Functions, Formulas and Fiction

Regulation in the next 10 years

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Outline

• Challenges in regulation
  – Technical
  – Adaptive
• Addressing adaptive challenges
• Regulatory system
• Addressing change in the system
Survey

1. Which is most likely to become the driving issue for change in energy policies in Barbados?
   1. Environmental concerns
   2. Energy costs
   3. Technology change
   4. Dependability
Survey

2. Which of the following, if increased 25 percent, would make the greatest impact for good regulation in Barbados?

1. Independence of the FTC
2. Business community assistance to FTC
3. Consumer education
4. Political oversight of FTC
3. Which of the following represents the greatest energy challenge for Barbados in the next five years?

1. Energy costs
2. Smart grid
3. Environmental regulations
4. Efficient energy use
5. Adapting to unforeseen circumstances
Technical Challenges in Regulation

• Rate reviews (accountants, economists, engineers, lawyers)
  • Rate base (assets, depreciation, etc.)
  • Cost of money (debt and equity costs, gearing, etc.)
  • Disallowances (prudency, known and knowable, etc.)
  • Public input (hearings, comments, etc.)
Technical Challenges in Regulation

- Interconnection arrangements (lawyers, engineers, economists)
  - Contract design
  - Evolution with next generation networks
  - Cost studies
  - Dispute resolution
Technical Challenges in Regulation

- Economic incentives (economists, lawyers, accountants)
  - Price cap design and review
  - Earnings sharing
  - Benchmarking
  - Regulatory lag
Technical Challenges in Regulation

• Renewable energy (engineers, biologists, economists, lawyers)
  – Renewable portfolio standards
  – Technical feasibility
  – Economic feasibility
  – Distributed generation interconnection and pricing
  – Market structure
Technical Challenges in Regulation

• Environmental regulations (environmental scientists, engineers, economists, lawyers)
  – Standards setting
  – Cap and trade
  – Monitoring and enforcement
  – Rate treatment of costs and revenue
  – International agreements
Technical Challenges in Regulation

- Telecommunications competition (economists, lawyers)
  - Mix with regulation
  - Competition assessment
  - Impacts of technology change
  - International impacts
  - International agreements
Technical Challenges in Regulation

• All require
  – Technical sophistication
    • Lawyers, engineers, financial analysts, accountants, economists, scientists, etc.
      – That are well educated and well trained
    • Analytically complex, but known
      – Legal authority
      – Legal processes
      – Policy direction
What would regulation look like if it were ready for these challenges?

- What performance is measured and monitored?
- What new incentives are in place?
- Whose investment is protected?
- Whose prices are protected?
- What experiments are in place?
- How are commitments honored?
Regulation is more than technical challenges

- Renewable energy sources
  - Who will bear the costs?
  - What will be the new environmental challenges?
- New technologies
  - Who will bear the risks?
  - Whose jobs will be impacted?
- Political pressures
  - Who will take political risks?
Regulation is more than technical challenges

- Economic incentives
  - Will the government keep its commitments?

- International relations
  - How should international pressures impact market, environmental, and price decisions?

- Competition
  - Will the government tolerate dynamic markets?
## Technical vs. Adaptive Challenges

<table>
<thead>
<tr>
<th></th>
<th>Problem definition</th>
<th>Solutions</th>
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<tbody>
<tr>
<td>Technical</td>
<td>Known. People ready for solution</td>
<td>Developed by experts</td>
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<tr>
<td>Adaptive</td>
<td>People disagree on existence or definition</td>
<td>Require learning new realities and losses</td>
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Addressing Adaptive Challenges

- “Trouble makers” surface the problem
- Dialogues to investigate and learn
- Experiments to test hypotheses
- Stakeholder engagement to distribute losses
What would adaptive regulation look like?

• Roles and relationships
  – Authority, accountability, communication
  – Clear, but experimental

• Three juxtapositions
  – Next, not best
  – Why, not what
  – Leadership, not leading
Regulatory Governance Model

Relationships for
Price Setting
Quality
Market Conduct

Citizens

Policy Makers

Commissioners

Regulatory Agency

Operators

Adapted from “The Imperfect Board Member”
Regulatory Governance Model

Citizens

Policy Makers

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Authority Scope

• In general, higher level groups hold lower level groups accountable for results
  – Without managing how results are achieved
  – With consideration for circumstances
Authority Scope

- **Policy makers**
  - Reflect on outcomes
    - What is the system supposed to produce?
    - Why does it or why doesn’t it?
  - Respect citizen expectations
    - Long run and short run
  - Select commissioners
  - Define and refine vision and mission
    - Evolving circumstances, but long-lived investments
Authority Scope

• Regulators
  – Establish prices, service standards, and market rules
  – Enforce decisions

• Operators
  – Determine means to achieve service vision subject to regulator decisions
Accountability for performance

• Operator rewarded/punished based on
  – Costs and price performance
  – Investment
  – Service quality

• Regulator held accountable for sector performance and for system performance
  – Prices and services
  – Stakeholder engagement
Regulatory Governance Model

Citizens

Policy Makers

Commissioners

Regulatory Agency

Operators

Communication

Authority

Accountability

Adapted from “The Imperfect Board Member”
Communication Line Exceptions

Citizens

Policy Makers

Commissioners

Regulatory Agency

Operators

Impacts Explanations

Policy ideas and feedback

Within the context of the proper role

Adapted from “The Imperfect Board Member”
Challenges to the model

• Minority voices
  – How are less powerful citizens heard?

• Formal vs. informal rules
  • Formal rules only do so much
  • How to honor informal agreements?
    • Transparency
    • Difficult conversations
How do we adapt our system?

Change is a continuing condition: The future holds more unknowns than it does certainties. “Reset” means that we develop fresh perspectives and knowledge about the future, while holding in trust the wisdom of the past.

1. Focus on Next practices, not Best practices.

2. Focus on Why rather than on What.

3. Focus on Leadership, not on Leading.

(Mark Jamison and Araceli Castañeda, 2009)
1. Next practices, not best practices

Best practice is about imitation (following in someone else’s footsteps). A focus on next practice is needed when we are going into areas where no one has gone before.

2. Focus on *Why* rather than on *What*

When we ask ourselves “What should we do next?” we emphasize practice. But the practice needs a foundation, basic principles, and values.

Ask “*Why* have certain practices or why have experiments been successful or unsuccessful?” so that we analyze our underlying priorities and our context. We learn, keep what is important, and discard what holds us back.

Collins, 2009. *How the Mighty Fall and Why Some Companies Never Give in*
3. Leadership vs. Leading

A leader provides direction (when the right direction is already known).

Reflection

Consider your answers to...

• Driving issue for change
• Greatest impact for good regulation
• Greatest energy challenge for Barbados

What is the most important thing for you to accomplish in 2010?
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