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“Doing Things Differently and Doing Things Right: African Utility Regulators and the Burden of  
Transparency”

A paper by

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**Paper title:** Doing Things Differently and Doing Things Right: African Utility Regulators and the Burden of Transparency

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## **Abstract**

This paper discusses the challenges of ensuring transparency in utility regulation in Africa. It finds that in a continent where public policy formulation and implementation in the public sector are usually characterized by a high degree of secrecy and the system of political accountability is rather weak, it is difficult to run a transparent and accountable regulatory body.

The paper argues that by its statutory existence, operational nature and task-design, a utility regulator, no matter its degree of independence, still maintains the attributes of a public body. It is also in constant and most times, troubled (depending on the dynamics of the political economy) interface with the government, as it represents the instrument for the execution of public policy. Because regulation is essentially the execution of public policy, a regulatory agency is domiciled in the executive branch of government and shares its opacity and indeterminacy.<sup>2</sup>

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<sup>2</sup> By 'indeterminacy' I mean that the relationship between legal materials and the actual workings of institutions in the executive branch of government are non-linear. Formal legal materials underdetermine outcome as 'politics'

This fraternal affinity poses peculiar problems for fledgling African utility regulators, as they are caught between two worlds: the world of business as usual (BAU), which suits other government agencies whom the regulator constantly relates with and the world of international best practice (IBP) to which by its mandate and policy documents it subscribes, and where its investors and other stakeholders want it to remain. The paper goes on to explain that making the choice between these two is never straight forward, given that these regulatory bodies, particularly those in electricity, rail and water are to a large extent, still being funded by the State. Their routes to financial independence are still dependent upon state authorities incentivising investment climate, thus, the regulator is in a delicate balance of courting the authorities and attempting to radiate transparency. These two could be conflicting at times in sub-Saharan Africa. The paper then proceeds to discuss, through working experiences, the best practice scenario in the relationship between regulators and stakeholders. From practical experiences, the paper opines that the level of transparency required in the regulatory process needs to exhibit certain features to meet the standards necessary for a utility to truly command sectoral market confidence. While many bureaucrats by default deem transparency as counterintuitive, the paper finds that it an essential requirement in a regulatory agency's decision making process. It concludes by arguing that there must be, embedded within the regulatory framework, a mechanism for ensuring transparency, since it is an indispensable tool for an effective regulator, and it is equally sacrosanct and critical to engendering real competition in any electricity market.

### **Power Sector Reform and Regulation in Nigeria**

Many African countries have embarked on the reform of the administration of their utilities, especially electricity. Power sector reform is now a fad in Africa. This is akin to

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affects the causality between formality and outcome. How the law says such institutions should behave and how they actually behave are often different

the fashionable moments in the 80s when the dynamics of neoliberal reconstruction of the global economy led to a sleuth of structural adjustment programs across Africa. These reforms were forced on African countries by the exigency of looking to international financial institutions like the International Monetary Fund (IMF) and the World Bank for financial bailouts in the midst of fiscal crisis. In similar vein, the reform of the power sector in Africa follows the heels of the similar reforms in the west, particularly the British where the government of Margaret Thatcher restructured British electricity and telecom.

In the particular case of privatization, I have argued that “Privatization as a reform policy is best understood within the context of the politics of economic reform. Its emergency as inevitable policy option for the Third World economies is not just a function of its merit as an economic policy but also a function of the ideological orientation of the triumphant Anglo-American capitalism which de-legitimizes the role of the state in the economy... It is important to note that privatization gained currency as an elixir for failing African economies and East European transitional economies at about the same time that the Berlin Wall collapsed, symbolizing the end of the ideological battle between two global grand narratives: capitalism and communism”.<sup>3</sup> So, privatization in Africa is another diffusion of ‘global best practice’.

Nigeria followed after the British model by unbundling the vertically integrated publicly owned electricity company into independent generation, transmission and distribution companies. These companies, apart from the Transmission Company of Nigeria (TCN), are now to be sold to private firms<sup>4</sup>. Nigeria also instituted an independent regulatory

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<sup>3</sup> Sam Amadi, *Privatization & Public Good: The Rule of Law Challenge* (Lagos, Center for Public Policy & Research) 2008, pages 46-7

<sup>4</sup> Since 2005 Nigeria commenced the bundling of the Nigeria Electric Power Authority into 18 companies (6 generation, 1 transmission and 12 distribution companies). The Electric Power Sector Reform (EPSR) Act, 2005

agency, the Nigerian Electricity Regulatory Commission (NERC) to regulate entry and exit, tariff and quality of service of the Electricity Supply Industry (ESI). As David M. Newbery points out, the English model of vertical separation has become the reference for reform of utilities across the world.<sup>5</sup>

The separation of the various segments of the electricity industry and the introduction of an independent regulator with the responsibility to set requirements for entry into and exit from the market, determine tariff and set and enforce quality of service standards introduce into the ESI dynamics that are different from the ones prevailing under state monopoly of the network. These dynamics identify multiple stakeholders with differentiate interests, rights and expectations. They change the work of coordination and expect the regulator to be fair and firm.

