (Current US$)	310.0 (Atlas method)*** 2,060 (at PPP)***
Land Area	181.0 thousand sq km
Life Expectancy	54.0 years**
Literacy	69.4 (of ages 15 and above)**
HDI Rank	130***

Source:
- World Development Indicators Database, World Bank, 2004
- Human Development Report, UNDP, 2003

(**) For the year 2002
(***) For the year 2003

Cambodia has an estimated total population of about 13.09 million people. The adult literacy rate[21] for males is considerably higher than those for females. Cambodia is one of the poorest countries in the world despite of the fact that poverty reduction has been incorporated as a major element of Cambodia's socio-economic development plans.

Being an agri-based economy, the country currently has more than 70 percent of its workforce employed in the agricultural sector. The contribution of agriculture in GDP has been in declining trend - contributing about 26 percent to GDP in 2004 down from 40 percent in 1995. The contribution of the industry sector has been increasing, whilst that of services seems to be stable. Industry sector contributed about 16 per cent in 1995, but due to quotas system for garment industry, its contribution rose to about 30 per cent in 2004. The service sector contributes about 45 percent to GDP.

Cambodia has been disrupted by civil war and isolated from the rest of the world under the Pol Pot (Khmer Rouge) regime and for quite long even after that. The country's basic infrastructure was totally destroyed; the intelligentsia devastated, including the majority of its legal, economic and engineering expertise. A democratic administration was established in 1993. However, most of the efforts did not come across effectively as the country continued to be torn apart by the civil war. It was only in late 1998 that peace was secured and a coalition government formed. Since then Cambodia has initiated fundamental reforms in many crucial areas and significant progress has been made in promoting economic recovery.

The economic growth picked up since the transformation in the 1980s of Cambodian economic policy to a free market economy from a centrally planned economic system. Economic growth reached the target of 7 to 8 percent per year. However, persistent weak governance and political crisis in 1997 combined with the Asian financial crisis at the same period led to a sharp economic slowdown. Cambodia's GDP growth slowed from 7 per cent in 2000 to 5.3 per cent in 2003.

[21] NIS defines Adult Literacy Rate as the percentage of literate persons aged 15 and above to corresponding population.

2. Evolution of Economic Policy Regime

In the developing world, Cambodia is special in view of the historical heritage of genocide during late 1970s. After the collapse of this dark regime in 1979, Cambodia pursued a centrally planned economic system and the country remained isolated from outside world except Soviet and Vietnamese assistance.

Cambodia's trading system was then totally controlled by the State. Land remained public property. During the first half of 1980s, the government permitted or recognized three economic sectors: the state sector, which comprised state industries; a co-operative sector, composed of rural production groups; and a family sector, consisting of rural or urban families engaged in the production of handicrafts or garden crops for exchange in state-controlled markets[22].

In 1987, Cambodia started to take initiatives in opening its economy by successfully abolishing state monopoly for foreign trade and adopted its first law on foreign investment in 1989, while the country was still in civil war. Reform towards the opening up of the economy in Cambodia was closely linked to the evolution of political situation in the country and external pressure. The pace of economic reform accelerated from 1989 as the Vietnamese army withdrew from Cambodia.

With support of international community, all conflicting political parties arrived at a common consensus through the 1991 Paris Peace Accord and international embargoes on aid and trade were removed. The 1993 Constitution sets forth a clear-cut market economy system where Cambodian people have full freedom to engage in trade and private ownership. The Government has undertaken many economic reform measures, which include trade liberalisation, privatisation and opening up of the economy. It, however, retains control over exports through licenses and permits on the grounds of compliance with the rules of origin required by other trading partners, health and security reasons as well as public interest concerns.

A new law on investment was adopted in 1994 with the intention to attract more investors to the country. The law regulated all investment, domestic or foreign, in Cambodia and granted national treatment to foreign investors, except in the ownership of land. The law also provided wide range of incentives to stimulate investment to both Cambodian and foreign firms. At the insistence of some donors, the 1994 investment law was modified in 2003 to provide a transparent, simple and predictable environment for private investments. The new investment law is more sophisticated than the old one especially in terms of procedures, while some forms of incentives, particularly tax incentives[23] have been removed.

All these reforms are closely linked to the integration of Cambodia into regional and global market. Cambodia became a member of ASEAN in April 1999 and committed to gradually reduce most tariff rates by 2010 under the AFTA (ASEAN Free Trade Agreement). In September 2003, Cambodia was fully admitted to the WTO with a package of deals that includes, in general, concessions and commitments to reducing tariffs, opening its service sector, and complying with the WTO Trade Related Aspects of Intellectual Property Rights (TRIPs) Agreement.

[22] Europa publication, The Far East and Australasia 2001, (Regional Survey of the World), 2001, p. 226
[23] In 2003, the investment law was amended immediately followed by the amendment of 1997 Law on Taxation.

The opening up of economy enabled competition resulting in lower price of imported products that has benefited Cambodian consumers. Anyhow, there are certain sectors where for a variety of reasons, competitive market may not exist or yield desired results, and require regulation. These sectors typically are electricity, telecommunications, transportation, water and banking sector. In Cambodia, the government directly regulates some of these sectors, while for others a specialised agency has been established to perform the regulatory functions.

Being one of the Least Developed Countries (LDCs) and now on its way to opening up and carrying out market-oriented reforms, Cambodia is striving to mobilise all domestic and international resources available, as well as grasp the opportunities for growth and development that have resulted from the liberalisation of trade and investment. In this context, the task of building a comprehensive framework of market-oriented laws to create well-functioning markets has moved to centre stage as an important priority on the development agenda of Cambodia. The various changes that are taking place in the policy landscape require a framework to ensure optimal regulatory intervention, stable institutions, and predictability, transparency, and accountability of state actions.

Against this background, the paper examines the institutional framework of sectoral regulatory agencies in Cambodia where in some sectors the Government continues to perform the regulatory function and in other a specialised agency has been set up to perform the regulatory function independently of Government.

Table 6.1 Evolution of Political, Legal and Economic Systems in Cambodia

Years	**Legal system**	**Political system**	**Political power**	**Economic system**
Before 1953	French-based civil code and judiciary	Under the French protectorate	Held by the French	Colonial
1953-1970 (The Kingdom of Cambodia	French-based civil code and judiciary	Constitutional monarchy	Held by Prince Norodom Sihanouk as prime minister	Market and then nationalization
1970-1975 (The Khmer Republic)	French based civil code and judiciary	Republic	Held by Lon Nol	Market, War economy
1975-1979 (Democratic Kampuchea)	Legal system destroyed	All previous systems abolished, extreme Maoist agro-communism	Khmer Rouge	Agrarian, centrally planned
1979-1989 (The People's Republic of Kampuchea)	Vietnamese communist model	Communist party, central committee, and local committees	Cambodian People's Party (Vietnamese backed)	Soviet-style central planning
1989-1993 (The State of Cambodia)	Greater economic rights	Communist party, central committee, and local committees	Cambodia People's Party (Vietnamese backed)	Liberalised central planning
1993-present (The Kingdom of Cambodia)	French-based civil code combined with common law in certain sectors	Constitutional monarchy	Shared between FUNCINPEC* and the Cambodian People's Party	Transition to a market economy

Source: Key Governance Issues in Cambodia, Lao PDR, Thailand, and Vietnam, Asian Development Bank, April 2001

* National United Front for an Independent, Neutral, Peaceful, and Cooperative Cambodia

3. Evolution of Sectoral Regulation

At the core of Cambodia's reform strategies has been privatisation that has been used as a principal means to release State intervention in trade activities. The privatisation can be divided into two stages. During the first stage (from 1991 to 1993), sectoral ministries had been granted authority to sell and lease State-owned enterprises (SOEs) within their area of responsibility with no requirement of external approval[24].

The most important privatisations took place during the second stage starting April 1995 following the issuance of a Declaration of the Cambodian Government on the Privatisation of Public Enterprises. An inter-ministerial committee was established under the leadership of the Ministry of Economy and Finance to draw up an inventory of existing enterprises, formulate privatisation strategies and monitor the privatisation process. The focus was on regulations intended to tighten and centralize the control over privatisation.

As a result, many SOEs were sold and leased to private sector. Some were formed as joint-venture enterprises. The privatisation program covers all trading activities of the public sector[25]. Nevertheless, reservation has been made in the area of natural monopoly or public service sectors where privatisation is being progressively undertaken in line with the establishment of appropriate regulations.

In Cambodia, the regulatory framework of regulated sectors varies from one to another in terms of the agency which performs the regulatory function. In some sectors, the relevant ministry acts as policy-maker as well as regulator and, in some other, a specialized agency has been established to perform the regulatory functions.

Among regulated activities in Cambodia, only electricity and banking sectors are currently regulated by special regulatory bodies with powers autonomous of the Central Government and line ministries; whereas, in sectors such as water supply, telecommunications and transport, the regulatory function is incorporated within sectoral ministries which simultaneously hold policy-making power in the area of their respective responsibilities.

Despite the above variations in approach towards regulation, the overall policy of the Government seems to be oriented towards the setting up of the independent regulatory body. In general, changes in Government's policies follows a common three stages of evolution. The process starts with

1. the endowment of the policy-making and regulatory powers together with the function of service operation/provision within each sectoral ministry, to
2. gradually providing autonomy to service provider/operators by means of privatisation or the establishment of state-owned enterprises, and ultimately
3. the setting up of independent regulator to perform regulatory functions, independent of the line ministry.

The various sectors that are being discussed in this paper have not moved at the same pace of evolution and that's the reason why different forms of regulatory agencies are currently in place. Thus, whereas the Ministry of Post and Telecommunication (MPTC) has been holding the conflicting roles as policy maker, regulator and service operator in the telecom sector, the

[24] WTO: Report of the working party on the accession of Cambodia dated August 2003 (WT/ACC/KHM/2), also available at: http://docsonline.wto.org/DDFDocuments/t/WT/ACC/KHM21.doc

[25] Declaration of the Royal Government on the Privatisation of Public Enterprises, dated December 20, 1994

National Bank of Cambodia has been given an independent regulatory status in the banking sector since the second half of the 1990s.

A brief examination of evolution of regulatory framework in three broad sectors: utility (electricity, telecommunications and water supply), transportation and banking follows.

3.1 Utilities

There are three main utility sectors: electricity, water supply and telecommunications. In these sectors, change in Government's policies on regulatory framework follows the three stages of evolution, as outlined above. The current different status of regulatory framework in each of these sectors derives from the pace of their evolution.

Electricity

Electricity appears to be the most developed sector in terms of regulatory institutional framework and the foremost economic activity in the area of energy sector; the other energy sub-sectors such as oil and gas are not yet economically feasible in Cambodia as the exploration of natural oil and gas is currently under government's domain.

Almost the entire electricity infrastructure in the country including generation, transmission and distribution facilities was destroyed during the civil war in the 1970s. After the liberation in January 1979, the Government of Cambodia started to restore electricity infrastructure in Phnom Penh City and main provincial towns of the country under the management of the Ministry of Industry, which acted as both policy maker and regulator. The electricity supply was directly governed by the Ministry, in Phnom Penh, through the "Electricité du Cambodge" (EDC), incorporated as an administrative structure of the Ministry and, in other provinces, through its provincial departments. Following the elections in 1993, EDC was restructured under the Ministry of Industry, Mines and Energy (MIME)[26].

The resurgence of economic activities and rapid improvement in the living standard of the population created an increased demand for electricity in the Kingdom of Cambodia. As a result, Cambodia needed to develop its power sector. But the resources at the disposal of the Government were considered to be insufficient to meet the rapidly increasing electric demand of each region.

Considering this situation, the Royal Government initiated an electricity sector reform process in 1996. The EDC was separated from the MIME and established as a wholly state-owned company to generate, transmit and distribute electricity throughout Cambodia. Simultaneously, the government promoted the private sector to invest in power sector to supplement the efforts of the State. Government's policy on power sector is limited not only to open the sector to private sector but also establish a fair and equitable environment for encouraging private investment in power sector.

Keeping this view, a Cambodia Power Sector Strategy was promulgated by the Ministry in January 1999. This strategy provides a comprehensive framework for the development of the power sector in Cambodia.

This was followed by the promulgation of the Electricity Law in February 2001 to regulate the business in power sector and govern the relation between electricity suppliers and consumers in a transparent manner. Subsequently, the government established the Electricity Authority of

[26] After the 1993's political election, there were changes in the ministries' structure and some of them were renamed.

Cambodia (EAC), as the Regulator of power sector. This was a big step of the Royal Government in carrying out reforms in the power sector.

The power sector in Cambodia is getting restored, after many decades of civil war. The electricity supply system still consists of large number of isolated systems, which are separately operated by different players at different locations and does not have major high voltage interconnection lines. Phnom Penh, provincial towns and other small towns have their own power system. Licensees in small towns, close to Cambodia – Vietnam border and Cambodia - Thai border, purchase electricity from neighboring countries for supply to the consumers in their areas but other areas have their own generation facilities.

The two main aims of the power sector development at present are:

- Long term development of the infrastructure of Cambodia's electric power system to ensure quality supply and meet the demand at reasonable price
- Meet the immediate electricity demand in different isolated regions in the interim, even at a cost of supply which may be higher compared to the cost after interconnection.

Cambodia still has very low capacity of power generation. The supply of electricity is very limited, especially in provinces. Many households in rural areas do not have access to electricity and where electricity is available, firms and individual consumers face some of the highest energy costs in the world. The cost of electricity is much higher than in neighbouring countries, Thailand (four times cheaper) and Vietnam (three times cheaper)[27].

Telecommunication

In the telecommunication sector, the policy and regulation functions are performed by the Ministry of Posts and Telecommunications of Cambodia (MPTC). In addition to these two roles, the MPTC had, until recently, operated the fixed wire network and also engaged in the international telephone gateway and the internet service provision. Since January 2005, all of these trading activities of MPTC have been transferred to Telecom Cambodia which operates as a separate SOE under the administrative supervision of the MPTC.

Cambodia has the unique distinction of being the first country where the number of mobile subscribers exceeds those on the fixed line network. The trend is being observed in many countries in the last five years or so, but in Cambodia this happened as early as 1993.

However, for Cambodia the reasons for this trend were not just the rapid advances in telecommunications technology. It was also the long civil war of the 1970s, which almost completely destroyed the existing fixed line network, and made its replacement or augmentation virtually impossible. The challenge of logistics and cost was huge. Mobile technologies came to Cambodia's rescue, since rollouts were much cheaper than fixed line networks as well as less time consuming.

Cambodia also recognized early that it would need private funding to augment the sparse resources of the government and was quick to initiate extensive liberalisation of all its telecom markets. Cambodia allows both local and foreign private investment although the latter must not exceed 49 percent. Following various recommendations from consultants and international telecommunication bodies to transform Telecom Cambodia into a commercial entity, there has recently been intention to privatise Telecom Cambodia[28]. Today almost all its market segments

[27] Khy Touk (2004): Industrial development in Cambodia: Main issues and opportunities, EIC Economic Review, vol. 1, No. 6
[28] Cambodia Daily, 11 March 2005, Vol. 31, issue 27

including fixed, mobile, Internet etc has several players that compete with each other. The market has seen dramatic growth in most segments especially mobile.

The fixed line business has three players including two private ones besides the MPTC. However the service is largely confined to the capital Phnom Pen with almost 80 percent of the fixed lines even though less than 10 percent of the population lives there.

Cambodia, unlike most other countries, does not have a dominant incumbent public sector operator. So the whole issue of regulatory reform, which is aimed at checking the dominant position of the public sector operator, is not required in Cambodia. The single biggest regulatory problem is to separate policy roles in the MPTC, since issues of policy development, sectoral regulation, and business operations are addressed and implemented by the same people in the same organization. The ministry is currently working on a draft communication law under which the establishment of an independent regulatory authority is intended.

Water Supply

In the water sector, the regulatory function is currently assigned to the MIME while the idea of establishing an independent regulator is being discussed in the national policy arena[29].

The MIME is responsible for water provision through its Departments of Provincial Water Supply in urban areas outside of Phnom Penh and through Phnom Penh Water Supply Authority (PPWSA), a State-owned enterprise, in the Capital City. All water supply systems are monopolies and operated almost totally by the public sector excluding 16 systems which are operated by the private sector through concession contracts. The water system faced high physical losses due to deterioration of pipes during the war and lack of appropriate maintenance thereafter. The proportion of the population with access to a water system is low (30 percent), especially in rural areas.

3.2 Transportation

The transportation system in Cambodia consists of the road network, railways, inland waterways and ports, and air transport. In these areas, both policy and regulatory power is assigned to line ministries of the Government: The Ministry of Public Works and Transport (MPWT) is responsible for the land and water transport while the State Secretariat of Civil Aviation (SSCA) is responsible for air transportation.

The evolution of policy for transportation has followed two important directions: the separation of the transport services from the sectoral ministry to be operated by state-owned enterprises in some sectors and the use of concessions with private companies in some others. For instance, in road transport, national route 4 is subject to concession to a private company while the other national route is under the management of MPWT.

