

National Treasury Workshop
17/18 November 2009

G:ENESIS

Regulator Design in South Africa

James Hodge
Competition and Regulatory Economics Practice

- South Africa has a variety of regulators with different designs and performance levels
 - Considerable recent debate over optimal design
 - Review of whether a common framework is appropriate
- The process of review and recent events has initiated debate on specific issues
 - Role of policy-maker and what does 'independence' mean
 - Performance and accountability of regulators
 - Transparency and rigour of decision-making
 - Appeals and jurisdictional considerations
 - Internal design - Role of councilors and CEO within the regulator

G:GENESIS

Role of regulator and policy-maker

- Independent regulators are not the end in itself – it is rather the means to the end
 - Ultimate objective set by policy – for infrastructure usually quality service at the lowest possible price and achieving social goals
 - Independent regulation important when private investment involved
- Independence there to prevent opportunistic deviations from the general policy framework and not to produce the general framework (legislation)
 - Policy-maker must provide the framework for decisions – legislation
 - Sector performance will be influenced by these decisions
 - Within general framework there may be short-term political incentives to influence pricing or competition with SOEs once private investment is made
 - Regulator independence is then important for specific decisions which are guided by the given framework – gives certainty

- Contract analogy:
 - Simplest form of regulation is through an independent judiciary enforcing a contract (licence) with the state
 - Regulators emerge to take this role when specialist knowledge is required, there are on-going requirements for timely 'arbitration', and there is an inability to contract all complexity/uncertainty
 - policy-maker writes contract (legislation) with investor & court (regulator) arbitrates on given contract
 - Investor impact of a lack of independence is analogous to bias in independent judiciary

- Some sources of practical difficulties in the policy-maker/regulator relationship
 - Policy framework (legislation) sometimes not specific enough leaving issues of substance open to the regulator to determine
 - Regulator ends up ‘making policy’ in contradiction to the implicit policy of government – where does policy end and regulation start
 - Indicates that legislation and related policy should be well defined and critical decision parameters determined
 - Unexpected system shocks may require adjustments to policy
 - Does regulator show flexibility or not?
 - Regulator fails to acknowledge or be accountable as an agency
 - Poor regulatory performance may create uncertainty itself, undermine investment and fail to achieve policy objectives
 - Regulatory capture may undermine policy objectives

G:GENESIS

Aspects of independence

- Independence needs to protect against direct and indirect state influence and stakeholder capture
 - Independence from direct influence
 - Executive authority: decisions should not be approved, vetoed or appealed to the line/shareholding ministry
 - Organisational autonomy: regulator should have own staff and not make use of departmental resources, physical separation often deemed desirable
 - State may influence decision indirectly by influencing the decision-maker
 - Appointments and dismissal, performance review and funding approval are all aspects that can be used to influence the regulator
- Transparency in decision-making and appeal amongst the best check

- In general, SA regulators now have executive authority

Details of executive authority of regulator	
NERSA	
- licensing	There is not scope for the Minister to directly impact the decision of the regulator
- regulation of prices / tariffs	There is not scope for the Minister to directly impact the decision of the regulator
- mediation / adjudicatory powers	There is not scope for the Minister to directly impact the decision of the regulator
ICASA	
- licensing	There is not scope for the Minister to directly impact the decision of the regulator but minister initiates call for network licenses
- regulation of prices / tariffs	There is not scope for the Minister to directly impact the decision of the regulator
- mediation / adjudicatory powers	There is not scope for the Minister to directly impact the decision of the regulator
Ports Regulator	
- regulation of prices / tariffs	There is limited scope for the Minister to directly impact the decision of the regulator. However, the National Port Consultative Committee (NPCC), which is a consultative committee to the Minister, also has the power to consider <i>substantial</i> changes to the ports authority's tariffs.
- mediation / adjudicatory powers	There is not scope for the Minister to directly impact the decision of the regulator
Aviation Regulatory Committee	
- sale or closure of an aerodrome	The Regulatory Committee can only make recommendations to the Minister in this regard.
- regulation of prices / tariffs	There is limited scope for the Minister to directly impact the decision of the regulator. However, any amendments to permission granted by the regulatory committee must be approved by the Minister.
- mediation / adjudicatory powers	There is no scope for the Minister to directly impact the decision of the regulator