In a regulated and vertically separated ESI the central challenge is to simulate the conditions of a competitive market through price signals and other information encoded in rules and codes. There are many theories that justify the need for regulation. They can be grouped under the categories of positive and normative theories. Normative theory of regulation describes how regulation ought to be done while positive theory points out how regulation is done in practice. From a normative perspective, regulation seeks to cure the inherent failure of any market, especially the market of natural monopoly like a network utility. This requires that prices are set at efficient levels that

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provides that these companies would be first corporatized in a holding company (Power Holding Company of Nigeria (PHCN) and later sold to preferred bidders who will hold controlling shares in the companies. As at March 19, 2013 preferred bidders have been selected for the companies and they are being expected to complete payment and take over something in September 2013. See [www.bpeng.org](http://www.bpeng.org) for more details on current largest privatization in Africa

<sup>5</sup> David M. Newbery, *Privatization, Restructuring, and Regulation of Network Utilities* (Massachusetts, MIT Press) 1999 page 200

allow for financing of investment and recovery of costs. Regulation is proposed as an alternative to competition because in a monopoly competition is usually inefficient

The positive theory challenges the ideal theory of regulation and argues that in practice various interest groups demand for regulation in order to promote their interests at the detriment of other interest group. “Regulators are seen as utility-maximizing arbiters between these various interest groups. Different interest groups have different bargaining power, depending on their costs of organizing and the benefits of manipulating outcomes, and they will intervene to redistribute benefits to their group at some additional inefficiency cost”.<sup>6</sup> Ronald Coase warns that whether it is the market or regulation we cannot escape failures - market failure or government failures.<sup>7</sup>

At the heart of efforts to avoid market failure is the management of information. Curing information asymmetry will result in a competitive ESI. Of all the reasons being put out for embarking on the reform of the power sector, the central objective is to simulate competition, so as to enable power consumers enjoy the benefits that are associated with multiple source service provision and the positive effects it brings<sup>8</sup>. The unique peculiarity of electricity has often prevented the entire value chain of the industry from being made completely competitive. During corporatization, states have been able to introduce a more or less effective competition at the generation and distribution ends, through deregulation and vertical disintegrations. However, transmission networks

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<sup>6</sup> David M. Newbery op cit, page 141

<sup>7</sup> Ronald Coase, ‘The Regulated Industry: Discussion’ in American Economic Review 54 (May) 194-8)

<sup>8</sup> However, as underscored by Ugaz 2001, reforms were sometimes also designed in a way to restrict competition even though it would have been possible to introduce competition. In Latin America, for example, Telefónica del Peru was granted exclusive rights for the operation of basic telephone services. The reasons for such a restriction of competition are on the one hand, to maximize revenue from privatization, given that a firm with monopoly power has higher value for private investors, and on the other hand to expand services in order to meet universal service obligations and improve quality, here exclusive rights might attract the needed foreign capital.

(grids) have largely remained in monopolistic condition or with substantial market power after these reforms have been introduced. This situation could be tricky for a fledgling regulator in Africa, given that the need to reform here arises mostly from the need to overcome inefficiency, incompetence, and both technical and non-technical losses.. The fact that wheeling of electricity product will remain is, could if not properly managed<sup>9</sup>, remain an inlet and conduit for corruption and inefficiency to persist in the sector. In Africa, the publicly owned transmission component of the electricity supply industry could serve as the back door for government officials to introduce policies that can undermine efficiency and competition.

In Africa, the electricity sector regulator, indeed any utility regulator, has a huge social responsibility in the reform of utility services. Some researchers have argued<sup>10</sup> that because of the “special technical and economical” characteristics of the power sector, and not at least because of its social and political sensitivity, a regulatory body is an indispensable and key component of an on-going reform process. This is why the establishment, institutionalization and capacitating of a regulatory body has equally been viewed as a strong evidence of political commitment to undertake a successful reform<sup>11</sup>. It is the responsibility of the regulator to ensure productive and allocative efficiency of the sector and the financial viability of the operators. The regulator

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<sup>9</sup> Our experience in Nigeria, is that given the sustained display of mal-management of the national grid by the unbundled/erstwhile monopoly, NEPA, the government while retaining a monopoly on transmission, competitively awarded the management of its expansion, strengthening and maintenance on a knowledge transfer contract to an experienced international company.

