

Conference: Which Competition Policy for  
Regulated Industries? Governance and Sector-  
Specific Perspectives

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## The Evolution of Regulatory Frameworks & Techniques



Ioannis Lianos & Javier Tapia  
Centre of Law & Economics  
UCL  
Istanbul, Sept. 2008

## Overview

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- ❑ Introduction: A brief deregulatory history
- ❑ What has been going on?
- ❑ European Regulatory Framework
- ❑ Regulation in the 21<sup>st</sup> Century
- ❑ Conclusions: Which implications for competition policy?

## The deregulatory (hi)story

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- ❑ The 'Great Transformation' of public utilities regulation
  - From Public Enterprise to Privatisation
    - ! But still great importance of SOEs
  - From Vertical Integration to Liberalisation
    - ! But many business groups with interests in different segments of the market or in different markets

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## The Outcome

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- ❑ The 'textbook' architecture of desirable regulatory reformed industries
  - Private ownership
  - Vertical separation
  - Competitive wholesale markets
  - Competitive retail markets
  - Regulation of network services
  - Incentives for quality of services

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## The (de)regulatory debate

### ☐ Centred on two themes:

- 'Micro'-concerns: focused upon pricing issues
  - ✓ Principal-Agent model & Mechanisms Design approach
  - ✓ Price-cap v. Cost-of-Service regulation (COS)
  - ✓ Access issues: pricing (particularly ECPR) & discrimination
  
- 'Macro'-concerns: focused upon
  - ✓ Credible commitment
  - ✓ Institutions (New Institutional Economics) – incomplete contracting

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## 'Wrapping-up' (I)

### ☐ Regulatory Contract

- A common fictitious *theoretical* framework to study the regulatory relation
- Regulation as a long-term (incomplete) contracting problem

### ☐ A number of different regulatory arrangements arise

- ✓ Public enterprise
- ✓ Discretionary regulation
- ✓ Concessions
- ✓ Private contracting



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## 'Wrapping-up' (II)

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- ❑ Institutional contractual arrangements depend upon country-specific factual conditions and history
  - Regulatory techniques differ
  - Regulatory institutional approaches differ
  
- ❑ Different roles assigned to Competition Law and regulation play a key role
  - Defining the extension of the regulatory relationship

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## Key Ideas

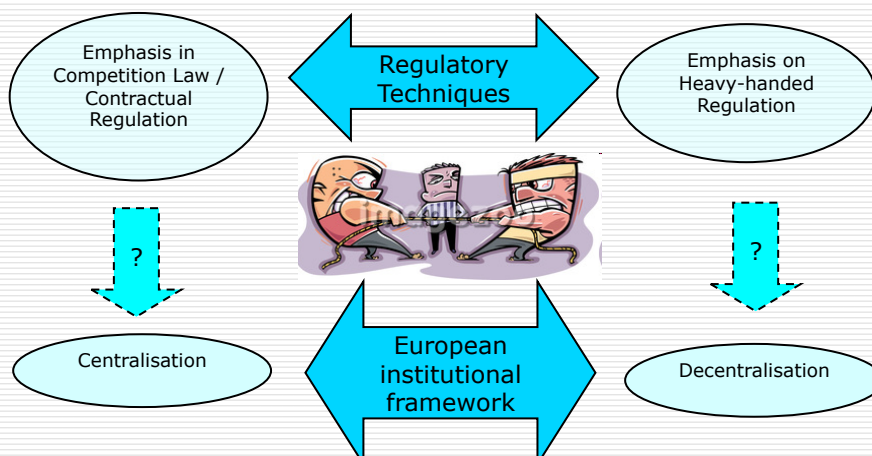
- ❑ Transformation of the regulatory frameworks is moving in two directions:
  - Transformation of regulatory techniques
    - ✓ More contracting out, incentive regulation & market-based tools
    - ✓ Tension between poles: State provision by public undertakings v. more reliance on markets
  - More European regulation
    - ✓ 2<sup>nd</sup> and 3<sup>rd</sup> Energy Packages; 'Regulation by Cooperation' (e.g. networks of regulators); Greater Centralisation (?)

