

# EFFECTIVE REGULATORY INSTITUTIONS & SOCIAL SAFETY NETS

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# I. Why Regulation?

- Key to Broader Sector (& government) Restructuring
  - Decentralized economic regulation (out of the Ministry) through separation of policy, regulation and operation
  - Key factor for investment
  - Balance utility/consumer/govt. interests
- Transparency and Public Participation
  - Reduce corruption/increase good practices
  - Open process for reg/utility accountability

# I. Why Regulation? (Cont.)

- Energy and Water Regulation: similarities and differences
- Why USAID Assistance?
  - Comparative advantage
  - Cross-cutting impact on economic growth, democracy and social portfolios
  - Investment and private sector participation
  - Potential for regional linkages
  - Low resource-high impact on infrastructure

## II. The Context for Regulation

- The Regulation-Social Safety Net Nexus:
  - “The tariff increases must go in tandem with social safety nets. If you don’t put them in place at the same time, there will be a backlash.”  
Jean Lemierre, President, EBRD
- Sector Reform: Restructuring, commercialization, competition, Public Private Partnership (PPP)
- Financial Problems
  - Company losses and system disinvestment
  - Government Budgetary Drain: national and municipal
  - Balance of Payments: Energy imports & debt

## II. The Context for Regulation (cont.)

- Economic Issues
  - Cost of poor service for economic growth
  - Impact on investment environment
- Social Issues
  - Tariffs and vulnerable households
  - Non-payment and discontent with reforms
- Political Issues
  - Corruption/lack of transparency/no public participation



# III. Characteristics of a Sustainable Regulatory Body

- Autonomy, Authority, Accountability, Ability (AAAA)
  - Autonomy
    - Appointment of Commissioners
    - Exemption from Government Salary Rules
    - Financing—License Fees vs. On-Budget
    - Removal from Office for Cause Only



# III. Characteristics of a Sustainable Regulatory Body (Cont.)

## – Authority

- Full Tariff Approval Authority
- Issuance of Licenses
- Electricity Market Role
- Data Collection, Monitoring and Enforcement

## – Accountability

- Public Participation and Transparency;
- Annual Report and Audit
- Appeal of Decisions to Courts Only (or Intl. Arb.)



# III. Characteristics of a Sustainable Regulatory Body (Cont.)

## –Accountability (Cont.)

- Budget Review
- Code of Ethics
- Removal from Office for Cause Only

## –Ability

- Capable Trained Staff
- Procedures and Management
- Sound Tariff Methodologies and Prices
- Licensing Practices
- Participation, Monitoring and Enforcement





# IV. Key Steps in Regulatory Development

- Sound Legal Framework
- Organization Structure/Staffing
- Priority Functions Developed: Tariffs and Licenses
- Additional Functions
  - Public Processes (Hearings, decisions, etc.)
  - Regulatory Reporting/Monitoring
    - Tariff formulation
    - Quality of Service (QoS)
    - Licensing
    - Identification of Abuses

## IV. Key Steps in Regulatory Development (Cont.)

- Oversee Development of Competitive Market and Role in Privatization
- Harmonization for Regional Market Development
- Benchmarking for continued improvement
  - Independence, Information Access, Security of Supply; Market Operation and Monitoring; Resources and Capacity; Core Regulatory Procedures; International Activities; Enforcement

# V. Lessons Learned

- Regulatory Development: Central to successful reform
- Commissioners and Staff Turnover: Training and professional development in on-going
- Regulatory Complexity: Increases with Competition and Privatization
- Long Term: Systemic reform and institution building takes 5-10 years—engagement needed at different points.