Railway transportation is still under the state and is operated by the Royal Cambodia Railways (RCR), a state-owned enterprise. However, railway transport has not been popular among Cambodians due to poor state of railway infrastructure, lack of standards of the railway services and security concerns. Currently there are plans to establish a separate regulatory body and for the introduction of contracts with private companies in some limited areas.

[29] Royal Government of Cambodia, Policy on Clean Water Supply, 29 August 2000, Chapter 6

In the seaport and inland waterways sector, key services are provided by different state-owned companies. Besides there are private sector operators that run small-scale business. Competition between the two sets of enterprises is limited as their respective markets are potentially different.

Pertaining to civil aviation, the Government has granted concession to private companies to operate the two foremost airports of the country: Phnom Penh International Airport, contracted out on a build-operate-transfer (BOT) basis to a French-Malaysian consortium, and Siem Reap Airport, where a private company is authorized to operate the activities and share revenue with the Government[30]. In addition, the SSCA currently operates, manages and maintains seven other domestic airports where transport activities appear to be almost inactive commercially due to poor physical condition of the airports. Some forms of concession are being sought for upgrading five of these seven airports. Currently, there are 22 airlines having direct flights to Cambodia, and all are private owned.

3.3 Banking

Cambodia has a two-tier banking system consisting of the central bank and commercial banks. The National Bank of Cambodia (NBC) is the central bank playing an important role in the field of monetary policy and regulation, independently of the Royal Government.

Under the Khmer Rouge regime, all money had been abolished and the central bank physically destroyed. Cambodia started its initial reform in the banking sector during 1989-1992 after a period of centrally planned economy in the 1980s when banks had no active role in allocation of financial resources due to low development in banking skill. This reform process gave greater autonomy to provincial and municipal branches of the mono-bank but the legal and structural framework of this sector was not yet well adapted to the requirement of the market economy.

The most important structural reform was made in the second half of 1990s, when Cambodia's banking system was transformed from a mono banking to a two-tier banking system by separating the central bank's functions from commercial banking activities. The Law on the Organisation and Conduct of the National Bank of Cambodia was adopted in January 1996 to confirm this transformed system. Thereafter, two other important laws have been successfully adopted: the Law on Foreign Exchange, enacted in May 1997 and the Law on Banking and Financial Institution, enacted in November 1999.

Competition between banks appears to exist particularly in the areas of lending and deposits and in business services. There are fourteen commercial banks, of which one is owned by the government (Foreign Trade Bank). The Foreign Trade Bank (FTB) was under direct management of NBC until 2000 when it was separated from the NBC in order to transform its identity into a state-owned commercial bank. Five largest commercial banks including FTB hold more than 50 percent of total banking asset and deposit. There are plans to privatise FTB, but so far it is wholly state-owned.

Three specialized banks have also been recorded; one of them, the Rural Development Bank (RDB) belongs to the government. Besides, there are nine licensed microfinance institutions, and about 27 microfinance institutions registered as NGOs, while about 60 NGOs are providing microfinance but are not registered.

To strengthen the banking system in earlier 2000 the NBC conducted a bank re-licensing program based on increased capital requirement and the CAMELS rating system. As a result, the

[30] RGC – NIS, Second Five Year Socioeconomic Development Plan, 2001-2005, p. 187

number of banks has been reduced from 31 in 2000 to 18 in 2004. This action is expected to upgrade standard and improve soundness and reliability of banking system to build public's confidence. Additionally, financial sector blueprint for 2001-2010 was introduced, which seeks to ensure a competitive, integrated and efficient banking system that is properly regulated and supervised.

Table 6.2 Regulatory Institutional Framework in Cambodia

Sector	Enabling Legislation	Regulatory Body
Electricity	Electricity Law, 2001	Electricity Authority of Cambodia
Telecommunications*	-	Ministry of Post & Telecommunications of Cambodia (MPTC)
Water Supply*	-	Ministry of Industry, Mines and Energy (MIME)
Road Transport	-	Ministry of Public Works and Transport (MPWT)
Civil Aviation	-	State Secretariat of Civil Aviation (SSCA)
Seaports	-	Ministry of Public Works and Transport (MPWT)
Railways*	-	Ministry of Public Works and Transport (MPWT)
Banking	Law on the Organisation and Conduct of the National Bank of Cambodia, 1996	National Bank of Cambodia

* establishment of specialised regulatory agency, independent of government under consideration

4. Evaluation of Sectoral Regulatory Framework

In Cambodia, traditional form of government's regulatory intervention seems to share common points in terms of ministries' own functioning. A broad picture of regulatory mandates and institutional framework in the water, telecommunication and transportation sectors, where the Government directly intervenes to regulate, will help clarify the working of this traditional form of regulatory functioning.

4.1 Functioning of Ministries Performing Regulatory Functions

In general, the establishment of each ministry is subject to promulgation of an organic law adopted under a two-thirds majority of the Parliament. The organisation and functioning of each ministry is determined by the Sub-Decree of the Council of Minister promulgated by the Prime Minister.

Ministers are nominated by the King following a politic-based proposal of the Prime Minister and removed by same procedures. Each ministry generally comprises various legal, administrative, financial and technical departments. Sectoral regulatory affairs generally fall upon a specific technical department within a ministry, anyhow other related departments, especially legal and administrative department, usually get involved in the regulatory process. Evidently, this bureaucratic mechanism leads to complexity and uncertainty of procedures and thereby may give room for discretionary and arbitrary decisions.

The budget of all ministries is, under active control of the Ministry of Economy and Finance (MEF), and incorporated within the annual budget of the Government adopted by the Parliament.

In terms of roles and duties, sectoral ministries are in general mandated by the Royal Government to direct and manage their respective sector as both policy maker and sectoral regulator. They perform these functions under administrative control of the Central Government.

Telecommunications

The Ministry of Post and Telecommunication (MPTC) plays an important role in issuing licenses to various operators together with its function as policy maker. Yet, there is no legal provision governing these licensing procedures. In the absence of an enabling law, the decision of the MPTC regarding the issuing of a license seems to be obscure and discretionary[31]. Absence of clear licensing policy and timetable for telecommunications, gives rise to lack of transparency for newcomers to invest in telecommunications[32]. In particular, the contracts signed between the MPTC and private operators generally form restrictions on market entry. For instance, the contract signed between MPTC and Telstra[33], an Australian firm, for the establishment of an international gateway stated that no new gateways would be built[34].

It should be noted that before all trading activities were transferred to Telecom Cambodia which operates as separate SOE, much criticism were made of the Ministry for its direct involvement in the ownership of mobile services, fixed line network, and international gateways business while the Ministry also set telecommunication policy and acted as sectoral regulator. For instance, the MPTC issued regulation to ban Voice over Internet Protocol (VoIP) that offers overseas calls at lower prices. The reason behind this prohibition was simply that the VoIP would reduce state revenue from telecom industry, which contributed significantly to the state budget.

Another failure of the regulatory system is that of interconnection between operators. The system has not till recently allowed interconnecting operators to share revenues of calls between them after initially following a system that did. With the originating operator being able to keep all the revenues paid by the customer, there is little incentive for operators to interconnect. This has meant the network is not seamless. Customers cannot speak to their counterparts if they do not use the same service provider. A customer wishing to reach someone on a different network must use the many telephone cafes in the country, which maintain separate connectivity to diverse operators and allow customers to use it to connect to customers on networks that they cannot otherwise reach from their own phones. Lack of effective interconnection between operators is both a hassle and an additional cost to the end user.

Cambodia is still identified as one of the countries in the South East Asian region that has the lowest levels of penetration of information and communication technology (ICT). Not many persons have access to telephone line and internet. Only about 0.26 per cent of the total

[31] Samnang Chea, Denora Sarin, Hach Sok (2004): Cambodia's commitments under the general agreements on trade in services, EIC Economic Review, vol. 1, No. 4

[32] Monyrath Nuth, *The Competition Scenario in Cambodia,*2005

[33] Testra was the Australia Company that contracted with the MPTC to install the first international gateway for 10 years. Testra owned 51 per cent of the revenue and the MPTC took the remaining shares. Its contract was expired in 2000 and the gateway now is owned and operated by the MPTC

[34] International telecommunication union (ITU): Khmer internet: Cambodia case study, March 2002, p. 7

population access the telephone line. Internet access and telephone costs are high. So, only limited numbers of people in Phnom Penh afford high costs.

Nonetheless, considering its past history, Cambodia has made considerable improvement in telecommunications. Cambodia's mobile phone system is close to being world class. There has been a remarkable rise in the number of mobile phone subscribers. Mobile phone market is open to private investment and competition[35].

Transportation

In the area of transportation, apart from the fact that the Ministry performs conflicting roles as both policy maker and regulator, the ambiguity of procedure in some areas leads to conflict of interest since there are multiple agencies providing oversight, licenses and permissions to operate, but there is no or limited coordination between them. Weak legal framework on concession procedures, especially in the area of civil aviation, gets much criticism from civil society and international communities and gives room for conflict of interest between Government's agencies which tend to compete with each other to enter into concession negotiations with private sector investors[36].

Water Supply

In the water sector, the MIME is mainly responsible for:

- Controlling and supervising the production and utilisation of clean water in municipalities and urban areas;
- Preparing policies, laws and regulations related to the control and usage of clean water;
- Issuing authorizations to conduct clear water business;
- Facilitating and liaising with institutions concerned to provide clean water.

Since a key issue in the Cambodian water sector is that of technical development due to poor infrastructure, all water supply systems are monopolies and are generally operated under State intervention through the establishment of an SOE in Phnom Penh and direct intervention of the MIME. Only 16 licenses have been awarded to small private providers to supply water in some parts of provincial and district towns, where the SOEs are not able to supply water.

Phnom Penh is the only place that supplies water to majority of its residents through the Phnom Penh Water Supply Authority (PPWSA), a state company. In recent years, the PPWSA has made considerable improvement in its operations due to political stability, government support and external assistance and its "changing of culture" based on educating, motivating, and disciplining its staff and the public[37].

Table 6.3 Features of Conventional Form of Regulatory Functioning in Cambodia

Sector	Key features of regulatory functioning under line ministry
Telecommunications	• Issuing of licenses non-transparent and discretionary • Unpredictability for new/prospective players • Restrictions on market entry • Weak interconnection regime

[35] International telecommunication union (ITU): Khmer internet: Cambodia case study, March 2002, p. 34
[36] See some criticisms in "*Cambodia at the Crossroads",* World Bank – IMF, 2004
[37] ADB, *Phnom Penh Water Supply Authority: Leading the way to self-sufficiency*, 2005, also available on http://www.adb.org/water/actions/CAM/PPWSA.asp

Transportation	• Ambiguity of procedures • Lack of coordination between multiple agencies leading to conflict of interest

In these sectors, there is no procedure for consumer redressal other than the usual procedure of conflict resolutions through the common administrative and judicial complaint. Participatory mechanism, though included in sectoral policies and strategic plans of the Government, appears to be absent in the legal and regulatory texts.

The regulatory framework in sectors reviewed above displays the typical problems encountered in this conventional form of regulation: discretionary decision-making, lack of transparency and predictability, ambiguity of procedures, etc. Effectiveness of a regulatory regime depends on how it works i.e. on factors such as its transparency, participation, accountability and predictability. However, the regulatory framework in sectors reviewed above does not stand the test of these benchmarks. In view of this, the setting up of an independent regulator in telecom and water supply is welcome. The government of Cambodia is also considering a separate regulatory body for the railways. Considering the limited resources (financial and personnel), the government should instead explore the option of establishing a hybrid transport regulator to regulate all sub-sectors of road transportation, civil aviation, railways and marine transport. This would also facilitate economies of scale in regulation by a single agency.

4.2 Working of Specialised Regulatory Agencies

4.2.1 Electricity Authority of Cambodia (EAC)

The Electricity Authority of Cambodia was established under the provisions of the Electricity Law adopted by the Parliament in February 2001. The Authority has been assigned the powers and duties to:

- Issue Licenses to Electric Power Service Providers
- Approve Tariff Rate and charges
- Issue Regulations, Procedures, Rules, Orders and decisions
- Resolve complaints and disputes related to the provision of services and the use of electricity

The EAC is granted by the Government the autonomy to regulate the electricity sector throughout the country. Within the purview of the Electricity Law, this regulatory autonomy may be seen through the separation of the EAC's function as regulator from that of the MIME and through the ability of the Authority to operate on an autonomous budget and administration.

The Electricity Law provides that the MIME transfer in an orderly manner the functions and duties defined in the law to EAC. The two main functions in power sector in the Kingdom of Cambodia are:

- Setting and administrating government policies, strategies, and planning
- Regulating, liaison, and arbitration between provision of services and use of electricity

The law provides that these two functions shall be separated from each other and assigned to the MIME and the EAC, respectively. Accordingly, MIME chalks out the path that power sector in Cambodia would take. It is also responsible for setting the technical standards for the power sector. EAC on the other hand is responsible for issuing rules, regulations and procedures to

monitor, guide, coordinate, including requiring both suppliers and consumers to follow the policy and guidelines and technical standards issued by the MIME (Table 6.4).

Table 6.4 Role of Line Ministry and Electricity Regulator in Power Sector in Cambodia

MIME	EAC
• Energy Policies • Electric Power Strategies • Power Development Plan • Technical, Safety, Environmental Standards	• Issue regulations • Licensing • Review cost and approve tariffs • Resolve disputes, Impose penalty

Along with this separation of power, interaction between the two agencies is clearly stated in the Electricity Law, which provides that the Ministry must provide the EAC all information on policies, strategies, planning and its decision concerning any reform in the power sector[38]. All of this information would be used as basis by the EAC in its own functioning[39].

In organisational terms, EAC consists of three members, including Chairman, and supported by a Secretariat. The Chairman and members are appointed by the King under proposal of the Prime Minister for a period of three years. No member is appointed to serve in the Authority for more than two terms. The members may be suspended from duties by the Prime Minister in case where they lose their civic right, are found to be mentally or physically incapable, or have committed any violation of their legal obligations or any breach of their professional responsibilities[40]. The Prime Minister refers the case to the competent court for decision and appoints temporary member for the suspension period. The members of the Authority retire from office when they attain the age of sixty. In case of retirement before the expiry of the term, the Prime Minister may permit the member concerned to continue his/her duties until the expired date of his/her term as necessary.

Until two-years after the completion of their term, neither the chairman nor any member can enter into employment or have any advisory or consulting relationship with any licensee.

The salary allowances, etc of members are determined by the Government. The chairman of the Authority, in consultation with other members, appoints all employees and hires other experts as may be necessary for the proper discharge of Authority's duties. The Authority determines the salary, and other remunerations of its officers and employees.

The EAC has an autonomous budget for its operation, which is resourced from fees paid by applicants and licensees. The EAC determines the license fee, subject to the maximum stipulated in a sub-decree of the Royal government. For each financial year, the Authority prepares a budget that sets forth its expected revenues and expenses, and states the proposed license fees together with the method of calculation. The budget is then submitted to the Government for review and approval.

EAC's annual financial statements, together with its accounting books are inspected by the National Audit Authority. Subsequently, the reports are submitted to the Prime Minister for approval, and published for public.

[38] Article 4, Electricity Law – 2001
[39] Article 5, Electricity Law – 2001
[40] Article 14 of the Electricity Law stipulates 6 cases on which the member may be subject to suspension.

In relation with electricity service providers, the Electricity Law defines EAC's duties which mainly deal with issuance of licenses, approval of cost and tariff rates, resolution of disputes over conditions of license, and other regulations ensuring quality and quantity of service provision and compliance with technical standards and overall policies of the Government.

In the context of licensing, EAC may issue, revise, suspend, revoke or deny licenses for supply of electricity services[41]. Both private sector and state-owned enterprise in principle may hold any license but special rights and priority are reserved for the state-owned company, Electricité du Cambodge (EDC). With this special right, the EDC provides transmission service throughout the country, except in particular territory served by any other isolated systems of the private sector where the EDC's transmission service cannot reach properly.

Currently, the EDC is provided with a consolidated license consisting of rights to generation, distribution and transmission services. The license grants it monopoly over transmission service for the entire country, and allows it to provide distribution service in its licensed areas and operate generation facilities at different locations.

Electricity Authority of Cambodia follows a transparent policy in deciding terms of license of electric power service providers. In cases, where improvement is made to electricity facilities and business is managed efficiently, licensees have a right to apply for extension of the term of license and EAC grants a longer term license. In case a service provider fails to improve its electricity facilities, operation and management, EAC selects another entity having ability to provide better service and revokes license of entity that fails.

Participatory mechanism has been incorporated in decision-making process of the Authority. Sessions of the EAC for hearing of any complaint are made public. The Authority's decisions, with its reasons, are published. All orders, findings, judgments, records and other documents are open to public examination in the offices of the Authority, except for information that is required to be kept confidential, provided the Authority adopts appropriate rules to ensure such confidentiality. Before promulgating any general order, or any rule or regulation, the Authority gives reasonable notice of its contents and an opportunity to interested persons and public to present their evidence and provide their opinion. Wide consultations are held before granting license.

After the Authority issues a final decision, each affected institution and party has the right of appeal to the Court of the Kingdom of Cambodia.