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## Counteracting forces



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## Emphasising Market-Based Approaches

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- ❑ Geographical scope:
  - European approach
  - Active involvement of the Commission in utilities sector
    - ✓ Use of Directives & Guidelines
    - ✓ Competition Law litigation
  - New Zealand 'light-handed' approach (changing?)
  
- ❑ Sector scope:
  - ☎ Telecoms

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## Emphasising Discretionary Regulation

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- ❑ Geographical scope:
  - US experience
    - ✓ Considerable powers to federal regulators
  - The UK
    - ✓ Licences system (contractual approach)

*Regulation is present even in competitive segments  
of the markets!*

- ❑ Sector scope:
  - ⚡ Electricity
  - 💧 Water

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## Redefining powers inside the regulatory relation (I)

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### □ Role of Regulators

- Clear task: creation & maintenance of competitive markets
  - ✓ i.e., maximise competition among rivals (to protect consumers)
  - ✓ *Compare* pre-deregulation role: comprehensive overseeing of the industry
- Proactive role
  - ✓ E.g., role of the Commission & NRAs in the UK
- High discretion
  - ✓ Highly technical regulatory frameworks

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## Redefining powers inside the regulatory relation (II)

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### □ Role of Courts

- Few substantial involvement in disputes
  - ✓ Both at national & European levels: few major cases (with important exceptions though –e.g., Corbeau)
  - ✓ US experience: ‘administrative phase’ after *Hope*
- Courts not really aware of regulatory problems
  - ✓ Regulatory frameworks ‘too technical’
  - ✓ Passive role

