

## Successful deregulation and privatisation

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The theory underpinning policies of deregulation and privatisation is that, except in particular cases, freely operating markets can be expected to deliver better welfare outcomes than regulated markets and than direct government production or production by government owned enterprises. It is arguably the case that just which kinds of goods and services are better left to unfettered markets and which kinds are better produced with some measure of government intervention will vary from country to country and over time.

Even when deregulation of a particular market or privatisation of a government enterprise is indicated, the conditions must be right if government failure is not simply to be replaced with market failure. The main message here is that the sequence must be right. Ideally deregulation and privatisation should follow:

- development of social safety nets
- sound companies regulation
- effective general consumer and competition regulation
- good corporate governance and auditing standards
- establishment of an active civil society consumer movement, shareholders movement and independent media to monitor companies

Deregulation and Privatisation are often thought of as coupled processes, but they should be seen as policies implemented for quite different reasons.

Deregulation might be indicated where regulation is presenting a barrier to entry and is not delivering a public benefit e.g. maintaining essential safety standards or continuity of supply.

Privatisation on the other hand might be indicated where analysis shows that a service or good can be produced or supplied more efficiently by private enterprise than by government. There are many reasons why this might be the case such as access to capital and greater workforce flexibility. However benefits of government production/supply are sometimes more subtle and should not be underestimated. These might include greater potential for long-term planning for example and things which are not always straightforward to regulate such as, maintenance of higher consumer safety and environmental protection standards.

It is perhaps better to think in terms of regulatory review and reform rather than deregulation. This is because no market should be seen as being able to be treated on a "set and forget" basis. A regulatory (or deregulatory) regime that might be appropriate for the circumstances (economic, technological, social) of a particular time might become inappropriate at a later time. It must be seen as a never-ending process.

The same might be true of privatisation, but reversing privatisation or re-nationalisation is much more politically difficult. It is hard to close the door after the horse has bolted so it is very important to ensure the criteria for successful privatisation are met and that the required regulatory arrangements are in place before it is effected.

It is sometimes the case that corporatisation of government enterprises might achieve many of the objectives without the risks involved in full privatisation.

Other options include:

- Partial privatisation
- Vertical disaggregation
- Horizontal disaggregation

Privatisation of a government enterprise may reasonably be considered if the market in which it operates does not already have competitors, but is readily contestable. If there are no tariff or non-tariff barriers such contestability might be via international trade. Whether or not a particular market is readily contestable needs very careful analysis. Sometimes barriers to entry are quite subtle perhaps even related to cultural factors.

It is also critical that there are no asymmetry of information problems which cannot be dealt with either by general consumer protection regulation or specific market regulation.

To reiterate a point already made, even if the conditions appear right for privatisation it still might be the case that maintaining an enterprise in public ownership is worthwhile if it can operate to compete down prices and compete up quality and to set standards for consumer, worker and environmental safety and generally maintain ethical behaviour in a market.

It is also possible that, while at the time privatisation is being undertaken conditions are appropriate, circumstances change, perhaps as a result of technological developments, to make the market in question dysfunctional. It could therefore be important to retain the power to readily institute price or quality controls without the need for new legislation. In some instances it could be necessary to re-institute a comprehensive regulatory regime. A general power to take action where monopoly power is exercised could be very beneficial. Under European law there is the power to take action in respect of monopoly pricing for example.

A significant issue arises where an enterprise to be privatised is required to meet community or universal service obligations, for example the provision of a basic telephone service to all communities. Changes in technology and/or social change might alter what is considered to be a basic telephone service. It is more straightforward for a government to require a public enterprise to raise the standard of a universal service than to regulate private enterprises to do so. The political power of a privatised enterprise could be too great for the

government to regulate it in the public interest – especially if the privatisation has allowed it to become part of a major trans-national corporation.

In many privatisation cases, especially where natural or near natural monopolies or significant positive or negative externalities are involved, special arrangements will be needed such as:

- a special industry regulator
- support for new entrants
- a system, perhaps non-state, co-regulatory, for mediation and adjudication of complaints/disputes
- support for specialist consumer advocacy organisations

The regulatory regime, including a non-state, co-regulatory complaints/disputes system, can be funded from within the industry thus relieving the burden on the public purse. It is also possible to have the specialist consumer advocacy organisation funded from within the industry. One sound system that has been used in the USA for public utilities is to give customers the opportunity to opt to pay a small levy on their account which the company passes on to the advocacy organisation. In Australia government is funding such advocacy organisations.

There is a risk of a special industry regulator becoming too close to the industry and making decisions more in its interest than in the public interest, a phenomenon called regulatory capture. An effective way to avoid this is for a general consumer/competition regulatory agency to have economy-wide authority, so that it can intervene in the regulation of any industry to maintain general regulatory standards. To ensure effective collaboration between the general regulatory agency and special industry regulatory agencies the chiefs of the latter can be ex officio members of the board of the general agency and vice versa.

Finally, it is important to note that getting the right price when selling a public enterprise might be difficult. Many privatisations around the world have sold short the public, the owners. Share prices for newly privatised enterprises have often risen steeply. On the other hand there is the temptation to arrange competitive privileges to boost the sale price. This of course results also in the public being sold short through the extraction of economic rent by the new private enterprise.

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