<sup>10</sup> Crémer H., Gasmi F., Grimaud A., Laffont, J.J. (2001): Universal Service: An Economic Perspective. *Annals of Public and Cooperative Economics* 72(1), 5-43. See also, Estache A., Martimort D. (1999): *Politics, Transaction Costs, and the Design of Regulatory Institutions*. Policy Research Working Paper 2073, World Bank

<sup>11</sup> Laffont J.-J. (2005) *Regulation and Development*. Federico Caffè Lectures. Cambridge University Press, Cambridge

ultimately should ensure that the tariff paid by consumers is fair and affordable and the service delivered to them of high quality. The regulator should shield consumers from monopolistic or oligopolistic manipulations of the market.

In the case of electricity, being an essential product whose under-consumption has huge negative externalities, some kind of social and equitable arrangements must be provided by the regulator, and financed either through targeted subsidies or redistributive pricing schemes that enable accessibility and affordability for all. Managing such subsidies and cross-subsidies and other mandated social programs is difficult and may soon become an opportunity for corruption. In Sub-Saharan Africa where access to electricity is still very poor, the newly established regulators are charged with accelerating rural electrification. In Nigeria for example, access to electricity is still very low, at about 50%. The reform law has created a rural electrification board to fast-track rural electrification.<sup>12</sup> Rural electrification could become another potent source of corruption in the electricity supply industry in Africa.<sup>13</sup> This is more so because it is targeted principally at the poor, illiterate peasants who are often disconnected from complaint and redress mechanisms. The dialectics of demand and supply of electricity disfavors these rural dwellers because they consume minimally

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<sup>12</sup> Section 88 of the Electric Power Sector Reform (EPSR) Act 2005 establishes the Rural Electrification Agency (REA) as a corporate body responsible for administering a fund for the purpose of promoting and supporting a rural electrification program through public-private participation. The agency will execute the Rural Electrification Strategy and Plan for Nigeria developed by the Minister of Power with the recommendation of the Nigerian Electricity Regulatory Commission (NERC)

<sup>13</sup> In 2009 a major corruption scandal gripped the Nigerian electricity supply industry on account of the management of the affairs of the Nigerian Rural Electrification Agency (REA). It is also known that so much fund has been pumped into the electrification of African rural communities, yet there have been poor result to show for the huge expenditure.



and would require costly and inefficient investment to transport power to them across difficult and distant terrains.

These many responsibilities put the African utility regulator on the spot. He is encumbered and challenged to reconcile divergent interests of operators and consumers. He is called upon to be a reliable facilitator of financial recovery for operators and full access for electricity consumers. He is expected to achieve the policies of government on the sector as well as project an image of independence. These binaries require the regulator to possess high intelligence and ethics in discharge of its responsibilities. They call for skillfulness in the science and art of regulation. But often, both the intelligence and ethics may not be in sufficient supply.

### **Corruption and the Regulatory Challenge**

Africa, deservedly or undeservedly, wears the toga of a corrupt continent. The corruption smear has become a disincentive to investment in infrastructure. Increasingly, African public officers are boldly facing the challenge of perception of corruption and designing institutions to counter the impression and fear of corruption. Today, the discourse of corruption has become integrated into the discourse of economic development. It is difficult to date precisely this integration. But the World Bank started to integrate discourse of corruption in the discourse of development in the Presidency of James Wolfensohn when the Bank began to demand greater accountability with use of development aid. It developed into the scholarship of transaction cost which, borrowing from the insights of New Institutional Economists like Douglas North, showed how the role of institution and the quality of governance of the institutions affect economic outcomes. Two leading scholars of law and development,

Cherly W Gray and Daniel Kauufman, elaborated the relationship between corruption and development with theoretic and empirical groundings. First, corruption increases transaction cost and uncertainty in the economy. It also “impedes long-term foreign and domestic investment, misallocates talents to rent-seeking activities, and distorts sectoral priorities and technology choices (by, for example, creating incentives to contract for large defence projects rather than rural health clinics specializing in preventive healthcare); it pushes firms underground (outside the formal sector), undercuts the state’ ability to raise revenue and leads to ever higher tax rates being levied on fewer and fewer taxpayers. This in turn reduces the state’s ability to provide essential public goods, including the rule of law”. They also argued that corruption imposes indirect taxation on the poor.<sup>14</sup> Corruption could easily defeat the intent and purpose of the market reforms through manifesting in high transactional and operational cost which does not translate to enhanced efficiency, but will be ultimately passed on to consumers.

Corruption takes many forms. The World Bank defines corruption as an abuse of power. Robert Klitgaard provides an interesting equation for corruption: “Corruption equals monopoly plus discretion minus accountability. Whether the activity is public, private, or nonprofit, or whether it is carried out in Ouagadougou or Washington, one will tend to find corruption when an organization or a person has a monopoly power over a good or service, has the discretion to decide who will receive it and how much that person gets,

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<sup>14</sup> Cherly W. Gray and Daniel Kauufman, “Corruption and Development” Finance and Development 1998 cited in Sam Amadi, Corruption and the Law, A Case of Unequal Justice”, a text of lecture delivered by Dr. Sam Amadi at the 2<sup>nd</sup> Lecture on Law and Social Development organized by Bamidele Aturu & Co. at the Lagos Airport Hotel, Ikeja, Lagos on October 26, 2009

and is not accountability".<sup>15</sup> This equation is good for consideration of the relationship between the regulator and corruption.