## V. Lessons Learned (Cont.)

- Scope of Regulation: Stay focused—electricity initially and gas; then heat and for some water. Multi-sector?
- Host Country Support: Frequently from Ministries of Economy/Finance
- Donor Leadership (USAID): Critical (initially and over time); leverage needed
- Change Agent: One person can make the difference

## V. Lessons Learned (Cont.)

- Efficacy & Government Interference: Regulation isn't understood; need dialogue with government/media
- Ebb and Flow: Progress not in a straight line; can vary engagement
- “Applied” Assistance: blended approach—direct technical assistance; regional networking; and U.S. Partnerships



## V. Lessons Learned (Cont.)

- Regional Regulatory Network: Efficient and effective complement to mission bilateral programs, e.g., training and professional development (see Energy Regulators Regional Association [www.erranet.org](http://www.erranet.org))

# Energy Reform & Social Safety Net Approaches

- The Regulation-Social Safety Net Nexus:
  - “The tariff increases must go in tandem with social safety nets. If you don’t put them in place at the same time, there will be a backlash.”  
Jean Lemierre, President, EBRD
  - Historical mismanagement of utilities
  - Sector reforms of unbundling, commercialization and privatization mean:
    - **Enforced collections**
    - **Significant tariff increases for investment and operations**



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# Social Safety Nets

- **Social Safety Nets** are non-contributory transfer programs targeted in some manner to the poor or those vulnerable to poverty and shocks. Social Safety Nets play a well-recognized redistributive role which is supported strongly by moral philosophy, expressed in many different ways. (World Bank)
- Social Safety nets are a social obligation, essential for reform success, and politically smart.





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# Three Approaches to SS Nets

- Social Assistance Payments
- Social Tariffs
- Energy Efficiency

# Option 1: Social Assistance Payments

- Conventional social safety net
- Immediate relief
- Different ways to disburse:
  - Bundled vs. unbundled direct cash payment to household
  - In-kind transfer to utility
  - Voucher programs
  - Reimbursement

# Social Assistance Payments (cont.)

- Targeting
  - Basic means testing
  - Burden limit
  - Normative consumption burden limit
  - Consumption earmark from guaranteed minimum income (GMI)
  - Proxy testing



# Social Assistance Payments-Armenia Proxy Means Testing Case Study

- Poverty family benefits: a bundled social assistance program introduced during increasing prices
- Assigns point value to independent variables
  - Social risk status
  - Number of family members incapable of working
  - Residence location
  - Housing situation
  - Family income
  - Presence of car, private business



## Social Payments--Pros & Cons

- |  |  |
|--|--|
| <ul style="list-style-type: none"><li>• Immediate, targeted relief<ul style="list-style-type: none"><li>– Cash in hand or prepaid services</li></ul></li><li>• May stimulate payment culture<ul style="list-style-type: none"><li>– Assuming metering and strict disconnection</li><li>– Receipt based programs</li></ul></li><li>• Avoids market distortion<ul style="list-style-type: none"><li>– Ability to cut subsidization</li></ul></li></ul> | <ul style="list-style-type: none"><li>• Costly<ul style="list-style-type: none"><li>– Generosity, coverage, duration of benefit</li></ul></li><li>• Difficulty in targeting and administration<ul style="list-style-type: none"><li>– Dwelling size and income have insignificant correlation</li></ul></li><li>• May hurt other social programs<ul style="list-style-type: none"><li>– Crowding out of broader social programs possible</li></ul></li></ul> |
|--|--|

