

private infrastructure deals. It does so in a way which minimizes the potential distortions of such actions and at minimal cost to government.

A number of outright privatizations may be a useful and even necessary way to sustain reforms in Colombia's infrastructure sectors. As well as having numerous benefits in terms of increasing efficiency, reducing the fiscal drain and improving the quality of service, this could also ease the financing of new infrastructure.

Private operations are, however, best provided in a competitive framework that promotes efficiency, quality of service and cost-reflective prices. The Colombian government has been extending competition in a number of infrastructure sectors, notably electricity and telecommunications. The competitive framework within which these services are provided is critical. In electricity, for instance, the role of the electricity market and competition in supply are likely to lead to pressure to rebalance tariffs and put pressure on inefficient generators and distributors. As the market system evolves, privatization of existing generation plant and distributors will be important, the former to create a group of companies that will be more comfortable with investing than completely new entrants to the market and the latter to create credit-worthy entities who can pay for the power they receive and contract with new and existing generators.

The question of government actions in a 'transitional' phase until the private sector becomes the dominant operator of services is a difficult one. Some forms of intermediate step such as mixed companies or 'subconcessions' between public and private companies can be problematic. Another complex issue is the granting of government guarantees and other forms of transitional support until the private sector becomes fully established as the dominant operator. The provision of some guarantees, of items which are the government's responsibility, may be important in the short run.<sup>24</sup> In the medium term, however, the more important condition will be the divestiture of the remaining elements of the systems which are forcing the need for guarantees, i.e. in electricity the privatization of distribution will help to eliminate the need for future public support of private generation projects. In some sectors, notably toll roads, government financial support may continue to be necessary to launch projects and the key will be to minimize the potential distortionary impact of this support.

Another part of the transitional phase is the likely increase in the number of 'mixed' companies where the shareholdings are part public and part private. Empirically these have proved to perform badly, even in comparison with public companies. The government can, however, take actions that can minimize the negative effects through public share offerings as part of the divestiture process, setting up a trust to administer the government's holdings at arm's length and establishing a timetable for divestiture of the remaining shares.

In a number of cases the private sector has entered the market through 'subconcessions', contracts written between public companies and private entities. The government should try to ensure that over time private operators face more regulatory and market risk and that public companies are not used as 'cushions' to shield private operators from these risks.

The government in this transitional phase will also face significant issues regarding 'competitive neutrality' between public and private operators. The government of Australia has systematically examined this issue and come up with a series of guidelines to ensure that public and private operators compete fairly with one another. Some of the useful measures that the Australian government is implementing include rules ensuring regulatory neutrality, ensuring that public entities earn returns equivalent to private companies and creating an ombudsman to allow private operators to complain if they feel the public companies are using their public status unfairly. These may be useful guidelines for the Colombian government to analyze in sectors where the public and private sectors are likely to compete.

Another major challenge the Colombian government faces is in providing assistance to municipal governments in the privatization process. In some sectors, notably water and sewerage, the role of the municipality in the process of private involvement will have to be strengthened through central government support. The central government can assist by:

- providing a 'one-stop shop' for municipalities to receive support in the process of privatization; and
- ensuring that financial support does not distort the municipalities' decisions to seek private participation.

The municipalities could help themselves through relying on domestic capital sources, merging their systems either before or after divestiture or allowing municipal systems to join existing adjacent concessions. In the short run, larger municipalities are moving faster than smaller ones, but hopefully positive demonstration effects will encourage reluctant municipalities to follow suit. Another important factor will be ensuring a better alignment of regulatory responsibilities between the municipalities and the central government.

Regulation of infrastructure services has proved to be a difficult task. In the short run, the introduction of competition seems to actually increase the amount of regulation, although with the hope that once viable competitors are established and the ground rules laid out the need for regulation will diminish or disappear. Colombia has gone some way towards developing the legal and regulatory framework for private infrastructure, but still has difficult challenges to face in implementing regulatory rules for competition in power and telecommunications and regulating residual monopolies in all infrastructure subsectors. In the longer run, with more narrowly targeted objectives, greater independence to regulatory agencies could be a way to increase the confidence of private investors in the stability of the regulatory framework. This would remove the existing conflicts of interest held by the sectoral ministers *vis a vis* the regulatory bodies as well as diminish the risk of inappropriate short-term political interventions.