Corruption festers in the absence of the rule of law. There are many ways to conceive the rule of law and its relationship with corruption. Rule of law requires primarily that the transactions in the sector be guided by laws regularly made by legitimate institutions of the state and not subject to the whims and caprices of the powerful interests in the society. In the context of the power sector reform, this results in the requirement that the reform be guided by well settled laws. Secondly, it is important that transactions are not only governed by settled laws, but also that such laws are reasonable and protect the rights of market participants. This goes to the discretion side of the corruption equation. The regulatory regime must clearly articulate process of decision making in the market that is legitimate, certain and protective of vested rights, as long as those rights do not violate the rights of other stakeholders. Exercise of power to make decisions by all the market participants must be transparent and accountable. Accountability is an easily abused word. In reality agencies fail to be accountable. Beyond broad phrasing, accountability is best guaranteed by detailed procedures for decision making that provide intelligible standards of review, whether judicial or administrative.<sup>16</sup>

In Africa experiences have shown that when officers executing the reforms are left with enormous but unchecked powers, there could be a strong urge to manipulate several

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<sup>15</sup> Robert Klitgaard, International Cooperation against Corruption, Finance and Development (March, 1988) page 3-4

<sup>16</sup> See generally Breyer et al, Administrative Law and Regulatory Policy, Problems, Text and Cases (Aspen Publishers, 2006)

aspects in favor of firms for illicit rewards. Corrupt tendencies may lead to biased initial decisions that could ultimately be costly in the long run. Ultimately, as Boehm and Olaya<sup>17</sup> have argued, corruption has potentially fatal effects on competition. It undermines the anticipated gains of competition in a power market by distorting the governance structure of the market.

Corruption can ultimately frustrate the initiation of successful competition in an emerging market if the powers of the agency responsible for control and regulation are easily manipulated. Scholars have found that often the state of the market in the period immediately after the reforms is particularly vulnerable and prone to corruption. As Boehm<sup>18</sup> found, and practical experiences attest to, novel public-private interfaces that are established in pursuance of the reform, as well as application of the new regulations together take the electricity supply industry into uncharted territories. Regulators and their staff are suddenly entrusted with powers to decide, reshape and re-design an entire power market landscape with multi-billion dollar implications. It is not quite clear whether they have the temperament and organizational resources to be restrained and wise in the exercise of such enormous power. In the ensuing confusion, corruption can easily be nurtured. Sometimes, reforming governments fail to streamline the structure of government and unwittingly create overlapping functions and agencies. This adds to the lack of clarity and coherence. The regulator is composed of commissioners who are usually appointed partly on political consideration and staffers who are career minded and often come from the larger civil service or assimilate the attitudes and expectations

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<sup>17</sup> Boehm F, Olaya J. (2006) Corruption in Public Contracting Auctions: The Role of Transparency in Bidding Processes. *Annals of Public and Cooperative Economics* 77(4), 432-452

<sup>18</sup> Boehm F. (2007) *Regulatory Capture Revisited – Lessons from Economics of Corruption*. Internet Centre for Corruption Research (ICGG) Working Paper No. 22, available at [http://www.icgg.org/corruption.research\\_contributions.html](http://www.icgg.org/corruption.research_contributions.html)

of the civil service. These situations add to the corruptibility quotient of the regulator notwithstanding the high sounding aspirations in the law and policy documents.<sup>19</sup>

### **Corruption and Regulatory Capture**

Public choice theorists take the rationale for regulation as the demand by powerful interest groups for regulatory capture. In the unclear environment of regulating utilities in Africa in the context of somewhat disorderly public sector reform where sequencing and experimentation are abandoned, the utility market is quite vulnerable to regulatory capture by powerful strategic interest groups. The capture could be ex-ante, or post-ante<sup>20</sup>. An ex-ante capture comes at the very early stages of the market design. Ex-ante capture tends to manipulate the structure and design, particularly, the regulations of the new market before they become operational. Post ante, occurs after the market structure and the regulations have been put in place and made operational. The prospect of regulatory capture is rife in the circumstances in many countries where foreign governments, as forerunners of their private sectors, pay the fees of the policy advisors to design the regulatory and policy framework of the reform. This is a common feature of Africa's infrastructure reform.