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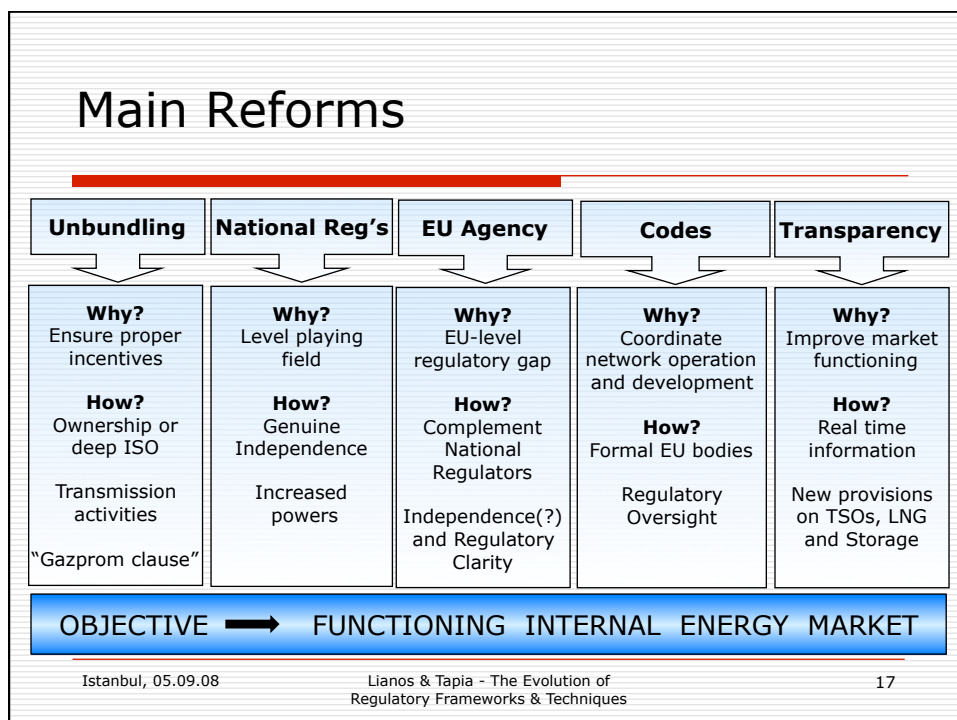
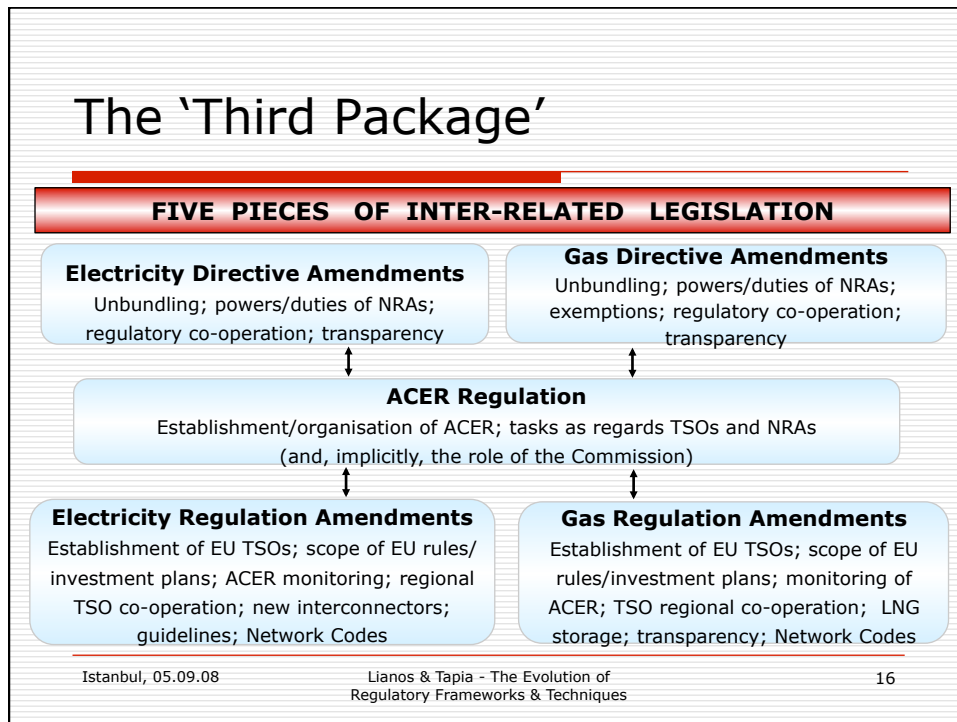
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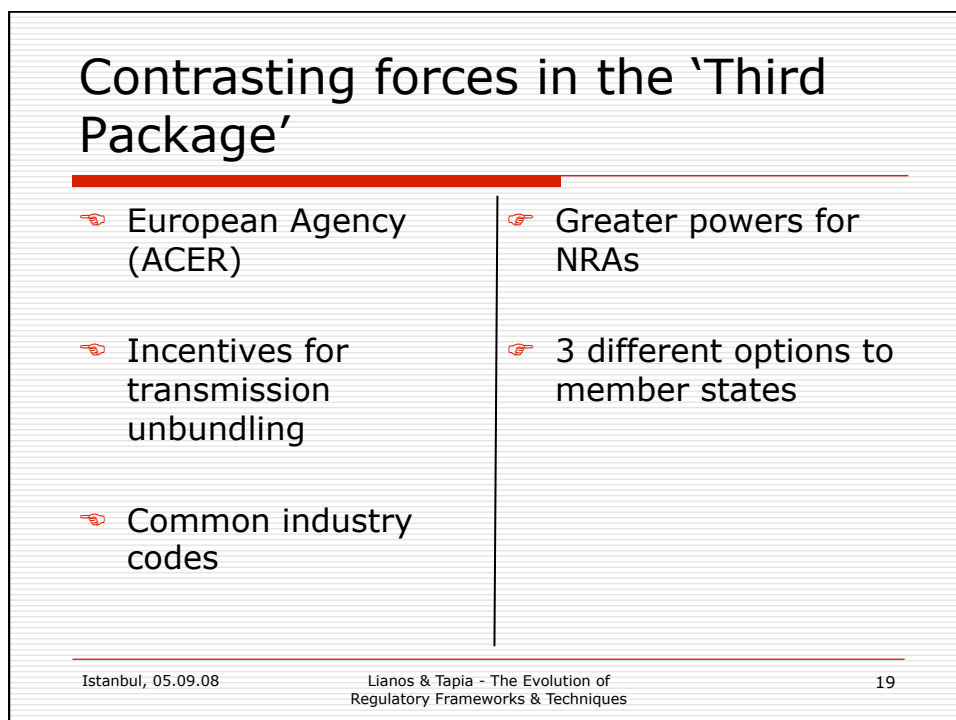
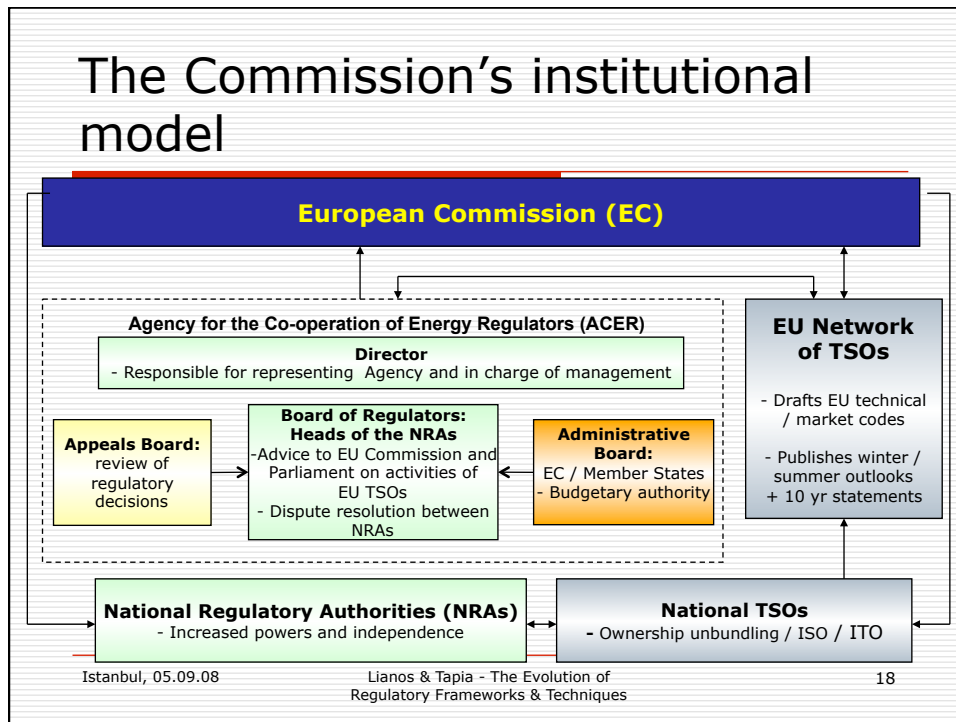
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## Decentralisation v. Centralisation