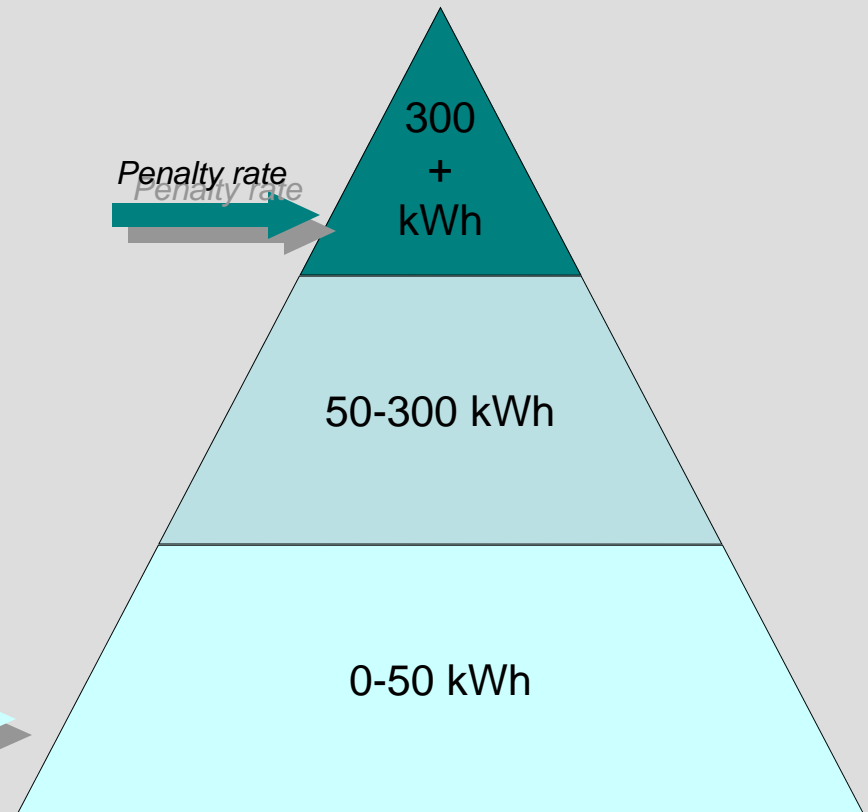
# Option 2: Social Tariffs

- Lifeline Tariff: charge a concessionary rate for electricity and heat consumption up to a “lifeline” level that meets bare minimum needs.



# Example: Hungary

- Lifeline rate set 16% below middle block, penalty rate set 17% above middle block
- Poor received 20% of subsidy
- If had been 2 block, would have only targeted 16% and cost 35% more





# Pros & Cons

- Easy to implement
  - Targeting not necessary
- Transparent
  - Major cash exchanges limited to between govt. and utility
- High Coverage
  - Good as a short term solution

- Poorly Targeted
  - All subsidized in lifeline block
- Distortionary Effects
  - Energy Use
  - Utility Efficiency
    - Short-term political objectives by govt
- Costly
  - For government, utility, or other consumers?





# Option 3: Energy Efficiency

- Characteristics of residential sector in E&E countries:
  - Lack insulation in residential buildings
  - Poor building construction/aging
  - Incandescent versus CFC light bulbs
  - Energy efficient appliances expensive
  - Limited awareness on energy efficiency
- Residential Energy Efficiency reduces end-use demand, and therefore utility bills.

# Technology

- **Heat meters and control devices**
  - Communal heating: heat cost allocators and radiator valves
  - Electricity/natural gas: timers, thermostatic controls
- **Building Upgrades**
  - Replace dilapidated doors, windows, roofs; CFLs instead of incandescent bulbs
- **Weatherization**
  - Caulking, sealing, reflective sheet behind furniture, furniture placement
- **New Infrastructure**
  - Automated lighting/doors, new building boiler



# Administration

- **Funding:**

- Government budget: federal or municipal
- Private sector/individual level
- Donor grants/loans



- **Targeting:**

- Can't get perfect
- Usually base off of statistics of when buildings were constructed

- **Implementing:**

- NGO, Contractor
- Train domestic energy efficiency teams?



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# Case Study: Lithuania Multifamily Housing Building Modernization

- Higher tariffs in 2004
- Shared stake between GOL and Housing Associations
- Heat cost savings averaged 60% or approx \$32/household/year
- Subsidy payments reduced by 40%





# Pros & Cons

- **Cost effective**
  - One time cost
- **No market distortion**
  - Billing consumption based
- **Environmental benefits**
- **Promotes conservation and payment culture**
  - Metering leads to understanding of bills

- **Strong institutional framework needed**
  - Govt, NGOs, donors, housing, industry
- **Targeting difficult**
  - Intermixed neighborhoods
- **Lack of technical and administrative skills**

# Output-Based Aid Approaches

- Innovative and flexible mechanism to harness private sector delivery of basic infrastructure and social services to the poor
- Focused on water, telecom and transport
- Contracting out provision of services with payments after delivery of specified outputs
- Combines performance contracts and subsidies
- Full cost recovery tariffs not always feasible
- Transitional subsidies and on-going subsidies