Does the entry of the private sector or the privatization of the sector as Nigeria is doing now eliminate the risk of corruption and regulatory capture? African public service has

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<sup>19</sup> The commissioners of the Nigerian Electricity Regulatory Commission (NERC) are appointed by the President and confirmed by the Senate. They are supposed to be persons who are versed in generation, transmission, system operations, distribution or marketing of electricity and law, accounting, economics, finance or administration (Section 34(2) of the EPSR Act, 2005)

<sup>20</sup> Laffont J. (2005) *Regulation and Development*. Federico Caffè Lectures. Cambridge University Press, Cambridge. See also, Smith W. (1997) Utility Regulators: The Independence Debate. *Public Policy for the Private Sector*, December, Note 127, 9-12, World Bank, Washington D.C.

been generally described as weak, corrupt, incompetent and unprofessional.<sup>21</sup> These negatives have made it difficult for the public service to be relied upon to deliver efficient and credible services. It is on the basis of this belief in the incompetence and corruption of the public service in Africa that many advocates of reform of utility regulation in Africa have often argued for a private sector-led market and the existence of an independent regulator as the panacea to the crisis of social infrastructure in Africa. But is this faith well founded? Is privatization and the establishment of regulators independent on paper enough to guarantee competitive and efficient market? The assumption is that the most recently established regulatory agencies, which by the nature of their very existence are modeled to display attributes of operational independence, could easily leverage on their new found expertise and organizational resources and breakaway from the aforementioned negative attributes of the public sector. After all, these regulatory agencies have designed their process around the core universal values of transparency, accountability, public engagement and predictability.

Practical experiences show that perhaps we are trusting too much and too early on the transformation of regulatory regimes in Africa based on process design and policy articulation. The relationship between paper independence and actual independence of the regulator is non-linear. Beyond laws and policy statements, the macro regime type, the political dynamics and the cultural norms that define governance in different African societies codetermine the quality of regulatory commitment and capture. The independence of the regulator is dynamic and may be negotiated at different stages of the development of the regulator and the responses of the markets participants. The strategic behavior of the winners and losers of regulation will also determine the extent

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<sup>21</sup> See UN findings on this issue at; [unpan1.un.org/.../public/.../unpan030231](http://unpan1.un.org/.../public/.../unpan030231). See the African Development Bank (afdb) findings on the topic titled, "Re-Orienting Public Management in Africa". [www.afdb.org/.../publications/00457497](http://www.afdb.org/.../publications/00457497)

of the protection of the regulator's independence by the political leaders.<sup>22</sup> This is especially so in the prevailing situation in Africa where political institutions are not fully differentiated from the emergent business class. The intricate relationship between institutions of government, fiscal dependence, and cultural norms inhibits the ability of newly established regulatory agencies to escape the path of dependence on the public service.

Electricity sector reform is customarily likened to deregulation. Therefore, it is expected that reform would lead to a reduction of government involvement in the electricity sector. However, in Africa, the reforms being undertaken have for some reasons got government much more involved in the sector. Government has been more disposed to treat electricity less as a technical and business issue and more as a social service. As a social service the citizens have a right to electricity and government has to treat it as a source of political gain. This tendency is further encouraged by the prevalent energy poverty and the acute undercapacity of networks.

It is arguable that the power sector reforms taking place in Africa, while being more or less structural,<sup>23</sup> have still not bequeathed the newly established regulatory agencies with the required degree of moral and technical capability and institutional pedigree to

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<sup>22</sup> See Jose A Gomez-Ibanez, *Regulating Infrastructure: Monopoly, Contracts and Discretion* (Harvard University Press, 2003) pages 39-54

<sup>23</sup> In the case of Nigeria this involves vertical and horizontal unbundling of the hitherto public monopoly. Vertical unbundling occurs with the separation of generation from transmission and distribution. Horizontal unbundling occurs with the decentralization of the companies into small districts or municipalities. Horizontal unbundling is yet to happen in Nigeria. But many states are already owning generation assets and will like to own their distribution and transmission networks.

overcome the ‘Business as Usual’ (BAU) patterns of their MDA<sup>24</sup> counterparts. It must be pointed out that the connotation of the much talked about ‘independence of a regulator’ may after all not be a face-value fact<sup>25</sup>. Practical experiences from the West can attest to this. For instance, in the U.K., the regulators are not purely independent given that their discretion is subject to legislation, case law and evolving regulatory practice. In the U.S., Brown<sup>26</sup> has found that regulators operate under a statute that requires tariff setting to be just and reasonable and not unduly discriminatory. The social policy that underlines tariff-setting also conditions and somewhat limits the independence of the regulator. The U.S. judicial system further limits the decision making powers of regulators, hence they are not wholly independent after all. Obviously, between 1993 and 2004, the World Bank realized the futility of the quest for “regulators independence” as a concrete pre-conditionality for lending to power sector reforms. It has thus changed its core policy for power reform lending, thereby making its stance more pragmatic<sup>27</sup>. Over all, the newly established regulators of sub-Saharan Africa seem to fare badly when it comes to displaying features of independence and exercising operational autonomy. This is understandable considering the lack of effective checks and balances in the politics of countries in the continent and the institutional weakness of the regulatory framework.