4.2.2 National Bank of Cambodia (NBC)

The National Bank of Cambodia, the central bank, is an autonomous public entity governed by the Law on the Organization and Conduct of the National Bank of Cambodia, adopted in 1996. The main mission of the central bank is to determine and direct the monetary policy aimed at maintaining price stability.

The central bank has been given operating autonomy from government's line ministry, the ministry of economy and finance (MEF). It is required to submit reports of the implementation and results of its mission to the National Assembly and the Royal Government. At the invitation of the Government, the Governor of NBC may address meetings of the Council of Ministers

[41] Article 35 of the Electricity Law defines *Consolidate License* as one which may be the combination of some or all of the other licenses.

(the Central Government). The Minister or Secretary of State of the MEF may also address meetings of the NBC's Board of Directors at the invitation of latter. The Governor or members of the Board may appear before the National Assembly or standing committee thereof to explain policies of the central bank or to comment on proposed legislation, at the request of the National Assembly[42].

In its relation with the Government, the central bank is the sole depository for the National Treasury (attached to the Ministry of Economy and Finance); the NBC receives from the National Treasury and disburses on its behalf, money and keeps account thereof; and, any charges to be levied by the central bank for these services is subject to the agreement of both parties[43]. In general, NBC acts as advisor to the Government on monetary and financial matters and has duty to inform the Government concerning any problem which in its opinion is likely to affect the achievement of objectives of monetary and financial policies.

In management[44] terms, the Board of Directors acts as managing organ of the central bank, consisting of seven members including the Governor – the Chairman thereof, the Deputy Governor and five other members, one being a representative of the Government, one of the MEF, one from the private sector, an academician and one representative of the National Bank staff.

The Governor and Deputy Governor are appointed, replaced and dismissed by Royal Decree on the recommendation of the Government. The nomination, replacement and dismissal of other members of the Board are subject to a sub-decree of the Government. The members of the Board are to be appointed for a period of four years and are eligible for re-appointment for only one further term. The reasons for dismissal of their membership are explicitly mentioned in the Law.

The annual budget of the Central Bank is approved by the Board of Directors and submitted for information to the Government and the National Assembly[45].

The Governor may appoint the officers and staff of the NBC and make proposal to the Board of Directors on the salaries and benefits for senior staff. The Governor and Deputy Governor receive remuneration from the Central Bank in the same amount as a member of the Government.

With support from international communities and donor agencies together with its internal policy, the NBC has made considerable progress in the area of human resource development through providing training and scholarship to its staff. While all civil servants of the Government are subject to a common statute, the NBC's staff is governed by a particular statute and their salary rate is particularly high when compared to Government's civil servants'.

The NBC is required to keep all books of account which reflect its financial position, and prepare and publish monthly statement of its activities. All its financial records are verified by a special committee appointed by the Government[46]. The NBC is required to submit to the

[42][42] Law on the Organization and Conduct of the National Bank of Cambodia, article 9
[43] Law on the Organization and Conduct of the National Bank of Cambodia, article 21
[44] Management of the NBC is regulated by Title IV of Law on the Organization and Conduct of the National Bank of Cambodia
[45] Law on the Organization and Conduct of the National Bank of Cambodia, article 20
[46] Law on the Organization and Conduct of the National Bank of Cambodia, article 57

Government and the National Assembly a copy of its annual accounts together with a report on its operations and on monetary and economic conditions during the year.

In relation with financial institutions, the central bank is exclusively responsible for the licensing, and supervision of commercial banks and other financial institutions[47]. To this end, the NBC is empowered to:

- Issue decisions, regulations, and other directives to execute its powers and responsibilities through proper licensing and supervisory standards and enforcement procedures;
- Appoint at its decision, its officers or any other qualified person to regularly inspect any bank or financial institution and examine relevant books, records, documents and accounts thereof;
- Require an officer, or employee of a bank or financial institution to furnish such information as requested for the purpose of supervision and regulation;
- Take remedial actions according to existing laws if there has been an infraction committed by a bank or financial institution or officer thereof.

A list of all licensed banking institutions must be published in the Bulletin of the NBC[48]. All decisions and regulations of the central bank are published in the Official Gazette of the Kingdom.

Table 6.5 Features of Specialised Regulatory Agencies in Cambodia

Functional/Organisational Aspect	Electricity Authority of Cambodia	National Bank of Cambodia
Composition	• Three (one chairman and two members)	• Seven (Governor, Deputy Governor and five other members)
Appointment	• Proposed by the Prime Minister and appointed by the King	• Governor & Deputy Governor appointed by the King on recommendation by the government • Other members appointed by the Government from a list prepared by the NBC Governor.
Term of office	• Three years, renewed for one further term	• Four years, renewed for one further term
Removal/Suspension	• Reasons for removal explicitly provided in the law. In certain circumstances the Prime Minister can suspend a member and refer matter to the competent tri bunal for decision	• Explicitly mentioned in the Law
Salary/allowances	• Determined by the Government	• Determined by the Government
Power to appoint staff	• EAC empowered to hire own staff • Staff salary and benefits determined by the EAC	• Governor appoints office r and staff • Staff salary and benefits determined by the NBC
Financial autonomy	• Autonomous budget, resourced from fees determined by EAC and paid by applicants and licensees • Budget approved by the Government	• Autonomous budget, resourced from NBC's income • Budget approved by Board of Directors of the NBC and submitted to the government for information
Relation with the line	• Clear separation of roles	• Operating autonomy from line

[47] Law on the Organization and Conduct of the National Bank of Cambodia, article 33
[48] Law on Banking and Financial Institutions, Article 15

Functional/Organisational Aspect	Electricity Authority of Cambodia	National Bank of Cambodia
minister	• Nature of interaction clearly stated in the law	ministry • Governor invited to address meetings of the Council of Ministers; Minister or Secretary of State of the MEF may also address meetings of NBC board
Accountability	• Annual Reports submitted to the Prime Minister for approval	• Submit reports of its operation to the Government and the National Assembly • The National Assembly or its standing committee may ask the NBC Board to explain its policies

Several commonalities of approach exist in the functional and organisational aspects of the EAC and the NBC. This reflects consistency in the approach to establishing specialised and independent regulatory bodies in Cambodia.

5. Concluding Remarks

Cambodia is fast emerging from its dreaded history. Efforts are on to put in place necessary infrastructure with the assistance of private sector to put the economy on a high growth trajectory. These efforts are bearing fruit as progress is witnessed in telecommunications, electricity supply, etc. Necessary institutional changes are being made to create conducive environment for the participation of private sector. In this context, independent regulatory agency has been created in electricity and banking sector, whereas similar efforts are on in telecom, water supply and railways.

The objective of government's sectoral policies towards establishing independent regulators is mainly aimed at improving accountability, predictability, transparency and effectiveness of the service provision. Keeping these objectives as the benchmark, it is observed that in the conventional form of regulatory functioning, where the line ministry performs regulatory function as well, absence of an enabling legal framework renders relevant procedures ambiguous and thereby gives room for discretionary or arbitrary decision.

Moreover, traditional regulatory method of centralizing regulatory power within sectoral ministries seems to present a constraint on the effectiveness of Government's intervention in managing regulated sectors, given the fact that the same ministry often performs conflicting roles of a regulator, policy maker and service provider. In such cases, relevant ministry in its capacity as administrative supervisor of each SOE gets involved in trading activities of regulated sector of which it holds function as both regulator and policy maker.

Thus, for instance, though EDC is a legally separate entity, it has been difficult for the Government to separate its own role as sector policy maker from its interests as one of EDC's largest customers, and to refrain from interference in EDC's operation. Therefore, despite remarkable improvement in electricity provision in recent years especially in Phnom Penh area, the EDC has been plagued by financial problem, arising from its inability to pass increases in the cost of power to consumers, and from high arrears in bill payment by government entities.

The regulatory structure that has evolved in electricity and banking are commendable. The government of Cambodia has provided financial autonomy to independent regulatory agencies

(EAC and NBC). Regulatory agencies have been given power to hire own staff and determine their salary structure. Relation with line ministry and National Assembly has been clearly spelt out in the law, which gives operating autonomy to regulatory agencies. In this context, provisions in Electricity Law clearly demarcating and specifying the respective roles of MIME and EAC, and the nature of interaction between the two agencies is worth emulating. Further, requiring the Governor or members of the NBC board to appear before the National Assembly or its standing committee to explain the central bank's policies are revealing. All these measures reflect the level of wisdom Cambodia has applied in addressing issues relating to regulatory framework that often impair functioning of independent regulatory agencies.

Given the commonalities of approach that exist in functional and organisational aspects of EAC and NBC, a similar framework is expected to emerge in other sectors as well. Since government's policy is currently oriented toward this new form of intervention, key issue therefore is the pace at which government moves to reach this orientation, through fastening the adoption of appropriate legal instruments that establishes these independent regulators.

It should be critically noted that empowerment of an independent authority to regulate a whole sector may easily lead to abuse of power if State's judicial mechanism is not strong enough to enforce and limit the autonomous rights provided to such authority. Apart from enhancing the current court system, the idea of recognizing and promoting the establishment of "consumers organisation", together with existing chambers of commerce, appears to be beneficial in combating the occasional abuse of power and ensuring consumers' and traders' interests.

This paper has given a brief overview of sectoral regulatory framework in Cambodia. The next task should be to assess the impact of functioning of regulatory bodies in meeting various objectives.

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Chapter VII
Regulatory Environment in Indonesia

1. Introduction

Indonesia is situated in Southeastern Asia and consists of a large archipelago between the Indian Ocean and the Pacific Ocean, with more than 13,000 islands. The largest islands are Java, Kalimantan (the southern part of the island Borneo), Sumatra, Sulawesi, and Papua (formerly Irian Jaya, which is the western part of New Guinea). Indonesia's total land area measures 1.9 million square kilometers. The size of Indonesia's population is about 230 million (2002), of which the largest share (roughly 60%) lives in Java.

INDONESIA COUNTRY PROFILE	
Population:	217.6 million***
GDP (Current US$):	257.6 billion***
Per Capita Income: (Current US $)	1,140 (Atlas method)*** 3,500 (at PPP.)**
Surface Area:	1.9 million sq. km
Life Expectancy:	67 years***
Literacy (%):	88 (of ages 15 and above)***
HDI Rank:	111 ***
Unemployment rate (%):	25.5%***

Sources:
- World Development Indicators Database, World Bank, 2004
- Human Development Report Statistics, UNDP, 2004

(**) For the year 2002
(***) For the year 2004

Apart from fertile land suitable for agriculture, Indonesia is rich in a range of natural resources, varying from petroleum, natural gas, and coal, to metals such as tin, bauxite, nickel, copper, gold, and silver. These resources propelled Indonesia to a strong economic growth for some 30 years.

Indonesia has been viewed as one of Southeast Asia's successful highly performing and newly industrialising economies, following the trail of the Asian tigers (Hong Kong, Singapore, South Korea, and Taiwan). Although Indonesia's economy grew with impressive speed during the 1980s and 1990s, it experienced considerable trouble after the Asian financial crisis of 1997 and by political turmoil in the country in 1998, which led to significant political reforms. Its per capita GNP, which peaked at US$ 1,120 in 1997, dropped sharply to US$580 in 1999, and recovered to US$690 in 2001.

Indonesia is now emerging from its political and economic crisis and has undergone tremendous changes in its structural and political reforms since 2001. These include major political liberalisation, the "Big Bang" decentralization on January 1, 2001, and an economic recovery and poverty reduction program. These have resulted in an upturn in economic growth, with a GDP growth averaging 4 percent over 2000 and 2001. Industry contributes the biggest percentage of GDP, which is 43.7%. Agriculture contributes 15.4% of GDP, and Services contribution is at 40.9%. Import of goods & services is 26.9% of GDP.

Several economic development problems remain, including poverty that reached 27% of the population, high unemployment (25.5% of those at productive age in 2004), a fragile banking sector, endemic corruption, inadequate infrastructure, a poor investment climate, and unequal resource distribution among regions.

Indonesia became a net oil importer in 2004 due to declining production and lack of new exploration investment. As a result, Indonesia is not reaping the benefits of high world oil prices,

and the cost of subsidizing domestic fuel prices has placed an increasing strain on the budget. Keys to future growth remain internal reform, building up the confidence of international and domestic investors, and strong global economic growth.

2. Evolution of Economic Policy Regime

The Indonesian Constitution of 1945 envisaged a democratic economic system. Article 33 of the Constitution provides as follows:

- The economy shall be organized as a common endeavor based upon the principles of the family system.
- Sectors those are important for the country and have an effect on the life of the people shall be controlled by the state.
- Natural resources such as land, water, shall be controlled by the State and exploited to the greatest benefit of the people.

Clearly, the welfare of the community was to predominate over that of individuals or particular groups. Such a conception clearly excludes any monopolies and restrictive or unfair trade practices by particular individuals, families or groups.

However, the sprit expressed in the Constitution has not been translated into actions by and large. Wealth has been concentrated amongst individuals and particular families who dominate various sectors of the economy and benefit of economic growth has not been distributed across the population. This concentration of wealth has given certain individuals and families the power to determine availability, quality and prices of the products offered to Indonesian consumer. Traditionally, businesses in Indonesia were protected from competition. Consequently, many of them were inefficient and involved in restrictive and unfair trade practices. Corruption was perceived to be rampant. The protected environment was not offering the businesses incentives to innovate and become efficient. All of this burdened the economy, heavily.

This phenomenon was further facilitated and flourished when politicians got actively involved in business activity. Political power was used to increase economic power and vice versa. Many of the policies of government were perceived as designed to profit only certain groups. Monopolies were provided protection from competition that resulted into exploitation of consumers and poor economic efficiencies. The clove and orange business in the agro-industrial sector and the national car project in the automotive industry sector are representative examples where political influence was used in creation of monopolies.

Bilateral and multinational assistance played a major role in Indonesia's development. Before 1965, Indonesia received substantial aid from the USSR and other communist states. Since 1966, foreign-aid pattern turned dramatically towards the West. A group of nations (including the United States, Netherlands, Japan, Belgium, France, Germany, Italy, United Kingdom, Switzerland, Canada, and New Zealand) and multilateral organizations (including the IBRD and Asian Development Bank) have joined to form the Inter-Governmental Group on Indonesia (IGGI) as a major funnel for aid. IMF too has been playing an important role in reorganization of Indonesia's financial structure and planning.

Indonesia follows a 'Five Year Plan' approach. Till mid 1970s the emphasis was on development of agriculture and agro-based industries including production of fertilizers, cement, agricultural

equipment, and agro-processing machinery. Assistance was also given to import-substitution industries such as textiles, paper, rubber tires, and housing materials.

During 1980s, the economy was growing at 6 percent/annum. The 1979-84 Plan emphasized the "development trilogy" of economic growth, equity, and national stability. Top priority was given to tourism and communication, agriculture and irrigation, mining and energy, education, and regional and local development. The subsequent plan, 1984–89, too focused on industry, agriculture, petroleum and mining, transportation and communications, and construction. However, low oil prices caused the government to reduce the developmental role. The next plan, 1989–94, witnessed specific priorities such as development of mining and energy, certain areas of manufacturing, forestry, agriculture, transportation, communications, and tourism. The discussions on privatisation were initiated by then.

The Guidelines of State Policy 1988 set out an important economic development policy framework which was aimed to promote privatisation and liberalisation as measures to overcome uneven population distribution in various regions of Indonesia, and equitable growth.

The stated goals of the sixth five-year development Plan (1994–99), included attainment of an annual average GDP growth rate of 6.2% and focus was on privatisation of a number of industries, and the gradual opening up of foreign investment. These goals were met till 1997, however in 1997-98 Indonesia witnessed an unprecedented economic breakdown. The debt burden went out of control and Indonesian currency lost its value significantly. The breakdown of the economy prompted international aid agencies to step in. An IMF-funded program that began in 1997 offered a total of $12.5 billion to Indonesia over a period of three years to support the financial system and aid in the restructuring of the economy.

With the fall of the Suharto government in 1998, after 32 years of continuous rule, came the reformation movement sponsored by intellectuals, students and other components of the nation politic. The stated objectives of the reformation movement included, clean and efficient government, good corporate governance, and the supremacy of law.

In August 1998, Indonesia and the IMF agreed on an Extended Fund Facility (EFF) under President B.J Habibie that included significant structural reform targets. President Abdurrahman Wahid took office in October 1999, and Indonesia and the IMF signed another EFF in January 2000. The new program has a range of economic, structural reform, and governance targets.

Both competition law and consumer protection law were ratified in the year 1999. This was considered as a historical milestone for the Indonesian economic system. The enactment of these two laws is part of the effort to achieve the aims of reformation.

3. Evolution of Sectoral Regulation

Water supply, highways, energy, and telecom are some of the sectors that are traditionally considered of strategic importance hence have been entirely managed by the national government/government-owned companies. As a reform measure, specialised regulatory bodies have been set up in all the four sectors at national level. At provincial level, there are other bodies as well, for instance, to regulate drinking water sector and transport sector in Jakarta, the capital city of Indonesia. This section charts out the evolution of regulatory regime in select sectors in the country.