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- ❑ The European 'golden oldie'
  - E.g., antitrust modernisation
  - Objective(?): *Controlled* decentralisation
- ❑ Tendency in utilities not yet clear
  - High powers for NRAs... BUT ...European regulatory oversight or (even) direction
  - (EC) 'Regulatory antitrust'... BUT ...still great national regulatory intervention.
- ❑ Example: the 'Third Energy Package'





## A bit of 'physics'...



### □ The physics of the Third Package.

- Newton's First Law of Institutional Reform:
  - ✓ Institutions at rest tend to stay at rest, and institutions in motion tend to stay in motion following a set direction, until acted upon by an unstable outside force
- Centrifugal and centripetal forces acting:
  - ☞ NRAs were at rest
  - ☞ Third Package has set them in motion
  - ☞ Without equal and opposite centralising force, object will tend to fly out of orbit

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## Facts

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- ❑ No role for new ideas (?)
- ❑ 'Regulatory antitrust'
  - Possibility of both *ex ante* and *ex post* controls
  - Revival of 'margin squeeze' cases
    - ✓ DT, Telefonica (EC) / Albion (UK) / LinkLine (US)
- ❑ More regulation of 'inputs' instead of 'outputs'
  - Even more pre-eminence of access issues

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## Facts

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- ❑ Change in role of parts in the regulatory relation
  - Economic expertise of Courts has increased
  - New regulatory objectives (e.g. in energy: security of supply, sustainability...)
  - Hybrids structural reforms
  - Reactive role for regulators
- ❑ The upshot: A round trip?

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## Our Predictions

- ❑ Regulatory relation:
  - Reactive role of regulators would lead to less and less regulatory intervention
  - Major interventions by courts
  
- ❑ Regulatory techniques:
  - More contractual approaches to regulation, *plus*
  - Increased role for *ex post* revisions (without substituting regulation)
  
- ❑ Regulatory framework:
  - Centralised approach (mainly through guidelines)
  - A need for different theoretical model?

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