- In general SA regulators have organisational autonomy

	Legal form	Physical location of regulator	Staffing arrangement
NERSA	Separate juristic person.	Separate buildings (Pretoria)	Separate staffing pool
ICASA	Separate juristic person.	Separate buildings (Johannesburg)	Separate staffing pool
Port Regulator	Separate juristic person.	Not yet known.	Separate staffing pool
Aviation Regulating Committee	Is not a separate juristic person and falls under the Department of Transport	No separate buildings	At least 2 of the 5 member regulatory committee must not be public officers or employees. Support staff members are made up of officers of the Department of Transport.

- Currently the line Minister plays a central role in appointment/dismissal except ICASA where independence is constitutionally enshrined

Regulator	Detail of appointment	Detail of Dismissal procedure
NERSA	The <u>Minister</u> appoints regulator members including: chairperson, deputy chairperson, CEO and the three regulators primarily responsible for electricity, gas and pipelines. Minister can also renew contracts of regulators.	Minster may dismiss regulator member if they fail to perform their duties as per the National Energy Regulator Act of 2004.
ICASA	The <u>National Assembly</u> presents a short list of candidates to the <u>Minister</u> for appointment. The Minister's appointment must then be approved by the National Assembly.	A councilor can only be removed from office on a finding by the National Assembly (or the adoption of a resolution by the National Assemble calling for the removal from office) on account of a number of offences as per the ICASA Act of 2000 as amended.
Ports Regulator	The <u>Minister</u> appoints all regulator members. The Minister is also responsible for appointing the chairman and CEO of the regulator.	Members of the Port Regulator can be dismissed by Minister for being absent from three consecutive meetings without a good reason and permission from the chairperson, failing to perform its functions diligently, failing to disclose interests and misconduct.
Aviation Regulatory Committee	The 4 member Committee is appointed by the <u>Minister</u> (2 members can be civil servants).	The legislation does not set out a procedure for the dismissal of members of the Committee. However, the Minister can make regulations in this regard.

- In general, funding and budget approval through the line Ministry

Regulator	Provisions for funding from government	Provisions for levies imposed on industry	Provision for dispute resolution charges & license fees	Provisions for donations and contributions	Comments
NERSA	✓	✓	✓	✓	In practice, all funding from levies. Budget approved by responsible Minister with concurrence of Minister of Finance.
ICASA	✓				Allowance is also made for the regulator to receive other monies as agreed by the responsible Minister and the Minister of Finance.
Ports Regulator	✓		✓		Fees for filing of disputes and appeals with the regulator require approval from responsible Minister with concurrence of Minister of Finance. Budget approved by responsible Minister with concurrence of Minister of Finance.
Aviation Regulatory Committee	✓				Funding from the Department of Transport. However, members of the Committee who are not officers of the Department receive remuneration from funds appropriated by Parliament for that purpose.

- Certainty and investment are enhanced through transparent and predictable decision-making
- Public processes and written reasons for decisions all contribute to ensuring influence can be detected and hence independence preserved
- Judicial review of administrative action enshrined in the constitution
- Promotion of Administrative Justice Act outlines procedural fairness and applies to all regulators
 - Predictability may be enhanced by outlining of specific processes to be followed
 - Transparency and independence is enhanced by public hearings and reasons for decisions
 - Procedures should be proportionate to the decision

- All administrative decisions are subject to judicial review which just falls short of an appeal on the merits