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<sup>24</sup> Please see UN findings on this issue at; [unpan1.un.org/.../public/.../unpan030231](http://unpan1.un.org/.../public/.../unpan030231). See the African Development Bank (afdb) findings on the topic titled, “Re-Orienting Public Management in Africa”. [www.afdb.org/.../publications/00457497](http://www.afdb.org/.../publications/00457497)

<sup>25</sup> See, “independent regulators: theory, evidence and reform proposals” [www.iese.edu/research/pdfs/di-0860-e.pdf](http://www.iese.edu/research/pdfs/di-0860-e.pdf)

<sup>26</sup> Brown et al., 2006

<sup>27</sup> According to the World Bank’s Policy Paper of 1993, “A requirement of all power lending will be countries to set up transparent regulatory processes that are clearly independent”. Compare this to the 2004 WB staff Operational Guide which stated, “a credible regulatory system requires more than a formally independent regulatory entity”



## **Socio-economic Constraints African Regulators' Transparency**

While acknowledging that there are limits to independent regulation of utility services globally, it must be pointed out that it is often the weak regulatory commitment, political expediency, fragile institutions, an absence of transparency, financial dependence, and capacity constraints that undermine independent regulation in Africa to a more endemic level. The administrative proximity and inter-dependence between the fledgling regulator and the orthodox government agencies unfortunately helps to ensure that the regulators make no clean break with prevailing BAU in the larger public sector. Let me explore some of these constraints.

### **Weak Fiscal Autonomy**

One of the major constraints to full exercise of independence and regulatory autonomy by utility regulators in Africa is the usual weak fiscal state of the fledgling unbundled market. The regulator ought to have its finances from the market it regulates. But where the market is still fledgling and insolvent it cannot guarantee financial viability for the regulator. Therefore, the regulator has to depend on support from the government. Without this support independence on paper would be nothing and the regulator will be unable to solve a variety of teething challenge it faces, key amongst which is being able to attract suitable professionals as foundation staff. Government financing or budgetary allocations come in tranches and are often delayed and incomplete. In societies where institutions are still weak, releasing finance could become a window for public officers to influence, control, capture and hold hostage a regulator. This sort of regulatory capture, borne out of lack of financial autonomy at the foundational stages, is perhaps the most dangerous as it erodes the opportunity to set up a model and incorruptible institution from the onset. It equally ensures that the recruitment process is

manipulated by public officers, who are adept at compromising meritocracy for primordial ethnic and political considerations. Once the pioneer personnel requirement is compromised, regulatory decisions potentially become biased and ineffective. It is therefore essential that a fledgling regulator, who is incapable of immediate financial independence, is sufficiently financially funded and statutorily fiscally protected, so as to make those crucial early decisions in an autonomous atmosphere.

Therefore, as a matter of critical import, the financial autonomy of regulatory institutions becomes central and entwined with their independency. It is often argued that regulators should be independent from political officer's influence. Without a doubt, firms and investors have to be protected against arbitrary, political decisions and political interference in general, for example in order to seek for votes to gain elections through low tariffs that do not reflect industry cost, or to allow for excess employment in order to appease unions, cronies and constituents.

As long as the regulator depends on the government to support its finance it can barely run away from control of the established bureaucracy. The implication of this exposure to the public service bureaucracy is the potential compromise of transparency and global best practice. A regulator of a financially insolvent utility market will be hard put to escape the 'Business as Usual' paradigm and enforce full transparency and accountability. It can mitigate this challenge by both enhancing the financial viability of the market and ensuring prudence in the management of its internal affairs so that it does not have to run to government for financial bailout.

## Political Interference is Not Political Will

Reform of the utility industry requires huge political will in the context of politically sophisticated interest groups. But political will is not political interference. Political interference is what militates against African regulators migrating from 'Business as Usual' to global best practice denote by transparent and accountability. While the decision to reform the power sector is taken as a political resolution, it is often very important to know where to draw the boundaries between those initial enabling political pronouncements that facilitated the reform to progress, and the core regulatory tasks and decisions which must now be left for the newly established regulatory body. Experiences show that this line could be blurred often times as the political decision makers find it difficult to restrain from making powerful decisions and pronouncements. Regulation has to be decoupled from political considerations in order to assure investors of certain rules and a level field. Potential investors have to be shielded from political manipulations and risks arising from political uncertainties. International firms usually point to the stability of the regulatory framework as a critical factor influencing their decision whether to invest in a given country or not. They fear the situation of 'lock in' after having sunk investments in the contract making them vulnerable to extortion and expropriation by politicians<sup>28</sup>. Existing facts show that this threat is genuine<sup>29</sup>, hence scholars see the autonomy of the regulator as the harbinger of efficient and effective regulatory regime.

