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"The Future Regulatory Architecture" (S L Rao)

CONSUMER MOVEMENT

Around 1985 or so, S Guhan (eminent administrator and economist), Sriram Panchu (Supreme Court lawyer) and I (manager and economist), decided to start a Consumer (now Citizens) Action Group in Madras where we lived. I think we had an inaugural meeting and young Pradeep Mehta who had just started the Consumer Unity Trust and Society at Jaipur was also there. He came to show solidarity with a new consumer movement and perhaps to see if there was anything he could use. That was the first time I met him. It was brief but he made an impact on all of us, with his handsome persona, articulation and clarity.

Our paths crossed again only decades later when I was Director-General of the National Council of Applied Economic Research and he was the *enfant terrible* of the consumer movement. His intellect and activism had moved him from consumer protection to competition. By 1998 when I became the first chairman of the newly created Central Electricity Regulatory Commission, he was beginning to see the close linkages between all three, the consumer interest, competition and independent regulation.

COMPETITION

I think it was in the late 1980s that some of us got interested in the subject of competition. Khemani from the World Bank sent me his mimeographed booklets. The Cadbury Commission had just reported on the topic in the United Kingdom; and there were similar reports from South Africa and /Australia. I was inspired to write an article in the Economic and Political Weekly (probably the first on the subject in India).

At about the same time, CUTS took up the advocacy of competition. It was in VP Singh's Prime Ministry that the SVS Raghavan Committee reported on the subject and recommended a Competition Commission for India. CUTS took the competition bill by the horns and organized a series of consultations and conferences and publications to push the idea forward and give it flesh.

Over the years, CUTS and the other organizations he was associated with, did yeoman work in helping to draft the Competition Act and later in helping the Competition Commission to get on its way.

Pradeep was actively involved in every debate on competition policy, members of the commission, the appellate tribunal, staffing, relationship between sectoral regulators and the competition commission, and so forth.

TRADE

He was also at the same time getting involved in issues of international trade and free trade. He understood that the opening of the Indian economy and low import tariffs opened opportunities for unfair competition among foreign exporters to India. Issues of dumping, non-tariff barriers, etc, became a part of the study of competition.

The Dunkel draft proposals on opening markets to freer trade and the prospect of a World Trade Organization as the apex body to settle international trade disputes, along with the protection of intellectual property rights now had great and immediate relevance for India. Pradeep jumped into this debate and made a strong impression on the negotiators.

GEOGRAPHICAL EXPANSION

He also began to see the potential for similar work to what CUTS was doing in India in other developed countries and became perhaps the first Indian non- governmental organization to extend its work into Africa, Viet Nam and of course Geneva, the headquarters of the trade negotiations. CUTS was perhaps India's first multinational ngo!

REGULATION AND GOVERNANCE

It was Pradeep's interest in Competition and Regulation that caught my interest so many years after the founding of CUTS and CAG when I had lost touch with both. I had written on both subjects, had practiced as a regulator (as the first CERC Chairman), and thought deeply about the subject. When CUTS set up the CUTS Institute of Regulation and Competition Pradeep asked me to join its Board and its managing Committee, which I did.

It was some time before he became active in my area of in88888888888888888888888888888888888888888888888888ter est-regulation and governance and the need for more objective selection of regulators, their accountability, etc.

Today we have a multiplicity of regulators. Almost all are retired bureaucrats, with Chairmen being usually from the Indian

Administrative Service. Many are subservient to the opinion of Ministers and bureaucrats in service. Few are truly independent and they tend to function as departments of governemnt, especially in the states.

The telecom regulator was emasculated when Parliament disbanded the old body that had decision making powers and created a new one that was only recommendatory. This gave immense discretionary powers over resources and pricing that were worth a great deal, to Ministers and bureaucrats. The abuse of these powers led to huge losses for the nation.

The Petroleum and Natural Gas Regulatory Board has no tariff powers. It has powers to license pipelines. However even these were notified and given to the Board well after its creation. Meanwhile the powers were used by the Ministry without consulting the Board. Appointments to the Board have been controversial and led at times to loss of harmonious working.

Now there is to be a Coal Regulator who will also ultimately be under the Ministry. Given that coal is nationalized and all powers over this valuable and critical natural resource are with government, an independent regulator operating transparently is long overdue. But the appointment of the Members must be objective and ensure that there are independent people in it.

The Airports Regulator was created recently. The functioning of this regulator has been unsatisfactory for passengers and the airlines. The entry of private sector into operating airports appears to have led to a tilt towards it.

There is also mention of creation of many other regulatory bodies. However nothing seems to have been learnt from the experience of those already created. Even older regulators like the Reserve Bank of India and the Securities and Exchange Board of India now face considerable pressure from government to take decisions that the Regulator does not approve.