3.1 Telecommunication

Telephone services started in Indonesia way back in year 1882 and at that time was provided by a privately owned company. The government in 1906 attained control of the sector and started delivering telecom and postal services.

In year 1961 a major change in the policy was observed. The government transferred most of these services to a company that was formed for the purpose, and its ownership kept with the government. Later, the company was split into two, to focus on telecom and postal services separately.

In 1974 the telecom company was further divided into two, on a functional basis. One of them, Perumtel, was vested with the responsibility of providing telecom services in Indonesia while the other, PT Inti., was to manufacture telecom apparatus.

In 1980 Perumtel's business was further divided into two and its international business was transferred to another government owned company called PT Indosat. Corporatisation of Perumtel took place in 1991 and it was renamed as PT Telekomunikasi Indonesia (PT Telkom).

The Indonesian telecommunications sector was initially regulated under the regime of Law No. 3 of 1989 on Telecommunications. As per this law, telecommunications services were divided into two categories: basic services such as telephone, telex and telegram, and nonbasic services, i.e. all value added services. Operators other than the two state-owned enterprises were allowed to provide basic telecommunications services upon (mandatory) cooperation with either Telkom or Indosat. Under this arrangement, any private entity seeking to provide basic telecommunications services could do so only in conjunction with Telkom or Indosat through either joint venture, joint operation (KSO), or management contract.

The regulatory framework of the post-1989 telecommunications regime heavily supported the monopolistic practices of the two incumbent operators, especially within the area of basic telecommunications services.

In order to encourage investment in basic telephony services, the Government decided to award 'exclusivities' on basic services from 1996. Telkom was granted exclusivity on local fixed wire services to 2010 and on domestic long distance services to 2005. For international services, Indosat and a part private company, PT Satelindo, were granted a duopoly until end-2004. The local fixed wireless market was designated as being open to limited competition and in 1994 one company (PT Ratelindo) was awarded a license. Mobile services were designated as open to competition, and by 1996 three companies (Satelindo, Telkomsel, Excelcomindo) had been awarded national GSM 900 licenses while several others were awarded licenses for analog services. Each of the new license holders was required to have either Telkom or Indosat as a shareholder. Thus, despite the entry of new players the sector continued to be controlled by the two state-owned enterprises.

The onset of the economic crisis underscored the need for liberalisation, leading the Government to prepare a 'Sector Blueprint' outlining its strategy for transition to full competition by 2010. This was in line with the rapid technological advances and development of the telecommunications industry. The Blueprint provided the framework for a new Telecommunications Law, enacted in 1999 to facilitate introduction of competition in the telecommunication sector. Among the key objectives were to: improve the performance of Indonesia's telecoms sector, and increase transparency and lucidity in regulatory processes, thereby ensuring that investors will have sufficient certainty in their respective investment plans.

The 1999 Act removed the separation between basic and non-basic telecommunications services applicable during the previous regime. Instead, the Government chose to differentiate the industry between telecommunications network operators and telecommunications service providers, whereby licensing is granted based on the business feasibility of prospective companies. Telecom operators are no longer obliged to enter into cooperation or form a partnership with incumbent operators, as was the case during the previous regime.

Table 7.1 Reforms Introduced by New Telecommunications Law in Indonesia

	Law 3/1989	Law 36/1999
Operator	Government through SOEs as Organizing Bodies	Public and privately -owed companies and cooperatives
Service Categories	Basic and non -basic services and special telecommunications	Telecommunications networks, telecomm unications services, and special communications
Business Modalities	Cooperation with an SOE through joint venture, operating concession or management contract	No obligation to cooperate with an SOE.
Exclusivity	Monopoly (local, domestic long distance) a nd duopoly (international) exclusivity for basic telephony services	Monopoly practices forbidden Provision for accelerated termination of exclusivities for basic services subject to fair compensation
Tariffs	Determined by Government	Determined by operator s based on formula established by Government
Interconnection Agreement	Interconnection and other payments due by other operators to Telkom are determined by Government	Establishes right and obligation of network operators to obtain and provide interconnec tion, and outlines principles on which agreements are to be negotiated
Regulator	Government	BRTI consisting of the Directorate General of Posts & Telecommunications and the Committee on Telecommunications Regulation

Source: Adapted from PT Telkom 2001 Annual Report

Recognizing that a regulatory body endowed with sufficient legislative authority is required to regulate and supervise the ongoing process of reform and also to enforce the laws and regulations of this sector, the Government, in July 2003, issued a ministerial decree on the establishment of an independent regulatory body in the telecommunications sector. The decree states that, "BRTI is the Directorate General of Posts & Telecommunications and the Committee on Telecommunications Regulation." The aim of the regulatory body is to ensure transparency, independency and fairness in the operations of telecommunications networks and the provision of telecommunications services. It is expected that the independent regulatory authority will facilitate improvement in the performance and service in the Indonesian telecommunications sector.

The Telecommunications Regulatory Committee consists of five members, including the position of chairmanship, which is assumed by the Director General of Posts and Telecommunications. The four other members are experts in technical (telecommunications & IT), legal, economics and social fields.

The setting up of the regulatory body reflects the Government's positive attitude in encouraging and endorsing the liberalisation process of the telecommunications sector. This is because establishment of an independent telecommunications agency is not explicitly mandated under the Telecommunications Act, but instead, it is only implicitly stated in the elucidation of one of the articles (article 4.2) of the Telecommunications Act of 1999.

Indonesia's telecommunications sector has weathered the economic crisis moderately well. Dramatic growth in the number of mobile subscribers since 1997 has been accompanied by increases in numbers of fixed lines in service, public payphones, teleshops (wartels) and internet shops (warnets). Despite reverses, private sector interest has also remained strong, as evidenced by the government's sale in December 2002 of an additional 41.9% interest in international and mobile operator PT Indosat to Singapore Technologies Telemedia Pte Ltd (STT), changing the status of Indosat into a *foreign investment company*.

Now, the monopolies are largely dismantled and competition is being introduced. The cross-ownership between PT Telkom and PT Indosat of third parties are being dissolved and processes are becoming relatively transparent. Competition is being introduced in all segments of the industry that has been helping in expansion of services across the regions and increase tele-density.

Over the decade from 1991 to 2001, the number of main lines in service has grown from 1.27 million to 7.22 million at an average annual growth rate of 19%, with teledensity increasing from 0.68 lines to 3.25 lines per 100 residents. As elsewhere in the region, the mobile market has enjoyed explosive growth. By the end of 2002, the number of mobile subscribers for the first time exceeded the number of fixed lines.

3.2 Water Supply

In Indonesia development of drink water sector was initiated in 1970 and the Law No. 22/ 1999 on Decentralisation and related regulations vested the local governments (of the Town /District) with the authority to implement and manage drink water piping system in their respective areas. At present, nearly 316 town/districts provide piped water through the Drink Water Regional Companies (PDAMs). Nevertheless, piped water reaches only 39 percent of the urban population. The corresponding coverage in rural areas is only 8 percent.

In last three decades, though the capacity of drinking water production in Indonesia has increased substantially, from 9,000 litre/second in 1970 to 94,000 litre/second in 1997, however is not sufficient to meet the growing demand. The economic crisis of 1997 has also impeded the pace of capacity addition for drinking water production. Government continue to invest huge money in the sector and government run municipal water enterprises (PDAMs) face many financial and managerial challenges in meeting the growing demand.

In Indonesia, the government initiated public private partnerships (PPP) in the water supply sector since the mid 1980s, though on a small scale. The major functions outsourced to private sector include meter reading, bill collections, and maintenance work.

In 1993, the first PPP project was set up on a BOT (Build, Operate and Transfer) basis in Serang Utara. Subsequently, in 1995, the next concession given to private sector was for the water supply services in Batam Island. In 1998, modified concession was given in western part of Jakarta which was followed by commencement of another PPP project in the Eastern Jakarta.

The Jakarta Water Supply Regulatory Body (JWSRB or RB) was established through Governor Decree no 95/2001 in September 2001.

In year 2002 in response to realisation of the constraints being encountered by PDAMs the government of Indonesia constituted a Sub-Committee for improving the performance of PDAMs. The Sub-Committee suggested following measures to improve the condition of PDAMs.

(i) Implementation of professional drink water management based on entrepreneurship principles;
(ii) Improve the quality of implementation of drink water services in accordance with full cost recovery principle without ignoring the interest of low-income people
(iii) Accelerate settlement of PDAM debts;
(iv) Establish and improve coverage of planned drink water services for the community;
(v) Increase government support on the aspects of management, funding system and adequate supply of water.

In year 2004 a new water resources law (No. 7/2004) was enacted to focus on the provision of sustainable water resources, management of water supply and waste-water, and participation of the private sector as well as PDAMS and the community. A supplementing government regulation on water supply and sanitation proposes to formulate the role, responsibility, rules and procedures to enable local governments in management of the water supply and wastewater system and to involve private sector in water projects.

The Regulating Body for Drinking Water for Jakarta was formed in 2001. The objective was to find win-win solution for the government and consumer. Currently BR's jurisdiction is confined to Jakarta.

Drinking water management in Jakarta is handed over to private sector, PT Palyja and PT TPJ (Thames Pam Jaya), in order to achieve effectiveness. The establishment of BR is a significant step forward. Before 2001, Regional Government of DKI Jakarta was a central actor in managing drinking water business with the capacity as regulator. Pam Jaya acted as monitoring body, and PT Palyja and TPJ acted as operator and organizer.

3.3 Transport (Aviation, Ports & Cargo, Roads & Highways, Public Transport)

Aviation

The Indonesian aviation industry is a rapidly growing one especially in last five years. The airfare has slashed significantly to boost the desire of users to shift the mode of transportation and switch over to aviation. The industry has grown at an average of 25% between 2001 to 2003.

In 2003 the sector was opened up for competition and a price war broke out. The number of operators is expected to grow by another 20% as entry of many more fleets is likely. In Indonesia, the Decree of the Minister of Communications No. 44/2002 governs the operations at the airports. Out of 187 airports, twenty are stipulated as international airports. And the government has also stipulated 20 hub airports, 17 of them are located at provincial capitals. The airports are distinguished according to their navigation facilities, namely Type A, B and C.

At present airports are being managed by the central and regional governments in Indonesia, through specialised bodies i.e. the SOE PT. Angkasa Pura I and II. Distinction has been made through the ministerial Decree [KM] No.44/2002 and the regional governments manage majority (more than 70%) of the total airports.

Ports

Indonesia has over 2,133 ports, out of which 977 are general ports and 1,156 designated as special ports. Out of the general ports, 725 are seaports. A government agency PT.Pelindo operates 111 ports. Two of the ports have the potential to become International Hubs namely Tanjung Priok and Tanjung Perak. The government is planning another port in the East Indonesia region as an International Hub, namely the port of Bitung in North Sulawesi. The government has also stipulated 25 strategic ports as the main gate for passenger and cargo flows.

The central government of Indonesia has issued several policy measures to meet the regional aspirations and to substantiate the provisions made in the Regional Autonomy Law (Law No.22/99 and PP 25/2000). Accordingly, regional governments (District/Municipality) are authorised to operate 321 ports, while 150 ports are operated by the Provincial Governments. This way, a total of 471 ports have been handed over to regional/provincial governments for operation. Anyhow, in respect of safe navigation, the responsibility still remains with the central government.

Indonesia is a maritime country with immense national seas potential. In 2001 the domestic sea transportation performed by the national fleet reached 60%. The ships that are operated by the national fleet are mostly old. The ministry, through Decree No.57/84, decided to write off ships that are older than 25 years. The decision had shocked the national navigation industry. Finally the government issued Law No.21/92 on navigation and Government Regulation No.82/99 on Public Transportation by Water, which was considered to sufficiently accommodate the national sea transportation interests.

As far as navigation and safety is concerned, a Master Plan 2020 has been compiled while taking into consideration the technical and economical aspects and local needs. With a view to bridge the development gap, especially in backward regions, a pioneering (perintis) transportation fleet has been initiated, which currently serves 49 routes with 49 ships. To sum up, the government and associated bodies continue with both the functions of regulation and service providing functions.

Roads and Highways

In comparison with other ASEAN countries Indonesia has a low density of road networks The length of road in Indonesia in 2004 was 261,379 km. Lack of finance has been amongst the major constraints to expansion of quality road network. Indonesia needs around Rp 6-8 trillion per year for road repair and maintenance. In comparison, the available government budget is estimated to be about 70% of the total requirement for road repair and maintenance.

To overcome the financial constraints the government has been promoting participation of private sector and the community, to take part in the improvement and maintenance of roads and bridges. Toll roads were introduced in Indonesia way back in 1978. Through the Government Regulation [PP] No. 4/1978, the PT. Jasa Marga (Persero) was given the authority to manage Toll Roads in Indonesia. However growth in Toll Road projects experienced stagnation after the occurrence of the economic crisis in 1997. The revival in private investments was observed by the mid of the year 2002.

Government is increasingly facilitating private sector to invest into toll road projects, for which several measures are being planned and implemented. The laws and procedures related to land acquisition and compensation are being simplified for speedy execution.

A Highway Regulating Body (BPJT) has been set up through decree No. 15/2005. The stated objectives of the BPJT include initiation of new projects and attract Foreign Investor in the sector.

As far as regulation of city transport is concerned a regulatory body called Transportation City Council (DTK) has been set up in 2005 with the stated objectives to regulate, evaluate, and improve Public Transportation in the city of Jakarta. At the moment, the focus of the agency is only on Land Transportation, where most of operators are private sector.

3.4 Energy *(Oil & Gas, Electricity)*

Oil & Gas

Indonesia is one of the largest natural gas producers in the world. In addition to technological advancement to explore the gas and coal reserve, development of an efficient transportation is crucial to ensure effective reach to markets.

The sector is governed through the law no 22/2001 concerning oil & gas and the related government regulations and ministerial decree.

In the downstream sector of oil & gas industry, the government intends to stimulate private investment, encourage open-access of oil and gas storage and transportation, stimulate natural gas utilization for energy diversification, adoption of market mechanisms through gradual elimination of subsidies, and build infrastructure for integrated gas network in the country.

To implement the stated objectives, in 2003, a regulatory body was set up in the oil & gas sector through a Presidential decree No. 53/M/2003. The regulatory body BPH Migas has an interface with consumers as well. The broad mandate of the agency is to promote efficiency and competitiveness and ensure better services to consumers.

Prior to setting up of the regulatory agency these functions were handled by Pertamina, the sole monopoly of fuel retail in Indonesia. In fact, in the upstream energy exploration, Pertamina collaborates with private corporations to form joint ventures, as it does not have required finance & technology.

The background for having BPH Migas is to follow the examples of other countries that already have Regulatory Body that works independently. The Government decree No. 22/2001 was brought in to ensure resolution and mediation of potential conflicts that may arise in the process of Deregulation and Restructuring in Oil & Gas sector.

Electricity

Traditionally the electricity industry in Indonesia has been controlled and operated by the government and services are being provided by a state owned monopoly. In 1990 the government realised that the state owned incumbent PT. PLN was unable to meet the demand which was growing at 15% on annual basis. Consequently, a policy to encourage private investment in the electricity generating sector was announced (known as IPP policy). The IPP policy was implemented in accordance with Law No. 15/1985 on electric power and the Foreign Capital Investment Law of 1967.

The government established a 'Team for the Preparation of Private Electric Power Enterprises' (PUKS). This was followed by establishment of a Negotiation Team comprising representatives of the Ministry of Finance, Directorate General of Taxes, Ministry of Mining and New Energy

Resources, Directorate General of Electricity and New Energy Resources, BKPM (The Capital Investment Co-ordination Agency) and the PT. PLN. The mandate given to the Negotiation Team was to negotiate with potential investors/bidders and subsequently report the outcome to PUKS.

In the subsequent phase, the Government established a Tender Team resulting in an award to the winner of the tender and the signing of a Power Purchase Agreement (PPA). Since the outbreak of the economic crisis in 1997 many of the IPP investors lost confidence and were demanding settlement by the government. The status of private electricity projects that initially were "deferred" according to Presidential Decree No. 39/1997 was continued according to Presidential Decree No. 15/2002. Following this, the government set up the Private Electricity Renegotiations Team (Presidential Decree 133/2002) which has been fairly successful.

Separate regulatory body has not been set up so far in the electricity sector, though the law No. 20/2002 provided for constitution of such a body. Interestingly, in 2004, this law was dismissed by High Court on the ground that the new law will put to an end the monopoly of the state owned service provider PLN and would be unconstitutional.

In June 2003, a Supervisory Body (PIP) was set up through Director General No. 114/2003 under the Department of Electricity and Energy. The stated objective of PIP is to look into the tariff related matters and bridge public interest and that of government owned service provider. PIP at the moment does not look into the quality of service related matters which are equally important.

Overall, privatisation and competition are not of the immediate priority. Instead, the focus is on enhancing operational efficiency through attaining active participation of consumer. However, widespread impression is that, PLN will not be able to retain the status of the single supplier of electricity in Indonesia and restructuring is inevitable.

3.5 Banking

Prior to occurrence of the crisis in 1997 several state owned as well private banks were operating in Indonesia.