	Review	Formal Internal Appeal Process	Appeal
ICASA	Yes		
NERSA	Yes		In relation to when there has been a contravention of a licence condition. The Petroleum Pipelines Act provides for a formal internal appeal by an aggrieved party.
Department of Water Affairs and Forestry	Yes		Decisions by the Minister of Water Affairs and Forestry, DWAF and Catchment Management Agencies can be appealed to the Water Tribunal. The types of decisions that can be appealed include the failure to grant a water use license and a claim of costs from a water catchment agency. The Tribunal's decisions can be appealed to the High Court.
Port Regulator	Yes		

- Freedom from direct influence is a necessary condition for independence from the state
- However, questions are raised about some of the indirect elements
 - Tension between required government oversight of agency and undue influence over decision-maker
 - Ministry sometimes best placed to make decisions on appointment and funding – may or may not make use of influence
 - May resolve by protecting regulator from those with the largest incentives for short-term influence over decisions - line ministry and shareholding ministry
 - Does parliament in the alternative have the resources to adequately oversee regulators – portfolio committee structure facilitates this
 - Can National Treasury alone provide oversight on funding

- The review process also seems a sound precondition, but there are mixed responses on a full appeal
 - Appeal may be a more powerful mechanism for raising quality of decision-making
 - Scope for abuse by regulated firms and may not necessarily be better equipped to provide a better answer
 - Credible threat of appeal or review may drive regulator to appease regulated firms and succumb to interests

G:GENESIS

Accountability

- Adequate accountability of the regulator is as important as independence
 - Avoidance of regulatory capture
 - Avoidance of poor performance by the regulator
- Performance oversight by the state as an agency of the state
 - Questions around who
- Transparency and judicial review of decision-making is often one of the best checks on poor performance and independence from other influences
- Adequacy of funding is also an important measure against regulatory capture but may not guarantee performance by itself
 - Alternative source for information and expertise

- Reporting is generally through an annual report tabled in parliament and few regulators have actual performance level agreements

	Reporting arrangements	Performance level agreements
NERSA	NERSA is required to produce an annual report which is tabled in Parliament. In terms of the PFMA, it reports to the Minister and National Treasury quarterly.	There is no performance agreement that NERSA members sign with the Minister or any other institution. However, individual energy regulators are required to sign a performance agreement with the Energy Regulator.
ICASA	ICASA produces an annual report that the relevant Minister must then table in Parliament.	The Minister in consultation with the National Assembly must establish a performance management system to monitor and evaluate the performance of the chairperson and councilors. An assessment should be conducted once a year by a panel constituted by the Minister (in consultation with the National Assembly). Once the assessment is complete the panel should make a presentation to the National Assembly.
Port Regulator	The regulator submits a report to the Minister who then tables the report in Parliament.	There is no performance agreement that a member of the port regulator has to sign with the Minister or any other institution.
Aviation Regulating Committee	The Committee produces an annual report that is submitted to the relevant Minister who then tables it in Parliament.	In terms of the legislation, members of the Committee do not have to sign performance agreements with the Minister or other institution.

- Despite annual reporting there remain concerns over the adequacy of oversight and accountability for some regulators
 - Careful oversight of strategic direction and prioritisation of regulatory issues
 - Especially the sequencing and timeliness of regulatory rules
 - Accountability for failure to deliver against stated objectives
 - What are effective sanctions that can be used against the chair, councilors and the CEO?
 - Who is responsible for ongoing performance reviews and does the fact it is the minister in some cases raise influence concerns?

G:GENESIS

Conclusions

- Many of the appropriate design elements are in place for SA regulators
 - However, concerns persist around independence and accountability
- The design elements around independence and accountability are usually necessary but not sufficient preconditions for good regulatory performance
 - Some design elements may be less material in the right environment
 - Elusive factors such as the right people, organisational culture, robust relationships with the state and stakeholders, rigorous and pragmatic decision-making, respect and authority, etc cannot be designed but have a significant impact on performance
- Need more work on other elements to building effective regulators