There is as yet no attempt to introduce accountability of regulators and some legislative oversight of their plans. There is also no doubt that this new mechanism of governance in India has been captured by the bureaucracy. Electricity and Information are subjects which have central and state regulators. Others so far are central because the subjects are in the central list in the Constitutions. These bodies have

provided a new arena for post-retirement appointments of retiring bureaucrats. While some are able to transform themselves (for example, CAG, CEC, some Governors of RBI), most carry their mindsets developed over more than thirty years in administrative service. They are subservient to government diktats, populist in philosophy (in keeping with having lived and worked for most of their lives in a so-called socialist framework), procedural in orientation, and with little interest in profit of the electricity enterprises an important measure of their efficiency.

Fortunately the Appellate Tribunal for Electricity seems to have some spirit and has taken steps to reform the power sector. This will no doubt happen with other sectors as well.

THE ROLE OF CUTS

Pradeep Mehta and his organizations will play an important role in all these debates and decisions. What explains an organization based in distant Jaipur developing so much influence on policy? There is no doubting that it is a result of the personality of Pradeep Mehta.

It was his apparent deep sincerity and passion that made him memorable and effective. His homework was prodigious. One can say that he blasted his way into the world of policy formulation.

Pradeep's role is that of the *agent provactrur,* not of the maker of policy. If he did not exist he would have to be invented. He plays a difficult role and occupies a central role in the areas of his interest.

FUTURE ARCHITECTURE

Most of the comments in this last section are derived from the experience with electricity, whose regulatory bodies have been in existence for long.

> **By 2025 the context should have changed. The key is the nature of reform and regulation that will develop and its objectives and methods. With more private investment and a diminution of government domination in all sectors, more experience of state owned enterprises with independent regulation, support from the Appellate bodies and Courts, introduction of commercial approaches and professional management, entrepreneurial styles**

of working, better technologies in place, reform in targeting and paying for subsidies, more transmission and pipeline capacities, introduction of comprehensive educational and training programmes for Regulators and their staff, we can expect a significant change in the manner of regulatory functioning.

More transactions will be market based and the regulator will be ensuring that the markets function transparently. Transmission and distribution capacity (in electricity, oil, gas, telecom, and others) will be adequate, with even some redundancy. Renewable energy will be a higher proportion of the total. Open access to pipelines and transmission lines will make for free movement of the regulated items. Market based tariffs, determined in many cases on independent Exchanges, will be determined by demand and supply with the Regulator having little role except in regulating markets. However the Regulator will continue to regulate long-term contracts and monitor the delivery of subsidies. Subsidies will remain and the Regulator must play a more proactive role with government in reimbursing utilities and ensuring that the subsidy reaches only those it is meant for and the quantities specified. However the service provider will not be required to manipulate prices so that cross-subsidies are possible. Cross-subsidies will disappear. The Regulator will actively encourage the development of competition in all areas from production to the consumer. By 2025 governments would have become accustomed to independent regulation and the relationships would have become more mature. The presence of a large private sector will mitigate today's ill effects of close government –enterprise relationships.

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2025

By 2025 we can hope that capacity and particularly privately owned capacity will increase to meet demand and there may even be adequate redundancy in each sector to meet sudden peak demands. In electricity, merit order dispatch will rule and load dispatch will be an independent and neutral non-profit

function. Transmission capacity will have expanded to enable a truly national grid and there will even be redundancy in transmission capacity. Thefts of electricity will be a memory and efficiencies and quality will have improved.

Regulators will no longer be trying to improve management, information and commercial cultures but will be promoting trading and developing markets. There might be South Asian Grids in electricity, oil and gas.

In electricity, distributed power will be common, using gas in small package generators as well as biomass gasifiers and solar technologies serving closed or isolated communities both in urban and rural India. State ownership might be high but will function independently. As renewables grow in the total energy mix, their costs will fall and lead to their greater use, encouraged by Regulators.

The Petroleum and natural Gas Regulatory Board as well as independent regulators for coal, railways, and airlines, perhaps even retail trade, might have been created by 2025. This proliferation of new 'independent' regulatory bodies could add another layer of clutter to our governance structure without improving it. We must build safeguards to keep them effective. Two actions are required.

1. **One is to reorganize ministries and departments so that there is more coordinated decision-making.**
2. **The other is to combine responsibilities so that that there are not numerous regulators dealing with related subjects. There must be mandatory consultations between regulatory agencies on specific issues that impinge on common jurisdictions. (The division between the overarching reach of the Competition commission and sector regulators with narrower focus is a good example). The Sri Lankan experience**

in providing for such regulatory consultation might be usefully studied and emulated.

BEYOND INDIA

We can expect by 2025 that the electricity and gas Grids in South Asia will be interconnected. This will raise further issues in regulatory coordination. It will be necessary to

- **Develop some common regulatory philosophies so that there can be coordination between regulators of different countries, essential to ensure Grid stability;**
- **Together explore potential sources of energy likely by 2025- coal bed methane, Gas hydrates, etc;**
- **As trading and markets develop, coordination in tariffs might become possible and will lead to common governmental actions on energy security;**
- **The use of storage of gas for the region and its strategic release might be another issue for regulators.**

This tribute to Pradeep Mehta ends on an optimistic note, like his personality. We are slow to change and to adjust our institutions but we will get there.

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