In 1997, the Indonesia's banking sector was devastated by the major crisis. The massive real depreciation of the rupiah, combined with a sharp rise in interest rates and the refusal of creditors to roll-over loans led to the insolvency of many Indonesian businesses and banks.

As result of the crisis none of the seven state banks and the ten largest private banks could manage to remain solvent. Out of 157 private banks, 79 were closed, 9 of them were merged, and 4 were nationalized. The public almost lost confidence in the banking system. Several of them continued to experience liquidity problems and the Bank Indonesia (the central bank) supplied them with large amounts of last resort loans. During 1998 the government tried to restore confidence by issuing a blanket guarantee of all deposits and other liabilities (except equity and subordinated debt) at domestically incorporated banks. Significantly, the net cost to the government of bailing-out depositors is in the range of at least 40 per cent of annual GDP.

There onwards, most of the assets of the banking sector are being controlled by the Indonesian Bank Restructuring Agency (IBRA), which was set up to manage nationalized banks as well as the assets that the government acquired when it took over the liabilities of insolvent banks as a result of a blanket guarantee to bank creditors issued in early 1998.

The International Monetary Fund (IMF) played a key role in the revival plans. The government in consultation with IMF drew up plans for recapitalising some of the insolvent banks and merging or closing down the rest. All seven state banks had to be recapitalised. Four of them were merged to form Bank Mandiri, which became Indonesia's largest bank, with 30 per cent of all bank deposits. The three remaining state banks were recapitalised separately.

Table 7.2 Regulatory Institutional Framework in Indonesia

Sector	Enabling legislation	Regulatory Body
Telecommunications	Law No. 36/1999; Minister of Communications' Decree No.31/2003;	BRTI consisting of Telecommunications Regulatory Committee and Directorate General Posts and Telecommunications
Oil & Gas	Presidential decree No. 53/M/2003 Law No. 22/2001	BHP Migas
Electricity	Director General No. 114/2003	PIP (Supervisory Body), under Director General of LPE, Dept. of Electricity and Energy
Ports	Ministerial Decree [KM]53/2002)	Central/ Provincial/Local gov ernments
Highways	Decree No. 15/2005	Highway Regulating Body (BPJT)
City Transport	2005	Transportation City Council (DTK)
Aviation	Ministerial Decree [KM] No.44/2002	Central/Provincial governments
Drinking Water	Water Resources law (No. 7/2004) Decree of Governor of DKI Jakarta No. 54/2005	Drinking Water Regulating Body (BR), Jakarta
Banking	Central Bank Act, 23/1999	Bank Indonesia

4. Evaluation of Sectoral Regulatory Framework

4.1 Regulatory Institutional Framework and Mandate

In Indonesia, setting up specialised regulator bodies under direct control of the ministry is a common practice. This is a clear recognition by the government that regulation is a specialised task hence should be performed by specialists. However, not many regulatory bodies have been given autonomy, which would involve transfer of executive powers from the ministry to respective regulatory bodies.

The regulatory bodies in telecom, transportation, highways, and electricity perform the role of an advisor and planner to their respective Ministries. Based on their recommendations, related line ministry takes decisions. Many of the regulatory agencies are also assigned with monitoring role, however action can only be taken at the Ministry' level.

Coming to specific sectors, the 1999 Telecommunications Law is vague about the degree of autonomy enjoyed by the telecom regulator. The Director General in the Ministry of Post and Telecommunications chairs the Telecommunications Regulatory Committee.

Local transport regulatory body (DTK) has only a recommendatory role. The mandate given is to recommend to the Jakarta's Governor on appropriate type of transportation for the city.

The water sector regulatory body (BR) is given mandate to recommend measures to enhance the performance of PDAMs. The obligation and authority of Drinking Water Regulating Body of

DKI Jakarta include setting technical standards, allowing operational cost and investments, tariffs, etc. and to resolve conflicts between consumers and service providers. The body is also given powers to ensure and manage competition among service providers.

The oil & gas regulator (BPH) has been given far greater functional powers. Minister's role is that of facilitator in development of the sector. The mandate of BPH is to look after downstream activities in the sector particularly in rural areas. BPH works closely with both Executive and Legislature and is supposed to co-ordinate for effective distribution, storage, and transport of fuel. It also decides upon the charges for transmission of fuel through pipeline and to determine prices at consumer end. BPH has been given powers to resolve disputes as well. However, the body does not focus much on competition aspect rather emphasis has been on supervision.

The Bank Indonesia, responsible to frame the monetary policy (banking sector) is the only 'independent' regulator in true sense. It has been provided with the status and position as an independent state institution and freedom from interference by the Government or any other external parties. Statutes govern the Bank and it has the authority to issue policy rules and regulations, which are binding to the public at large. The Bank works for effective monetary management and sustainability of financial systems in Indonesia. In the pursuit of the objective, the Bank Indonesia formulates and implements monetary policy, regulate and ensure a smooth payment system, and regulates and supervises the national banking system. It has several regional offices across the country.

4.2 Selection Mechanism

Related Ministries appoint the regulator in the stated sectors. The selection process by and large is transparent which is a good sign.

In most cases, the government has prescribed the job requirement for selection and appointment of regulators. The term of telecom regulator is for 2 years and except the chairman all other four members are subject experts which are recruited following a competitive process.

The water regulatory agency has five members that are appointed based on merit, through following a transparent process. Announcement of vacancies is made through media and candidates have to pass through a vigorous test process prior to being appointed as regulator. However the chairperson is still nominated by the government, without following proper selection process.

In case of the local transport agency (DKT), thirteen out of fifteen members of the agency were selected through a transparent process. The government nominated other two members. To appoint oil & gas regulator (BPH) a team from University of Indonesia was appointed as Consultant to identify and recommend names of the right candidates to get appointed as regulator for the oil & gas sector. The recommendations were submitted to the parliament and the president appointed the members.

The electricity regulator (PIP) can have up to nine members and some of them represent consumers and academia. The related minister appointed 6 experts as members and they co-opt the rest three.

The selection process of regulators is transparent and in most cases experts/representative stakeholders are given a fair chance to get selected. This is happening despite of the fact that all these agencies are sub-ordinate to related ministries. Nevertheless, there are deviations from this approach as government officials continue to dominate regulatory selection in some sectors. For instance, 3 out of 5 members of highway regulatory agency (BPJT) are from related departments/ministries in the government. The rest two represent business/professional services. The related ministries are vested with the power to sack a member of regulatory agencies on grounds of misconduct.

In case of Bank Indonesia the president nominates the governor with an approval of the House of Representatives. The appointment is made for a term of five years with a provision for re-appointment. The governor nominates 4 to 7 deputy governors who are appointed by the president. Interestingly, the president has no power to dismiss a member of the Board of Governors of the Bank Indonesia. Removal is possible only in case a member voluntarily resigns, is permanently handicapped, or is proven guilty of criminal offence.

4.3 Financial Resources

For all regulatory agencies those are sub-ordinate to the related ministries, expenses are charged from the government's budget. This situation causes bureaucracy and less independence. Electricity regulatory agency (PIP) is funded through local government. In some cases there is urgent need to provide sufficient resources to regulatory agencies to allow them to carry out their functions. For instance, the transport regulator (DTK) does not have even a meeting room and cannot afford offering good salary to their staff, which has affected its performance.

The water regulator in Jakarta city, an independent body, is partly funded through charging an amount to co-operation projects. The Oil & Gas regulator is paid out of a 'control fund' to which service providers contribute.

4.4 Human Resources

Many of the regulatory agencies have not been provided with sufficient staff strength. Some of them rely on the personnel of the related ministry, on ad hoc basis. The telecom regulatory body has total five staff of which three are government officers and rest two are hired from market. Water regulatory body in Jakarta has power to recruit up to 15 staff on a contract of not more than one year.

Staff of most of these regulatory agencies is not exposed to training, by and large. Rather they rely on wisdom of the members. Consultant can be hired for specific purposes however the processes are cumbersome, as it requires approval of several related departments/agencies in the government.

Irrespective of the degree of independence a regulatory may have, the number, quality and capacity of its staff can always make a huge difference. To cite an instance from the telecom sector: The 1999 law requires a move towards cost-based interconnection charges based on the long run incremental cost model. However, the DGPT has gone on record acknowledging that it is poorly equipped to deal with issues arising in this area.

4.5 Decision-making Process

Despite most of the regulatory agencies being sub-ordinate to their related line ministries they follow proper consultation process to make decisions. Stakeholders, including public, are invited to comment and provide feedback through media. Some regulators organise public hearings as well. Though there are some exceptions such as the regulatory agency for highways that is not known to promote stakeholder consultation.

Ministers generally do not interfere in the process, though they are the final authority to take decisions. Be that as it may, certain processes are in-built that lead to politicisation of decisions. For instance, the practice of seeking Parliamentary endorsement of proposed telecom price changes inevitably involves the politicization of pricing. The government decision in January 2003 to postpone the 15% tariff increase announced only a few days previously exacerbated concerns about this process, which also affects investment decisions. In contrast, the oil & gas sector regulator is relatively independent and takes decisions independent of the government.

Box 7.1 Jakarta Model for Consumer Representation in Water Supply

In Jakarta, consumer involvement was initiated soon after the Jakarta Water Supply Regulatory Body (JWSRB) was established in November 2001. In January 2002, the JWSRB facilitated a stakeholder meeting that led to the establishment of the Consumer and Community Communication Forum (CCC Forum) which aimed to synergize the efforts of all water stakeholders in enhancing reliability of water supply in Jakarta. Since then, the Forum has become a valuable platform for information-sharing among water stakeholders, including the JWSRB, community and consumer representatives, NGOs, government officials, PAM JAYA (the local government-owned service provider), and water operators.

In parallel, the JWSRB established an in-house consumer bureau, the Community Opinion Investigation Committee (COIC), tasked with the responsibility of facilitating the functioning of the Forum, administering consumer satisfaction surveys and soliciting input from all stakeholders. In addition, in March 2003, the JWSRB facilitated the establishment of Water Supply Customer Advisory Committees (WCCs) in five municipalities of the Jakarta province. WCCs are NGO-type non-statutory organizations with the mandate to voice consumer interests. WCCs' responsibilities include: (i) monitor level of service; (ii) raise consumer complaints on service quality; (iii) facilitate communication between consumers and water utilities on service improvement; (iv) promoting access for the poor. The JWSRB retains responsibility for disseminating the information received from the WCCs and the CCCF through the media.

In case of independent banking regulator, the Bank Indonesia, the Board of Governors meets at least once every month to deliberate and decide on general policy on monetary affairs. The process is that of deliberations amongst the Board members and no public participation is provided for. The Bank Indonesia interacts with government without compromising its independence. There is a sense of realisation that despite the Bank being independence institution, a consultative co-ordination with the government is desirable for the reason that the duties of Bank Indonesia are inseparable from national economic policy as a whole. Government may request the opinion of Bank Indonesia on any economic issue. Further, the Bank Indonesia can also offer inputs and opinions to the government regarding the State Budget and other policies relating to its duties and responsibilities. A government representative may attend the Bank's Board of Governors Meeting without having a right to vote. Such harmonious

relationship is desirable between government and any other regulator and the country should consider following similar approaches.

4.6 Accountability Mechanism

Telecom regulator submits a report to the minister every quarter. There is however no provision to measure its performance vis-à-vis the objectives.

Oil & Gas regulator (BHP) reports to the President, every 6 months. No provision has been made to facilitate external evaluation. The water regulatory agency of Jakarta is supposed to submit activity report to the Governor of Jakarta and get its financial accounts audited by an independent authority, annually. An appellate body has also been provided to consider appeals against the orders of the water regulator. An interesting mention is found about the highways' authority (BJRT) given a mandate to evaluate the water regulator's (BR) performance. Such peer review arrangement is indeed a good practice that should be encouraged.

The banking sector regulator, Bank Indonesia, is obliged to share relevant information with the public. This is done through sharing information via media about evaluation of monetary policy implemented in the previous year, monetary policy plan, and monetary target for the next year. This information is also reported directly to the President and the House of Representatives. The Bank Indonesia is required by law to submit a quarterly progress report to the House of Representatives on implementation of its duties and responsibilities. The State Auditor (BPK) examines the accounts of the Bank on annual basis.

4.7 Interface with Competition Authority

As per the provisions made under Article 35 of Competition Law, the main role of the competition authority of Indonesia (KPPU) is to protect competition. However, the division of responsibility between the competition authority and sectoral regulators has not been defined clearly which might create problems in future.

For instance, the telecom regulator (BRTI) is responsible for economic and technical regulation along with competition issues. Since the BRTI is assigned to supervise competition issue in the sector, there would be potential overlap between the mandates of KPPU and BRTI.

KPPU is empowered by law to give recommendation to government, including sector regulator regarding competition issue. By disseminating competition values to the executive and legislative institution, KPPU could speed up the process of internalisation of competition values and culture in each institution. Through the "*Policy Harmonistion Mechanism*" KPPU identifies related industrial policies which are believed to effect competition in each sector. Under policy harmonisation mechanism, KPPU has initiated discussions, workshops and seminars for technical department or ministerial institution. Some policies and regulation have been reformed, while several others are being evaluated.

In sum, competition concerns are relatively new to Indonesia and the institutional structures are still evolving. There is a clear need for KPPU to develop frameworks for cooperation with sector regulators. This can be done through establishing a regular information exchange with all sector regulators so that the competition authority could be more effective in identifying anti-competitive practices and optimally use its capability.

5. Concluding Remarks

The Indonesian government recognises the regulatory function as a specialised task hence most of the sectors have been provided with specialised bodies to perform these tasks.

No consistent model is followed in Indonesia with respect to the setting up of regulatory bodies and their relation with the government. On one hand, there are agencies, which are not 'independent' and have been set up as expert bodies within the related ministries. These bodies submit their recommendations to the related ministries for a final decision. On the other hand, certain regulatory agencies have been set up as independent of the government. The Bank Indonesia is one such example. The oil & gas regulator and the water sector regulator that has been set up recently in the Jakarta City are other examples.

Interestingly, in electricity sector initially the government intended to set up such a body however later on had to withdraw the related legislation (see Box 7.2).

Box 7.2 Competition Considered Unconstitutional!

In Indonesia there was a plan to establish an independent regulatory body by law as part of a power sector reform/privatisation package. The plan was however disrupted when the law, Electricity Law No. 20/2002, was deemed "unconstitutional" and revoked by the High Court because it provided a legal basis for privatising its state-owned electricity utility. According to the Indonesian Constitution, electricity is considered a public service that should remain under government's control, so the law allowing the state utility responsible for provision of electricity services to be privatised was considered unconstitutional.

Source: http://www.palangthai.org/docs/IntlRegulators16Aug05.doc

Another feature of inconsistency comes from the nature of financial autonomy granted to regulatory bodies. For instance, the water regulator has not been given financial autonomy. In contrast, the oil & gas regulator is provided with financial autonomy. This shows inconsistency in the government's approach.

A commendable practice observed in Indonesia is that despite most of the regulatory agencies being sub-ordinate to related ministries, in many cases, process of selection of regulators is transparent and competitive. Many of these agencies follow proper consultation process and make efforts to reach out to the stakeholders.

The way forward is of imparting autonomy to existing sectoral regulatory bodies without compromising on their harmony with the government. After all meeting policy objectives is far more important and having harmonious relationship with government should not be looked as averse to regulatory independence as long it does not undermine regulator's autonomy. Adequate measures to ensure accountability also have to be incorporated.

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Chapter VIII
Regulatory Environment in Vietnam

1. Introduction

The Socialist Republic of Vietnam occupies an area of 330,991 square kilometres on the Indo-China peninsula, bordering China, Laos, Cambodia, the Gulf of Thailand, the Gulf of Tonkin, and the South China Sea.

Vietnam is a one-party communist state, governed by the Communist Party of Vietnam (CPV). All important political and socio-economic development strategies of Vietnam are outlined in the Resolutions adopted by CPV in its Congress convened every four year.

Vietnam is a densely populated, developing country that in last 30 years has had to recover from the ravages of war, loss of financial support from erstwhile Soviet Bloc, and rigidities of a centrally planned economy.

VIETNAM COUNTRY PROFILE	
Population	81.3 million***
GDP (Current US$)	35.1 billion **
Per Capita Income (Current US$)	430.0 (Atlas method)** 2,380 (at PPP)**
Land Area	331.7 thousand sq km
Life Expectancy	69.7 years**
Literacy	92.7 (of ages 15 and above)*
HDI Rank	109***

Source:
- World Development Indicators Database, World Bank, 2004
- Human Development Report, UNDP, 2003
- Economist Intelligence Unit, June 2003

(*) For the year 2001
(**) For the year 2002
(***) For the year 2003

Overcoming internal obstacles and the aftermath of wars, Vietnam has changed itself for better, largely due to Party Congress VI in 1986, which outlined the country's economic development towards a socialist-oriented market economy by gradually liberalising a lot of economic activities. As a result of Vietnam's willingness and desire to become a market economy, reforms have been prudently implemented with the aim to allow for long-term, sustainable growth.