However, political opportunism is only one side of the regulatory capture equation. Regulatory autonomy, conceived in terms of removal from the direct influence of public

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<sup>28</sup> Armstrong M., Cowan S., Vickers J. (1994) *Regulatory Reform. Economic Analysis and British Experience*. Cambridge, MIT Press

<sup>29</sup> Spiller P. (1996) Institutions and Commitment. *Industrial and Corporate Change* 5(2), 421-452

sector bureaucracy does not cut deep enough. Such conception of autonomy while militating against the political capture of the regulatory agency may however unwittingly facilitate an unhealthy cozy relationship between the regulator and regulated firms. The corruption literature indicates that such autonomy together with the resulting discretion and information asymmetries can result in an environment where corruption flourishes. The complete autonomy of the regulator will only be optimal if one can fully trust in the integrity, intelligence and wisdom of the regulator. Autonomy is susceptible to corruption. Thus it will be mostly effective in climes where the institution of governance has been effectively strengthened, and predictable punitive measures are in place<sup>30</sup> to punish abuses. An Independent regulator can deliver on its lofty cardinal promises only upon the conditionality that appropriate deterrent mechanisms are in place to safeguard the state of autonomy from abuse. Thus even if autonomy may be a straightforward claim in western countries with established strong institutions, we should be cautious and state that autonomy is subject to abuse in countries with a weaker institutional environment.

In a capital intensive industry with complex contacting framework, the regulator must be viewed as a powerful coordinator of the orchestra. The lure for personal enrichment could be high as the regulators may be tempted to pursue their personal goals which may conflict with their public function. For this reason some have argued that there should be reasonable limits on regulatory autonomy. This does not mean that the regulator should be second-guessed with respect to decision making. But at least it

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<sup>30</sup> One of the distinguishing features of a society where institutions have been strengthened is the strength of its deterrent and punitive system. For instance, in most African countries, despite a long list of confirmed cases of malfeasance, only few public officers have been brought to justice. Even those convicted are often suspected to be victims of government opposition witch-hunt. Compare this with the more dreaded and effective public revenue protection in OECD countries.

should be made politically and administratively accountable to stakeholders. This should be more so in Africa where safeguard mechanisms of the regulatory regime are still untested and ineffective. Even if it is not possible for the regulator to be completely autonomous, it is at least arguable that leaving the regulator completely without any political influence can really be socially desirable.

***Regulatory Design, Autonomy and Accountability:***

Ultimately, the design of the regulatory framework should therefore take into account this balancing act. The regulator has to be reasonably protected against harmful political influence without becoming totally unconstrained by political officers. As Ugaz<sup>31</sup> aptly captured it, “independence should not be confused with lack of accountability.” Thus, putting the discretion of the regulator under some form of check can be quite desirable. Through a systematic reduction in the discretionary power of the regulatory body, the urge and incentives for the firms to capture the regulator will reduce as the regulatory decisions become subject of post-decision review.<sup>32</sup>

In his World Bank paper on the issue of regulatory independency, Smith<sup>33</sup> laid out procedures aimed at limiting the discretion of the regulator without falling back to political dependency. He posited ‘independence’ as “arm’s-length relationships with politicians, firms, and consumers” According to smith, the necessary steps required to

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<sup>31</sup> Ugaz C. (2001) *A Public Goods Approach to Regulation of Utilities*. United Nations University, Discussion Paper No. 2001/9

<sup>32</sup> The superiority of the US regulatory framework in this wise is shown by the fact of a well developed administrative law framework that provides clear administrative and judicial processes for the review of regulatory decisions. The Administrative Procedure Act (APA) sets out clear rules and procedures for administrative actions in the US. The Act is a powerful control on the otherwise huge executive, legislative and judicial powers of regulatory agencies in the country.

<sup>33</sup> Smith W. (1997) *Utility Regulators: The Independence Debate*. *Public Policy for the Private Sector*, December, Note 127, 9-12, World Bank, Washington D.C.

uphold political independence include; distinct legal mandate, professional criteria for appointment; executive and legislative branches involvement in appointments; fixed terms with protection from arbitrary removal, staggered terms of appointment, exemption from civil service salary rules, reliable funding-such as earmarked levies. In the same vein just as it is important to make regulators independent they should also be made accountable. The most important measure that can assure accountability of regulators is effective transparency, which should manifest in open and consultative decision making, publication of decisions and frequent and good faith feedback from stakeholders. Other measures that strengthen accountability include an efficient judicial review process (including appeal process), scrutiny of the regulatory body's budget by the legislature, and a comprehensive and effective code of conduct that prohibits conflicts of interest and mandates prudential behaviors. The regulator's performance should also be constantly scrutinized by relevant public watchdogs.