Vietnam has achieved remarkable results in macroeconomic development during the past 15 years. The growth rate hovered around 8 percent from 1990 to 1997. Thereafter, it started to slow down due to the Asian financial crisis; then peaked again at around 7-8 percent from 2000 to 2004, making Vietnam the world's second fastest growing economy. Incidence of poverty has declined from 58 percent in 1993 to 32 percent in 2000. Vietnam's rank in human development index has improved from 121 in 1994 to 109 in 2001.

Industry has been the leading sector of Vietnam economy. During 1992 to 1997, growth of this sector was 4 to 5 percentage points higher than that of overall GDP. As a result, GDP structure changed remarkably with expansion of share of secondary sector, relative to primary sector. Share of state sector in GDP has fluctuated in the range of 38-41 percent and that of domestic private sector has steadily declined from 69 percent to 50 percent over the period 1991-2004. Foreign-invested sector has become an integral part of Vietnam's economy with increasing share in GDP from 6.3 percent in 1996 to 14 percent in 2004.

Exports have increased tenfold during past 14 years, from US$ 2 billion in 1991 to more than US$ 20 billion in 2004. Export merchandise has become more diversified with the share of primary commodities in total exports declining from about 80 percent in 1992 to 45 percent in

2004, while that of manufactures increasing from 6 percent to 32 percent. Similar to exports, import values also increased tenfold but not steadily during 1991 to 2004.

2. Evolution of Economic Policy Regime

Prior to 1986, Vietnam had been following a centrally planned, socialist economic system. Its salient feature was the policy of subsidising State-owned enterprises (SOEs), regardless of the cost; with the expectation that those enterprises would play the leading role, helping cater to the demand of whole nation.

An ambitious industrialisation plan was launched after reunification of Vietnam in 1974, which had many features of a typical centrally planned economic development model. The Five-Year Economic Plan 1976-80 determined the economy strategy, which laid emphasis on heavy industries. A capital-intensive industrial base was built up with external support, mainly from the Soviet Union. Private entrepreneurial activities happened only to a limited extent, mostly in the tertiary sector.

Capital, production inputs and labour allocated to enterprises were administratively decided. All key prices, including wages and interest rate on capital were decided by the government. The goals of enterprises were set in terms of quantitative production targets. SOEs were not made accountable for any inefficiency or commercial losses as long as the quantitative targets were achieved. The scope for initiative at the enterprise level was very limited. Foreign trade was State monopoly.

This administratively forced industrialisation policy only caused lower industrial growth and led to an inefficiently structured economy. Despite the increasing number of SOEs, and large share of public expenditure allocated to the sector, these enterprises were mostly loss-making, not able to even meet the economic targets, and produce enough to supply the whole society.

By late 1970s, Vietnam was facing a major economic crisis, with acute shortages of food, basic consumer goods, and inputs to agriculture and industry; and a growing external debt. Partial reforms, introduced from 1979 to 1982, could not address key issues of pricing; financial discipline; and reform of bureaucratic administrative structures. Public sector and trade deficits increased alarmingly. Inflation accelerated rapidly and growth began to slow from 1985. Government attempts to reduce these imbalances through currency, price and wage reforms were poorly coordinated, and fiscal imbalances and inflation became acute. Instability reached its peak in 1986, leading to social pressures for comprehensive reforms. Thus, the *Doi Moi* (reform) process was initiated in 1986. Major policies of the post-1986 period now carry the new ideas of liberalisation, modernisation and integration.

Since the beginning of the *Doi Moi* process, Vietnam has implemented a number of significant changes in its administrative structure. The SOEs were given more managerial autonomy in making decisions on production and price determination, financial investment and required to operate under profit principle. Foreign investment has been encouraged through the promulgation of new foreign investment law. Domestic trade and exchange barriers have been relaxed.

Under the 1992 Constitution, the Government is charged with the supervision of public sector agencies and overall management of the economy. State intervention is henceforth confined to its regulatory role of the market. Consumers' and producers' rights are recognised and

encouraged. Competition is no longer considered an 'alien' and 'capitalistic' concept, but upheld as a major driver for economic development. The adverse impacts of Asian financial crisis on the economy and challenges faced by Vietnam in ongoing international economic integration have further pushed up economic reforms in recent years.

The major structural reforms that have been undertaken are summarised below:

Equitisation of state-owned enterprises: Substantive SOE reforms occurred in late 1980s through increasing managerial autonomy, imposing a hard budget constraint, and rationalising or consolidating the SOE sector. A Five -Year SOE Reform Plan was adopted by the government in 2001. Two key components of the program are: to diversify, divest, and even liquidate small and medium sized and non-strategic SOEs; and to restructure retained large SOEs for improving their efficiency and competitiveness.

Attracting private participation: In year 2000, the new Enterprise Law was passed to ease market entry of the domestic private sector. The removal/modification of business licenses in large number of sub-sectors significantly reduced business registration costs and shortened the approval process. This gave a big boost to registration of private domestic enterprises.

Improving the environment for FDI: The amended Foreign Direct Investment Law promulgated in 2000 has improved the environment for attracting FDI by streamlining licensing and administrative procedures for foreign enterprises.

Trade reform: Trade liberalisation process started in 1998. Trade monopoly by the state was abolished and other enterprises are allowed to participate in trading activities. Vietnam has signed bilateral trade agreements with several countries. Vietnam's efforts now focus on making domestic laws in line with WTO practices and undertaking bilateral negotiations with the objective to be a WTO member.

3. Evolution of Sectoral Regulation

In the central planning period, state-intervention was spread over almost all the industries. At present, state-intervention is found in some industries, which are primarily the ones with natural monopoly characteristics or crucial for economic development. Examples are: electricity, telecommunication, banking, insurance, transportation, and oil and gas. In most of these industries, the competent ministries play the role of regulators; in particular the Ministry of Post and Telematics, Ministry of Industry, and Ministry of Transportation. The only exception is the State Bank of Vietnam, which regulates the banking sector.

At present, government policy emphasises on separating commercial operations from the ministries; in other words, ministries mainly undertake state management functions, which include policy and regulation functions. The question of separating policy and regulation has been raised recently, especially during the drafting of the Competition Law. However, given the administration structure and limitation of resources, creation of regulators, independent from the ministries are not found feasible in the short-term. There are some legislations that envisage creation of independent regulators. For example, the Electricity Law stipulates the establishment of electricity regulator. However, even this has been set up under the relevant line ministry. Therefore, establishment of independent regulators, outside of line ministries is not the approach followed in Vietnam.

Below we summarise the nature of sectoral regulation in select sectors: communications, electricity, transportation, and banking.

3.1 Communications

Post and telecommunication activities in Vietnam were, for a long time, regulated and operated by the same agency. Until 1992, Vietnam Post and Telecommunications (VNPT) performed the roles of both regulator and operator in telecom sector. In October 1992, government established the Department General of Post and Telecommunications (DGPT) as sector administrator with the purpose of separating policy and regulatory functions from the network operation/service provision function. VNPT was made responsible for commercial activities, but it continued to be under the direct control of DGPT, thus reconfirming the model of regulation and operation function being vested in same agency.

In 1995, in the face of increasing domestic demand and changes in key sectors of Vietnamese economy, government started to implement a pro-competitive policy in telecommunications. This included the decision to separate sector's management and commercial functions. Accordingly, policy and regulatory functions of DGPT were formally split off from operation functions of VNPT. In addition, monopoly of VNPT as network provider was brought to an end by the licensing of two domestic telecommunication companies.

Government's policy of fostering competition in the telecommunications sector is reflected in the following two key documents that govern the telecommunications sector:

- Post and Telecommunications Development Strategy issued by the Government in 2001. The strategy identifies objectives and measures to develop telecom market in Vietnam. It sets general policy orientation: transformation from monopolistic to competitive telecom market, while maintaining leading role of state-owned enterprises. The approach of liberalisation is to allow qualified domestic enterprises, mainly SOEs, to provide basic as well as value added services, and then open up the telecom market to foreign players in accordance with international commitments.
- Ordinance on Post and Telecommunications issued by the Standing Committee of the National Assembly in 2002. The ordinance encourages enterprises from all economic sectors to engage in telecom activities in a fair, transparent, and competitive environment. It determines state management, including telecom policy and regulation activities, over telecommunication sector and roles of different authorities in implementing state management.

Besides, the Government has issued a series of decrees detailing regulations in P&T Ordinance, including a decree in November 2002 on upgrading DGPT to ministry status, which is now the Ministry of Post and Telematics (MPT). As a result, the regulator (i.e. MPT) has more power to make policy and to develop legislation and regulations over the fields of posts, telecommunications and IT. MPT now performs function of policy-making and regulation while VNPT is the incumbent operator providing both telecom networks and services. However, MPT is still involved in the management of VNPT through its role as representative of state capital in VNPT, especially through senior personnel appointments.

Vietnam's legal framework for telecom industry has improved significantly, becoming more open and liberal, especially following the establishment of MPT in November 2002. This reflects government's commitment to ensure a competitive and dynamic telecom sector. In some opinions, this has been done to attract more foreign investment and also to facilitate signing more bilateral trade treaties as the country edges closer towards WTO membership.

Since its establishment, the MPT has facilitated remarkable progress in telecom sector. It has changed the monopoly environment into business competition in telecom and IT services. MPT has, so far, licensed six enterprises to provide network infrastructure. There are 13 companies permitted to provide telecom and internet services. Six licenses have been issued to mobile phone operators, including Mobifone and Vinaphone, affiliated to the state-owned VNPT; Viettel, a military-run company; Sfone, a business cooperation contract between South Korea's SK Telecom and state-owned Saigon Postel; VP Telecom, a unit of state-owned Electricity of Vietnam; and Hanoi Telecom, a joint venture between a local firm and Hong Kong's Hutchison Whampoa.

The monopoly of state corporations has gradually given way to competition. One notable example is that VNPT is no longer the only provider of international gateways. Private and foreign invested enterprises are now able to take part in supply of post and telecom services. Though foreign telecom enterprises are allowed to provide telecom services in Vietnam's territory only if they have business contracts or commercial agreements with Vietnamese enterprises.

Telecommunications is amongst the fastest growing industries in Vietnam. Vietnam's telecom sector has been rated by the International Telecommunication Union as the second fastest-growing telecom market in the world after China. From a time when its teledensity was barely one percent 10 years ago, it is now over 10 percent with an annual network growth of over 25 percent per year in the same period. The number of main telephone lines grew from 0.4 per 100 inhabitants in 1995 to 8 in 2003, at a cumulative average growth rate (CAGR) of 45 percent, which is one of the highest in the world. Number of mobile phones in use is set to surpass number of landlines in the near future. Mobile phone market grew 63 percent in 2004, which is largely attributed to mobile phone charge reductions, facilitated by progressive policies and regulations of the MPT. Telecom enterprises in Vietnam are obliged to contribute to public telecom services, which consists of compulsory services[49] and universal services[50].

3.2 Electricity

The initial reform of Vietnam's power sector started in late 1994 and focused on reorganisation and consolidation. Under the old centrally planned system, Vietnam's power sector was run by three regional state-owned Power Companies, which were extensions of the former Ministry of Energy, responding mainly to administrative needs rather than business requirements. In an attempt to reduce direct intervention of line ministry in daily operations of power companies, build up a corporate culture within the sector to replace old bureaucratic atmosphere, and develop large and internationally competitiveness business unit, Electricity of Vietnam (EVN) was established in 1995 through merger of all three regional monopoly power companies. In the re-organised power sector, EVN is business-oriented with profit being the primary motivation for its operations and regulated by the Ministry of Industry (MOI). The MOI is responsible for approving all pricing policies and capital investment decisions, as well as selecting board of directors of EVN and its CEO.

Private participation was also encouraged in the power sector in the form of independent power producers (IPPs). The IPPs are allowed to generate and sell electricity directly to customers in designated industrial zones at prices negotiated between the IPPs and customers. The IPPs can also sell their excess electricity to the national grid.

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[49] Compulsory services are services provided on the basis of state's requirements for economic and social development, defence and securities

[50] Universal services are defined as telecom services provided to every one under conditions, prices, and quality determined by relevant authorities.

The Development Strategy for the Electricity Sector framed in October 2004 states general principles for the development of a competitive electricity market. Accordingly, the country is striving towards a gradual formation of a domestic competitive power market. Vietnam has framed a three-phase plan to introduce competitive electricity market. In the first phase, competition will be introduced in the generation stage where electricity generators will be competing in selling their products to a single buyer, Electricity of Vietnam (EVN). The wholesale market will become competitive in the second phase with the traders and major consumers being allowed to buy electricity in the market and, therefore, able to select their suppliers. The retail market will be set up in the third phase where electricity generators, distributors, and retailers all compete to sell electricity to consumers and, on the other side, all consumers, including ones buying electricity directly from the transmission and distribution grids, are free to choose the sellers. This market scenario is considered as the highest level of competitive electricity market in Vietnam. The implementation of the three-phase process is expected to take about 30 years.

In accordance with the Strategy, the National Assembly passed the Electricity law governing activity in the electricity sector, effective July 2005. The Law governs all entities involved in electricity activities. The Law specifies state management functions in electricity sector and roles of different authorities in undertaking these functions. The Government determines and issues major policies and legal regulations. Ministry of Industry (MOI) plays the role of state management agency. The Electricity Law provides for the establishment of an electricity regulator. Accordingly, the Electricity Regulatory Authority of Vietnam (ERAV) was established in November 2005, as a unit under the Ministry of Industry with the purpose of assisting the Minister in undertaking regulatory activities in the electricity sector.

3.3 Transportation

Vietnam gives high priorities for development of infrastructure in road, railways, inland waterway and maritime. It encourages organisations and individuals, both Vietnamese and foreign, to invest in transportation infrastructure.

The laws on transportation provide for the role of different state bodies in land transportation (highways and railways) and water transportation (inland and maritime). The Ministry of Transportation (MoT) undertakes state management functions in land and water transportation. The Ministry has established separate agencies within its organisational structure to implement state management functions, including regulation functions in specific transportation sub-sectors. These are Vietnam Road Administration; Vietnam Railway Administration; Vietnam Inland Waterway Administration, and Vietnam National Maritime Bureau.

The civil aviation law governs the civil aviation sector. The law determines the roles played by different agencies in undertaking state management functions of civil aviation. The government oversees the aviation sector nation-wide. The Civil Aviation Administration of Vietnam (CAAV) is responsible for state management function in the aviation sector and reports to the Ministry of Transport.

Vietnam Railways, a state general corporation, is the monopolist service provider in railways. It manages tracks and provides transport services, and has four main companies to carry out its activities. Railways face competition with other modes of transportation, such as road and waterways. In road transportation, competition is quite high in passenger transportation and weak in freight transportation. Competition in inland waterway is quite high with many enterprises participating in inland waterway activities, while maritime transportation is dominated

by the Vietnam National Shipping Lines (Vinalines), a state corporation. In the aviation sector, there are only two carriers: Vietnam Airline and Pacific Airline. Both are units of the Vietnam Airlines Corporation. The scale of Pacific Airline is very small as compared with that of Vietnam Airline, which monopolises domestic flights.

3.4 Banking

The State Bank of Vietnam (SBV) was established in 1951. Until 1988, SBV played the role of a Central Bank, setting broad monetary policies and regulations, and the role of a commercial bank, carrying financial activities of a regular retail bank.

Reforms in banking sector started in 1988 with the setting up of a two-tier system, separating commercial banking from central banking and creating four state-owned commercial banks (SOCBs) and the State Bank of Vietnam (SBV) as the central bank to assume enhanced regulatory role. In 1990, entry into the banking system was liberalised and all economic sectors allowed to participate in banking business.

Despite fundamental structural changes initiated in 1988, resource mobilization and allocation by the banking sector were still limited. At the same time, banking sector was structurally fragile. Its composition was dominated by State-owned commercial banks (SOCBs) and its credits by State-owned enterprises (SOEs). Lack of competition, non-price based operation, as well as lax banking policies and regulations impaired the development of the banking sector.

To rectify the problems, the Law on the State Bank of Viet Nam and the Law on Credit Institutions became effective in October 1998, and several related decrees were introduced. The Law on State Bank of Vietnam provides more autonomy to SBV in carrying out banking regulation and supervision. The law on credit institutions has provisions to ensure safety of the activities of deposit- and non-deposit-taking institutions.

The State Bank of Vietnam (SBV) has promulgated a number of provisions for the establishment of financial institutions and enhancement of deposit-taking, loans, and portfolio investment operations. These measures have contributed to directing credits to the most productive sectors, and enhancing the soundness of credit institutions.

Like many other regulated sectors in Vietnam, gradual approach has been applied in reforming the banking sector. Although non-state sector is allowed to participate in banking business, restrictions in terms of capital structure, business forms, and scope of operation are used to control their operations. With development of the economy and pressures from economic integration, these restrictions are being gradually relaxed.