My experiences as a regulator assure me that it is easier to ensure the regulators independence from political interference than it is to ensure same from the regulated entities. It is also more attractive for a regulator to focus on its independence from political authority than its accountability to stakeholders, including political leadership. But in some circumstances, enhancing accountability may be a more profitable preoccupation for a regulator and may have more implication for market growth than independence from political authority. Transparent decision making and regulatory intervention is a major challenge a newly established African regulator must overcome to begin to effectively deliver on its mandate of a competitive and efficient market.

## **Taming the Corruption Monster through Transparency**

Corruption is a potent threat against the reform of the utility industries in Africa. And corruption is essentially the abuse of process for private or group gain. In the famous equation by Kaufman, corruption thrives where discretion goes without accountability. And transparency is the oil that lubricates accountability. Corruption thrives in opacity: in a luminous clear world of free-flow of information it is difficult and even risky to abuse existing rules in order to derive selfish pecuniary or strategic benefits. Not at least because those that are affected by corruption would be able to interfere and prevent corrupt deals from being settled. But as scholars have found<sup>34</sup>, if there is an information advantage and discretion on one side, this advantage can be abused and translated into a corrupt information rent for the better informed. Anti-corruption policies in regulation thus have to aim at reducing information asymmetries. Since discretion is unavoidable and necessary in regulation, introducing transparency, collecting data and information, and ensuring accountability should be primary objectives for anti-corruption efforts. As Bellver and Kaufman went on to buttress, “Increasing transparency through accessible, relevant, and accurate information is necessary but not a sufficient condition for accountability. Citizens also need the capacity and resources, political and financial, to exercise that right effectively.” So, information per se without capacity or mobilization is not enough.

Defeating corruption is a function of information at the hand of those who are able and willing to use it to change the game. A regime of transparency facilitates such situations. Public enlightenment and sensitization is critical here. It has often been the case that the media plays the oversight role of ‘watchdog’ for the society in various facets of public administration. Many financial and transactional scandals, including fraudulent

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<sup>34</sup> Bellver A., Kaufmann D. (2005) ‘*Transplanting Transparency: Initial Empirics and Policy Applications*. World Bank Discussion Paper, Washington D.C.

contract awards, misapplication of rules, misuse of public trust, have all been uncovered by the media. Thus, an Informed, free and independent press is a powerful tool to promote transparency and accountability in utility regulation. It is principally the default setting of opacity and ambiguity in administrative systems of institutional structures that ultimately impedes participatory and responsive governance by state institutions designed to serve people in Sub-Saharan Africa<sup>35</sup>. The electricity regulatory bodies, who fortunately are new entrants, must resist the urge to go the way of most public institutions before them. They enter the scene as reformers and are mandated to revolutionize this key segment of the economy. They should take the benefit of hindsight in seeking to be different.

***Conclusion:***

Thankfully, many African countries, under the conditions of globalization, are getting caught in the golden straightjacket of global best practice, apologies to Thomas Friedman.<sup>36</sup> They are being required by their financial benefactors to sign up to regimes of transparency and accountability such as the freedom of information law. Such legal institutions provide enablement for the regulator to still be tied to the apron-strings of government and yet promote global best practices. In Nigeria, the government has enacted the Freedom of Information (FOI) Act which requires all public institutions to make proactive disclosures of critical information available in retrievable forms in public domain. The Nigerian Electricity Regulatory Commission (NERC) has latched on this law to require the Nigerian electricity market to comply with these mandatory disclosures.

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<sup>35</sup> See UN findings on this issue at; [unpan1.un.org/.../public/.../unpan030231](http://unpan1.un.org/.../public/.../unpan030231). See the African Development Bank (afdb) findings on the topic titled, "Re-Orienting Public Management in Africa". [www.afdb.org/.../publications/00457497](http://www.afdb.org/.../publications/00457497)

<sup>36</sup> Thomas L. Friedman, *The Lexus and the Olive Tree* (Anchor Book, 2000)



NERC itself has become the first public institution in Nigeria to comply with the requirement of the FOI Act in order to be a credible enforcer of the disclosure rules in the FOI Act.

The dilemma of getting caught between being a world class regulatory organization in tune with global best practice and being trapped in the prevailing bureaucratic public sector 'Business as Usual' setup is reduced by the tendency of African governments to subscribe to different regimes of transparency and accountability, thereby committing regulatory agencies to integrity of decision making. The wise regulator, while still being drip-fed by the public sector bureaucracy can invoke the requirements of these legal and institutional regimes to break away from 'Business as Usual' and stride towards 'global best practice. The ability of the regulator to become transparent and accountable is not determined solely by its denomination in statute as an independent and autonomous regulator. It is not also determined by policy statements and institutional designs alone. The macro institutional settings and the reality of fiscal insolvency constrains the autonomy and independence of the regulator. But Freedom of Information laws and such other legal transplants can help the regulator eat his cake and have it. By presumably fulfilling the requirements of these laws, the regulator can remain embedded in the bureaucracy of the state and still be sufficiently autonomous and transparent in its regulatory actions.

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