Vietnam has now moved to a diversified system in which state-owned, joint-stock, joint-venture and foreign banks provide services to a broader customer base. At the end of 2004, aside from the four SOCBs, Vietnam's banking sector had expanded to include 46 joint-stock banks, 5 joint-venture banks, and 26 branches of foreign banks, and more than 900 small people credit funds. However, the four main state-owned commercial banks - the Bank for Investment and Development of Vietnam (BIDV), the Bank for Foreign Trade of Vietnam (Vietcombank), the Industrial and Commercial Bank of Vietnam (Vietincombank) and the Bank for Agriculture and Rural Development (VBARD) – still account for 70-80 of all lending activity. Domestic private banks have weak capital capacity as compared with the SOCBs. Foreign banks have large amount of capital as compared with domestic ones, but find hard to garner large market shares because of restrictions on lending as well as the state intention to maintain the leading role of SOCBs.

Table 8.1 Regulatory Institutional Framework in Vietnam

Sector	Enabling legislation	Regulatory Body	Other Agency
Telecommunications	Post and Telecom Ordinance 2002; Decree issued in 2002	Ministry of Post and Telematics	
Electricity	Electricity Law 2005	Electricity Regulatory Authority of Vietnam (ERAV)	Ministry of Industry, as state management agency; ERAV set up under Ministry to assist it in regulatory activities
Road Transport	Laws on Transportation; Vietnam Civil Aviation Law	Vietnam Road Administration	Ministry of Transportation, as state management agency; all these agencies report to the Ministry
Railways		Vietnam Railway Administration	
Seaports and Water Transport		Vietnam Inland Waterway Administration; Vietnam Maritime Bureau	
Civil Aviation		Civil Aviation Administration of Vietnam	
Banking	The Law on State Bank of Vietnam 1998	State Bank of Vietnam	

4. Evaluation of Sectoral Regulatory Framework

4.1 Functioning of Ministries Performing Regulatory Functions

The organizational structure of a ministry consists of departments that assist Minister in performing state management functions, and professional units which typically conduct research. Some ministries establish bureaus or general departments, while some also have business units under their management.

According to the Law on Government Organisation passed in December 2001, the Prime Minister has the power to submit proposal for appointments or dismissal of ministers or minister level officials to the National Assembly for approval. Within the ministry, minister has the power to appoint or dismiss department directors, vice-directors and equivalent officials.

All ministries are required to submit their annual budget estimates to the Government. The ministries are allowed to keep certain percentage of fees they collect, mainly through licensing procedures, though these fees account for small part of ministries' financial resources.

Ministries are responsible for managing personnel structure and payroll, and other regulations and policies on remuneration, award and punishment applicable to State cadres and staff within the management of a ministry. They also provide/facilitate professional training and refresher courses to staff in related fields.

Ministers participate in the decision formulation regarding issues that the Government submits to the National Assembly for approval. Ministries are subject to examination by the Prime Minister on works undertaken. On the request of the National Assembly Standing Committee, the Nationality Council or the National Assembly's Committees, ministers provide necessary information. Ministers are also required to respond to the questions raised by the National Assembly regarding matters in the branches or domains under their ministries' State management. These accountability regulations are applied to all ministries, including the ones covered in this paper.

4.1.1 Telecommunications

The key functions and responsibilities of the Ministry of Post and Telematics (MPT) can be put under three different groupings:

- Policy-making functions, which involves submitting to the government drafts of laws, ordinance and other legal regulations; development strategies, master plans, etc
- Regulation functions, which involves licensing; tariff regulation; managing interconnection of telecom networks; allocation of radio frequencies; ensuring standards and quality of telecom networks and services; redressal of complaints, and punishing for violations of telecom laws
- State representative functions i.e. representing government in enterprises where State capital has been invested and performing duties and enjoying rights in such enterprises.

In the context of licensing, MPT evaluates applications for licenses and submits them to the Prime Minister for a final decision. It also solicits opinions of relevant ministries and government branches, where required, and submits responses so received to Prime Minister. After receiving Prime Minister's approvals, MPT grants licenses to enterprises. The licensing regime has been liberalised to a certain extent, but the terms and conditions to obtain a telecom license are not sufficiently transparent, as are the licensing procedures. This provides for too much discretion, and leads to non-transparent decision making.

The P&T Ordinance mandates access to essential facilities and provides for an open interconnection regime. All telecom network operators are entitled to interconnect with all other telecom networks on fair and reasonable conditions. Particular obligations are placed on parties who are in a dominant position. These obligations provide for good faith negotiations and prohibit refusal to interconnect.

Telecom enterprises, holding essential means, formulate model interconnection agreements with transparent and non-discriminatory conditions and submit them to MPT for approval. After approval, these model interconnection agreements are made public for uniform application to all telecom enterprises. In case no agreement is reached within the stipulated time or conflicts arise during implementation of the agreement, MPT holds consultative meetings with the parties to arrive at a mutually acceptable agreement. If no agreement is reached, MPT takes an appropriate decision. However, connection between telecom networks, in particular with VNPT, the state-owned incumbent is a major problem. There are opinions that VNPT is not cooperative in this issue. (see Box 8.1).

Box 8.1 Interconnection with VNPT: An area of concern

VNPT's network is used by the majority of users and interconnection to it is vital for competition to survive. Under current regulations, VNPT, as country's largest telecom service provider and dominant market holder, is required to ensure there is communications connection between the corporation and other operators. However, VNPT frequently denies adequate

interconnection by either providing insufficient resources, delaying the process and simply overcharging for a facility so critical to the competitors' business.

In one such instance involving VNPT and Viettel (incidentally both are SOEs!), the interconnection dispute reached such high proportions that finally the Prime Minister had to intervene to settle the matter.

In the dispute, VNPT seemed to be using its dominance to check competitive threat from Viettel. According to the military-run Viettel, the two companies had struck an interconnection deal in December 2004. However, VNPT provided less than 50 percent of connections, and as Viettel's mobile phone subscription rocketed, lack of adequate interconnection triggered a wave of complaints by Viettel customer about service quality, affecting its market. In a bid to save the company from financial crisis, the Ministry of Defense, Viettel Mobile's owner, wrote an official letter to Prime Minister, accusing VNPT of not providing adequate connection. In the past also similar problem arose in connection with Sfone, the country's first CDMA, which was resolved by MPT.

In July 2005, the government directed VNPT to ensure smooth connections for competing mobile networks like Viettel in line with prevailing regulations. Later, the government asked MPT to cooperate with other relevant ministries to draft a plan to set up an agency to monitor telecoms connections. Rival operators of VNPT have also urged MPT to establish an agency with legal capacity to supervise connections between providers.

The P&T Ordinance prescribes a threshold for presumed market dominance, which is 30 percent market share in respect of one type of service in a licensed geographical area. Market dominance attracts specific restrictions, for instance, a requirement for separate accounting and supervision and surveillance of market share, tariffs, etc.

Tariffs remain subject to stringent regulation. There are five types of tariffs set out in the P&T Ordinance. Different rules for tariff determination apply to these five categories (Table 8.2).

Table 8.2 Tariff Regulation Regime for Telecommunications in Vietnam

Type of Service	Deciding agency and rule for tariff determination
Charges for important telecom services that affect various sectors and socio-economic development	Prime Minister has full discretion to determine tariffs for this service category; MPT consults Ministry of Finance before submitting relevant documents to the Prime Minister for approval of tariffs
Charges for services provided for the purpose of community service	MPT has authority to determine tariffs for both these categories of service. The basic principle is that retail tariffs should be determined on a cost basis, considering contributions that may be required for universal service and development goals.
Charges for services provided by enterprises in dominant positions in relevant market	
Interconnection charges	Interconnection charge are regulated by MPT based on cost and after adding contribution for community service obligations
Charges for all other services not covered in the categories above	Enterprises may decide their own tariffs for all other services

Before 1995, only VNPT was authorised to operate in Viet Nam. Though, VNPT's monopoly ended in 1995, the race to cut mobile phone charges began only in 2003 largely due to the entry of new operators, and facilitative actions taken by MPT.

July 2003 heralded new developments: Internet telephony was formally allowed, enabling operators to offer overseas calls at throw away prices. Further, Viet Nam's mobile phone network monopoly ended with the entry of Sfone. Before this, there was no competition as both the mobile phone operators, MobiFone and Vinaphone, are affiliated with VNPT.

Prior to this, in April 2003, MPT provided a floor and a ceiling allowing telecom operators to charge prices in that range. MPT continued to manage firms with more than 30 percent market share, which effectively implied more control over VNPT's operations. Further, in November the same year, government did away with price bands for all telecom services, allowing operators complete freedom to fix tariffs. This freedom, however, is applicable for operators whose market share is under 30 percent. Hence, MPT regulates tariffs of those operators with dominant market share, whereas other operators are allowed to set their own tariffs.

Given this freedom, other operators took on call charge reductions as a means of competing and launched large-scale promotion campaigns and cut charges to attract more customers. Tariffs slipped further with the emergence of Viettel, owned by Ministry of Defense, in October 2004, which has been offering lowest telecom charges in a bid to compete with other three competitors.

Before the arrival of competing operators, VNPT claimed the reason for its high charges was the need to repay its bank loans. Now, by constantly seeking MPT's approval in offering various incentives to its customers, the giant appears to be acting contrary to its previous explanation, and is more than a touch concerned about competition. Viet Nam's telecom battle peaked in September 2005 with simultaneous price-cutting announcements from rivals Vinaphone (largest mobile carrier) and Viettel (third largest mobile carrier).

Government's goal is that newly-licensed operators maintain a 25-30 percent of market share. However, until January 2005 these operators held less than 10 percent of market share. An important difficulty facing new operators is connecting to VNPT's nationwide network (see Box 8.1). Related to this is the obstacle of lengthy network deployment time. New operators expect to gain a firm foothold in the market once they finish preparations on their networks in 2005.

Another difficulty faced by new operators is that tariffs in Vietnam are still cross-subsidized and not aligned to costs. Due to this, VNPT's competitors face considerable challenges when they seek to match its cross-subsidised tariffs. Low local rates and very high long distance rates, which are not aligned to the cost of providing services, make it virtually impossible for VNPT's competitors to compete effectively. Vietnam is yet to undertake full rate rebalancing to remove these anomalies. This, therefore, remains a long-term risk to fair competition.

Consumer Interest

To protect consumers' interest, MPT makes service providers comply with a set of Quality of Service (QoS) criteria. Any enterprise, which fails to comply with these criteria, faces the prospect of being shutdown. To cite an instance, in May 2004, MPT had asked VNPT to pull its socks up following repeated breakdowns of its two mobile services, Vinaphone and MobiFone. The two largest mobile operators experienced network congestion after demand skyrocketed following tariff cuts. This led to frequent breakdowns in service causing inconvenience to customers, making the MPT issue necessary direction to VNPT.

Is MPT impartial and independent?

Viet Nam has separated the regulator (MPT) from basic telecommunications suppliers in a formal way. However, the important question is whether MPT can be considered impartial about the interests of VNPT and other State-owned telecommunications suppliers.

According to the International Telecommunications Union (ITU), regulator's independence include the following three dimensions:

(1) Independence from market players:
(2) Independence from political influence or control
(3) Independence based on credibility and capabilities

As the objectives and functions of regulators vary from country to country, so too does the degree of regulatory responsibility differ, based on government structures and political systems. In Vietnam, the National Assembly is the ultimate decision-making authority. It formulates laws and ordinances. The Government issues decrees, directives and steers the direction of telecommunications development. MPT, the regulator, implements policies approved by the National Assembly and the Government, develops regulation, oversees the operation of telecom networks, and settles disputes. However, the one party system in Vietnam has a large influence on the telecommunications regulatory structure.

In practice, Party organs have authority superior to government and administrative organs, and representatives of the Party are woven into the structures of all major government, administrative, and commercial entities. Thus, the independence from political influence and control (the second dimension described above) is institutionally not possible in Vietnam at this time. What is institutionally and politically possible thus far in Vietnam is the first and third dimensions of independence, that is independence from market players and independence based on credibility and capabilities.

Although MPT has been created independent of the dominant VNPT, there is still widespread concern regarding the apparent ability of VNPT to influence MPT in the governance of the sector. Questions regarding the impartiality and independence of MPT typically focus on issues such as the inability - or perhaps unwillingness - to investigate and act on alleged anti-competitive practices by VNPT and its subsidiaries, or the various problems experienced by suppliers trying to interconnect to VNPT's network. More fundamentally, concerns focus on the continuing close relationship between MPT and VNPT. There is substantial rotation of personnel amongst MPT and VNPT, and even an overlap of responsibilities; for example, the head of MPT is also on the board of VNPT.

Be that as it may, the MPT has taken a number of initiatives to improve access for newcomers and promote competition in the sector. *First*, MPT allowed VOIP services, which helped new telecom companies to quickly obtain considerable revenue streams with low initial capital investments. *Second*, whilst regulating the tariff of VNPT, MPT has allowed other companies the freedom to set their own tariffs for most of their services. *Third*, MPT has deliberately set differential interconnection fees between the mobile system of VNPT and those outside VNPT. Previously, a call from outside the VNPT mobile network to a phone on the VNPT mobile network had to pay an interconnection fee of 820 dong/minute, while a call from a VNPT network to a non-VNPT network had to pay an interconnection fee of 900 dong/minute. Since April 2004, the former was reduced to 765 dong/minute. This pricing asymmetry is provided with the rationale that new telecom companies have to bear huge initial capital outlays and need a lead time for making break-even, and hence need a lower interconnection fee, which

constitutes a substantial part of their costs. *Fourth*, with the introduction of S-Fone and Viettel Mobile and their aggressive marketing and promotion schemes, especially in terms of lower tariffs, VNPT mobile networks have also requested MPT to accept price cuts similar to those offered by S-Fone, which would undermine the competitive positions of S-Fone and Viettel Mobile. However, the price cuts requested by VNPT were delayed by MPT, with the reasoning that new services such as S-Fone need to be protected and supported for some period of time for development.

MPT is nevertheless handicapped by a general lack of skilled personal and institutional capability necessary to fulfill its crucial role as the telecom regulator. Another problem is its lack of capability to mediate between telecom companies in cases of disagreement and to enforce its decisions. One example is its indecisiveness in forcing VNPT to allow S-Fone direct interconnection. The issue remained unresolved for quite some time, despite MPT requesting VNPT to find a solution for S-Fone.

Another aspect of being an independent regulator is the process and extent of public consultation. International good practices are that, in term of procedures, broad consultation is undertaken with the public and industry to ensure transparent and impartial decisions and licensing. In Vietnam, however, most of the decisions are made internally by MPT or by discussion with other Government agencies, with little consultation with the public and industry.

MPT, as both a policy making and a regulatory body, has taken some steps to make itself a credible agency. However, it is desirable to make MPT more impartial and transparent in its regulatory processes. MPT should enable wider public participation and consultation for the issuance of new policy, laws and regulations. It should pay more attention and effort to the drafting and early issuance of regulations which are essential for enhancing competition, especially those that will guide the implementation of the Ordinance and Decree. MPT should enhance the capability and expertise of its staff on key issues that affect competition, notably pricing and the technical aspects of interconnection, so that they can intervene and arbitrate quickly when disputes arise.

4.1.2 Transportation

The Ministry of Transport is in charge of state management of land transport (highways, railways) and water transport (inland waterway and maritime). Its main functions and responsibilities are:

- Policy-making, which includes, submitting to the government national master plan, draft laws and by-laws, policies on transport development and management
- Regulation, which includes, framing and enforcing standards; classifying categories of seaports, road network, railways, inland waterways; approve works, transport construction projects, etc.; issue certificates and licenses of operation regarding traffic; enforcement of laws, regulations and other policies

Railways

The Vietnam's track network is classified into three types: (i) national tracks for the regional, and national demand; (ii) urban tracks for rail traffic within the urban or its surrounding area; (iii) specific tracks for transportation needs of particular organisations.

The Ministry of Transportation (MT) is empowered to announce national, urban, and specific tracks connected to the national network and to open or close the segments of national network. The provincial people committees announce the urban tracks managed by local governments.

Ministries and local governments also announce the specific tracks not being connected to the national network and under their management. The Minister of transport issues technical procedures for railway stations and makes decisions on opening or closing of stations.

For being used in transportation, the rail vehicles have to be registered and certified about quality, technical safety, and environment protection. The Ministry of Transportation prepares and issues documents on these issues. The Ministry of Transportation is responsible for licensing railway operations. Furthermore, the Ministry on an annual, quarter and seasonal basis establishes rail transportation schedule, which is important for operations of individual train journey. The Government regulates the fees and fee collection methods and rents for the rail infrastructure invested by the state. Fees and rent for non-state invested infrastructure are determined by the investors.

Road transportation

The Ministry of Transport is responsible for the national roads and the provincial people committees for provincial and urban roads, the investors for the specific roads. The Ministry of Transport stipulates and regulates types, quality standards, and technical safety for the vehicles, and the Ministry of Police regulates and implements the works of registration of vehicles. The Ministry of transport prepares and regulates transportation schedule for public passenger transportation.

Inland waterway transportation

The inland waterway network is classified into three types: national, local and special levels. MT manages and maintains the national inland waterways, the provincial people committees (PPCs) for local ones and organisations and individuals for their assigned ones. MT classifies and announces the different types of inland waterways. Minister of transport issues regulations on vehicle registration and the provincial people committees carry out the registration in accordance to the Ministry of Transport's regulations. The port authorities are agencies implementing the state management functions at the ports and Minister of transport regulates organizational structure, operations and scope of the port authorities.

Maritime transport

Vietnamese fleets are given priority in domestic transportation of goods and passengers. The foreign fleet is also allowed to provide domestic transportation in certain cases when Vietnamese fleet have no capacity to provide transport services. Minister of transport and Directors of seaports make decisions on allowing the foreign feet to do domestic transportation. Like other transport vehicles, the ships need registering and meet the safety, security, and environment protection standards before operation. The Ministry of Transport issues the standards on maritime safety, securities and environment protection and regulates the registration of ships in Vietnam. The Registrar Administration, which is a body under the Ministry of Transport, implements the registration of the ships. The Government regulates conditions and procedures to close or open the sea ports, manage sea lines and maritime activities at the sea ports. Minister of transport, in consultation with the provincial people committees, announce the open or close of sea ports and the supervision areas of port authorities.

Civil Aviation

The aviation industry in Vietnam comes under the principal jurisdiction and management of the Civil Aviation Administration of Vietnam (CAAV), which, as a government agency, used to report directly to the Prime Minister's Office. In October, 2002, CAAV was shifted under the umbrella of the Ministry of Transport (MoT).

In terms of its organisation, CAAV consists of a management board (headed by one director general and two deputy director generals) and ten administrative and operational departments overseeing a number of business entities in the industry. Of these, Vietnam Air Traffic Management Services (VATM), a state owned enterprise under the supervision of CAAV, is responsible for managing and controlling the air traffic, and providing air traffic services as well as other support services to all civil aircraft operating in the Vietnam.

During the 1990s, the civil aviation sector underwent a number of changes in management. Vietnam Airlines and many other businesses were put under the authority of the CAAV. In May 1995, Vietnam Airlines Corporations was established, bringing together several service companies. The corporation is run by a seven-seat management board whose members are appointed by the Prime Minister. Though directly reporting to the Prime Minister's office, the corporation works closely with CAAV under MoT and has to comply with the strategies, policies, regulations and procedures in the aviation sector enacted by CAAV and MoT. The Corporation includes three air transport businesses: Vietnam Airlines, Vietnam Air Service Company, and Pacific Airlines.

Table 8.3 Features of Conventional Form of Regulatory Functioning in Vietnam

Sector	Key features of regulatory functioning under line ministry
Telecommunications	• Entry of new players and competition facilitated by progressive actions of the MPT • Asymmetric regulation to check practices of dominant players • Issuing of licenses not sufficiently transparent • Interconnection with VNPT (the state-owned incumbent) an area of concern • Consultation with public and industry in regulatory process largely absent, affecting MPT's credibility • MPT handicapped by lack of skilled personnel
Transportation	• Ministry of Transport responsible for state management in land and water transportation • MoT determines schedule in rail and road transportation • Civil Aviation Administration of Vietnam (within the Ministry of Transport) responsible for civil aviation

4.2 Working of Specialised Regulatory Agencies

4.2.1 State Bank of Vietnam

The management board of the SBV is chaired by it's governor, who is a Governmental member. Other members of the board are from other government ministries or are appointed by the Prime Minister. Within the SBV's structure, the Banking Inspection Department is the specialised inspection agency in the banking sector. The department inspects the operation of credit institutions and banking activities of other institutions in order to ensure the safety of the banking system as a whole and protect the legitimate rights and interests of deposit customers. The Prime Minister appoints the General Inspection Chief on the basis of governor's suggestion.

The National Assembly decides and supervises the implementation of the national monetary policy. The Government formulates projects for the national monetary policy to submit to the National Assembly for decision. In order to do so, the Government has established a National Advisory Council to help it in making decision on monetary policy issues. The Council consists

of Deputy Prime Minister (as its Chair), State Bank Governor as the standing member, representatives from Ministry of Finance, Ministry of Planning and Investment, other relevant ministries and agencies, and banking experts. SBV is responsible for the implementation of national monetary policy. It specifies and announces prime and refinancing interest rates.

SBV's incomes and expenses are made in accordance with regulations of the State Budget Law. The Government specifies stipulations on peculiar financial incomes and expenses suited to SBV's professional operations. The difference between SBV's incomes and expenses is primarily from revenues from banking operations after excluding operating expenses and reserves. SBV deducts part of the difference between incomes and expenses to form funds to serve the national monetary policy in accordance with Governmental regulations, and the remainder is contributed to the State Budget.

Based on the Law on State Bank and the Law on Credit Institutions, the regulatory functions of SBV in banking activities are as follows:

- Planning and developing strategies and policies of credit institution system;
- Drafting the laws, ordinances, and other regulatory documents;
- Granting and withdrawing establishment and operation licenses of credit institutions; granting and withdrawing banking licenses of other institutions;
- Making decisions on dissolution, separation, incorporation and merger of credit institutions;
- Examining and inspecting, operation of credit institutions and banking activities of other institutions;
- Applying measures to prevent violations to the banking laws;
- Collecting, processing, providing information and forecasts on monetary and capital markets.

SBV supervises the operations of banks and non-bank financial institutions (NBFIs). For this, it provides both off-site and on-site inspection, sets prudential regulations on lending, and stipulates minimum capital requirements. The approach is more in the nature of a rigorous internal audit rather than a bank examination. SBV has developed an off-site surveillance system. Monthly information submitted by banks are automated and used to produce standard reports. Based on the evaluation of the off-site reports, a rating ranging from "A" (best) to "C" (worst or problem bank) is assigned, and banks rated "C" may have their licenses withdrawn.

The law on SBV sought to provide the central bank more autonomy in the conduct of monetary policy and the banking regulation and supervision system. However, contrary to its initial intention, these functions remain subservient to Government intervention. Because of lax coordination with other government agencies such as Ministry of Finance and Ministry of Planning and Implementation in carrying out economic policies, the autonomy of SBV is limited. In particular, the Government continues to interfere with the credit allocation mechanism to serve the multiple socioeconomic objectives of the economy.

The Government normally selects projects of SOEs complying with the national industrial policy, and asks SOCBs to allocate mobilized resources. This practice deprives bank management of autonomy in decision making for profit maximization.

SBV has promulgated a number of provisions on setting up deposit-taking, lending, and portfolio investments to secure an effective monetary policy, direct credits to most productive sectors, and enhance the soundness of credit institutions. However, supervisors appear to encounter difficulties in enforcing prudential regulations. Excessive lending primarily to State enterprises is a particular problem, as regulations limiting credit to a single borrower are easily

circumvented. There have been delays in conducting international standard audits of the major banks.

Fair competition is the surest way to improve efficiency. To promote competition, first the playing field should be leveled and sufficient incentives for improving performance given to players. However, markets for SOCBs and JSBs are completely separate in terms of depositors and borrowers. Due to the segmented nature of financial markets, competition is not a great concern to SOCBs. Even the seemingly stronger competition among JSBs is confined to interest rate competition. This business environment has limited the internal and external expansion of the banking sector.

In the context of supervision of the implementation of prudential regulations, besides monitoring and supervision by the credit institutions, supervision and monitoring is carried out by the SBV, by the line ministries and Government agencies, and by People's Committees. The supervisory scheme needs to be streamlined so that banking is separated from political interests, and supervision is carried out by an autonomous agency, such as the SBV.

The law on SBV fell far short of the initial expectation in enhancing the autonomy of the central bank. The law needs to be revised to allow SBV to implement monetary policy independent of politics. Since Vietnam is in the process of establishing good practice, the law has to make sure that the SBV policy decisions are made according to transparent standards and discussion, and that they are announced openly through the proper channel. SBV, on the other hand, should be made fully accountable for its decision.

The law on credit institutions also needs to be amended to level the playing field for foreign banks and JVBs vis-a-vis the domestic banks. At present, foreign banks are subject to special capital requirements, deposit restrictions, and collateral rules; and they have no access to the SBV refinance facilities. At the same time, the law does not provide a regulatory framework for the foreign bank branches that have thus far been governed by their operating licenses. Equally of concern are stipulations regarding the directed and subsidized lending, which specify that the Government can direct banks to provide subsidized loans for SOEs. Already over 50 percent of SOCBs lending is directed to SOEs and is not secured.

The interest rate regime in Vietnam has recently been significantly liberalised; therefore, the credit institutions now are free to determine their deposit and lending interest rates. The credit transactions are negotiated by the banks and their clients, and SBV does not intervene into the credit transactions.

SBV is responsible before the Government about the monetary policy implementation and state management in banking sector. SBV reports to the Government and National Assembly on the implementation of national monetary policy and about its activities.

4.2.2 Electricity Regulatory Authority of Vietnam

The Ministry of Industry (MOI) is responsible for state management in electricity. The Ministry organises preparation of electricity development master planning and submits it to the Prime Minister for approval. The provincial people committees organise the formation of the master planning within their jurisdictions, submit the plans to the provincial people council for approval and then to the Minister of Industries for final approval. The provincial people committees guide the formation of and make approval of electricity development master planning of districts, and examine the implementation of the planning approved by the local authorities.

Under the Electricity Law, the MOI is responsible for administering electricity activities and use, and the People's Committees manage electricity activities and use within their jurisdiction. The MOI issues licences for electricity wholesalers and retailers and for entities involved in electricity generation, transmission and distribution activities connected to the national electricity network. The provincial People's Committees issues licences for organisations and entities operating electricity activities on a smaller scale within the provinces, in accordance with guidance from the MOI.

Under the law, electricity retail tariffs are prepared by the MOI with assistance from the Electricity Regulator and approved by the Prime Minister. Electricity generation and wholesale tariffs, fees for electricity transmission and distribution, and auxiliary services are proposed by the entities involved in relevant electricity activities and evaluated by the Electricity Regulator and approved by the Minister of Industry.

The electricity units can determine the electricity prices at the stages of generation, wholesale and retail stage within the band and schedule approved by the competent authorities. One of the underlying principle in electricity pricing, as set by the Law is "to ensure the right of entities purchasing and selling electricity in the market to make their own decisions on the price of purchase and sale of electricity within the electricity tariff stipulated in the state regulations."

The Electricity Regulator assists the MOI in:

i) preparing rules and guidance on the operation of competitive electricity markets;
ii) suggesting measures to adjust and maintain the balance between electricity supply and demand;
iii) issuing, amending and revoking electricity licences;
iv) issuing guidance on the conditions and procedures for interconnection to the national electricity system;
v) preparing electricity retail tariffs;
vi) providing for the tariffs for electricity generation and wholesale, and the fees for transmission and distribution;
vii) observing the implementation of plans and projects of investment in the development of electricity sources, electricity transmission and distribution grids for compliance with the master plans;
viii) observing the implementation of the approved electricity tariff; and
ix) settling complaints and disputes in the electricity market.

Workforce training and development is a top priority at ERAV. The regulator has set technical standards that apply to specific jobs so that appropriate training can be provided for specific workers.

Table 8.4 Features of Specialised Regulatory Agencies in Vietnam

Sector	Key features of regulatory functioning under line ministry
Banking (State Bank of Vietnam)	• SBV Governor and other Members are from the Government • Banks assigned performance rating • Government intervention in banking regulation and supervision system, particularly in credit allocation mechanism • Coordination of SBV with other ministries/government agencies limited • Banking sector made a credit window of the government • Supervision and monitoring carried out by multiple agencies

Electricity (Electricity Regulatory Authority of Vietnam)	• Electricity regulator established as a unit within the line ministry (the Ministry of Industry) • ERAV assists the Minister in carrying out regulatory activities

4.3 Interface with Competition Authority

According to the Competition Law promulgated in 2004, the competition authority has the tasks and powers to control the process of economic concentration; to investigate competition cases related to competition-restricting and unfair competition practices; to sanction unfair competition practices. The laws on the sectors mentioned in this report specify the state management functions of relevant ministries. Among the state management functions, there are some functions relating to the competition issues, such as entry into the market (licensing), non-discriminatory access to the incumbent' network (inter-connection issues), control of the tariff of monopolists or dominants in the relevant markets, settlement of disputes, and punishment for violations to the laws.

The above description of functions indicates that there is potential overlap or conflicts between competition authority and the regulators in Vietnam, especially the market entry and non-discriminatory access. The Competition Law state clearly that where there is any disparity between the provisions of the Competition Law and those of other laws on competition restriction or unfair competition, the provisions of Competition Law shall apply. Furthermore, the Competition Law also covers enterprises producing, supplying products, providing public-utility services, enterprises operating in the State-monopolised sectors and domains.

The above regulations provide for strong application of the Competition Law. However, exemptions provided in the law tend to lessen the power of Competition Law in dealing with state-monopolised sectors. Particularly, the Competition Law provides exemption in cases where enterprises rationalise the organisational structure, raising business efficiency; enterprises promote technical and technological advances, raising goods and service quality, etc. The cases of exemption from prohibited economic concentration if one or more of the participants in economic concentration is/are in danger of dissolution or bankruptcy or the economic concentration has an effect of expanding export or contributing to socio-economic development, technical and technological advance. With these criteria for exemption, there is larger room for the state owned enterprises, especially the large state general corporations to avoid the Competition Law.

5. Concluding Remarks

For long, most of the ministries in Vietnam played the role of a policy maker, regulator and operator through SOEs. Realising the disadvantages and inappropriateness of having authorities operate two simultaneous management functions over economic organisations, the CPV Party stressed in 1986 that administrative authorities at all levels must fundamentally reform the mode of management so that they perform their appropriate function of state governance while transferring the function of business and production to the economic units themselves.

Vietnam has accordingly made some progress in separating policy and regulatory functions from the provision of services. However, this approach has not been fully put into practice, as the line between the two functions of state governance and economic management of SOEs is still vague. The essence of the two functions has become blurred under the ambiguous catch-phrase

"ministerial control" which is used to describe the state ownership relationship. The ministries still maintain linkages with the enterprises in some form, for example direct management of state owned enterprises or state representative at the enterprises. These strong linkages create concerns about the neutrality of the ministries in making decisions on regulatory issues.

While separation of commercial operations from ministries is emphasised upon, separation of policy and regulation functions (by creating a non-ministerial regulator) is not the preferred approach in Vietnam. The Constitution entrusts the government with the overall management of the economy. Accordingly, State assumes the role of policy maker and regulator. In certain sectors (telecom and transportation), regulation is performed directly by the government. Furthermore, even in sectors, where a specialized agency is created to perform regulatory functions, government intervention nullifies their independent functioning. This is true in banking, as observed in the paper, as well as in electricity, where the regulator has, in fact, been set up as a unit within the Ministry to assist it in carrying out regulatory activities. Therefore, the prevailing approach is of vesting policy as well as regulatory functions on line ministries.

The functioning of regulatory regime in telecom and banking presents an interesting contrast. In banking, the functioning of SBV has been constrained by government intervention in various ways and this is reflected in the overall performance of the sector. In contrast, the functioning of MPT in telecom has done wonders for the sector. This experience highlights an important point in regulatory reforms – the success of regulatory regimes depends on the objectives/priorities set by the government. In telecom, government objectives are clearly laid out in the various policy/legal documents, which have provided the necessary platform for the MPT to spur competition and facilitate an orderly growth of telecom services. However, in banking, there are conflicts in policy objectives – the objectives of the government are in variance from the goals set for SBV. Consequently, government intervenes to realise its objectives and market regulation is sacrificed for other objectives of the government.

Given the existing political and public administration culture of Vietnam, and the resource constraints, creation of an independent non-ministerial regulator seems difficult, at least in the immediate future. In this context, the performance of telecom sector, which is witnessing a boom under the aegis of MPT, in fact, raises a fundamental question: is regulation key or regulators? A key lesson that emerges from the working of regulatory regimes in Vietnam is that for regulatory reforms to succeed, more important is a commitment on the part of the government, and clear and consistent objectives across all policy/legal documents applied to a particular sector.

Secondly, there is need to build the credibility of regulatory agencies (read Ministries). This came out strongly in the case of MPT. In the absence of public consultations and transparent procedures, MPT's credibility has been questioned. There is need for regulatory agencies to undertake wide consultation with public and industry to ensure transparent and impartial decisions.

It needs to be realised that 'regulation' refers not to the mesh of complicated and opaque rules, but to a set of transparent, consistent, and non-discriminatory rules that creates a competitive, dynamic environment in which firms can thrive and provides opportunities for stakeholders to participate.

Thirdly, capacity building is the need of the hour. The MPT has established some independence, most importantly from the influence of the dominant state-owned operator VNPT. However the agency's capabilities and expertise are in urgent need of upgrading. This applies across all

ministries and agencies entrusted with regulatory functions. ERAV has rightly identified workforce training as one of its top priorities.

An important concern that emerges in implementing regulation functions is the complex relationship between the ministries and state owned enterprises. A crucial requirement to improve implementation of regulation functions is to make state owned enterprises independent of line ministries. However, this does not seem feasible as, under the Constitution, the Government is charged with the supervision of public sector agencies. Considering this, a separate agency could instead be created to represent the State's interest in all SOEs, say, a Ministry of State-owned enterprises. This would at least address the conflict of interest that arises when the line ministry, which performs policy and regulatory functions, also represents State's interest in the SOEs it regulates.

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