## Notes

<sup>1</sup> This note touches upon electricity, telecommunications, water and sewerage and toll roads. Other important infrastructure sectors such as ports, railways, gas are excluded from the paper (other than as examples) in the interests of keeping the paper manageable.

- 2 National Council for Economic and Social Policy
- 3 The line between regulation and policy-making is a fine one. Generally the line is drawn between policy-making (which is conducted by government) and the implementation of policy which is the act of regulation (and can be conducted by regulatory authorities). What actions are undertaken as acts of policy-making as opposed to regulation vary from country to country. This issue will be analyzed in section V.
- 4 Project Finance International, March 1996.
- 5 CONPES 2928.
- 6 Resolución No. 86, Comisión de Regulación de Telecomunicaciones (CRT).
- 7 With a fixed entry fee of US\$150 million new entrants have an incentive of getting as close as possible to the mark of 35% of telephone lines. However, no company can ever have more than 40% of all lines.
- 8 Also from the Fondo de Comunicaciones for 10 years.
- 9 The supplier has to pay a charge to the local distribution company for the use of its wires in supplying the power to the customer.
- 10 Mammonal was financed through contracts with a number of industrial customers around Cartagena.
- 11 Galal, Jones, Tandon and Vogelstang (1994).
- 12 Port privatization has led to port operating costs falling from around US\$21/tion to around US\$6/7 per ton. Ship turnaround has fallen from ten to two days.
- 13 See section VI on how to address service for low income population.
- 14 For a lengthier discussion of these issues see Chertan (1996).
- 15 The Government is currently designing adequate financial instruments for local and international refinancing, put options, and liquidity guarantees. This instruments are to be implemented through a infrastructure financing facility that will also address risks like sovereign and political risks in 1998.
- 16 Boudman and Vining (1989).
- 17 Many of the details of this section were taken from 'PSP in the W&S Sector: An Overestimated Harvest? Lessons From Six Experiences in Developing Countries' by Daniel Rivera.
- 18 Eastern Europe has numerous examples of this form of trust. In the UK, the government stated in the Initial Prospectuses of its privatized utilities that it did not intend to influence the commercial activities of privatized companies through its residual shareholding. In Bolivia the shares of the 6 largest public enterprises that were capitalized are held by an international custodian and the shares are managed by private investment managers aiming at maximizing risk adjusted returns.
- 19 Formally it is still only INVIAS guarantee but the Government guarantees that INVIAS budget will have enough funds to honor its liabilities.
- 20 This is presupposing that the government puts in place a program to price and account for guarantees in its budget, a task which the government is undertaking and expected to have in place in 1998.
- 21 Government of Australia (1996).
- 22 In some countries, such as the UK, policy is associated with major changes in legislation. In fact, in the energy sector, after the privatization and establishment of regulatory agencies, the sector ministry, the sectoral Department of Energy was abolished and its residual functions were transferred to the generalist Department of Trade and Industry.
- 23 The classification of the strata is on the basis of geography and not on actual income.
- 24 It will be important to price, account and budget for these guarantees in the government budget. The Colombian government is in the process of doing this.

## References

BOARDMAN, A. and A. R. VINING (1989). "Ownership and Performance in Competitive Environments: A Comparison of the Performance of Private, Mixed and State Owned Enterprises". *Journal of Law and Economics* 32, April, 1-33.

- CHERIAN, SAMUEL (1996). "Stock Market and Investment: The Governance Role of the Market". *Policy Research Working Paper*, Series number 1578, March, World Bank.
- CHRISTMAS, J. and DE ROOY (1991). "The Decade and Beyond: at a Glance, Water International, 16.
- CONPES (1995). "Participación del Sector Privado en Infraestructura Física", documento 2775, Consejo Nacional de Política Económica y Social
- CONPES (1997). "La Participación Privada en Infraestructura -Seguimiento", documento 2928, Consejo Nacional de Política Económica y Social, 11 de junio de 1997.
- COMISION DE REGULACION DE TELECOMUNICACIONES, Resoluciones Nos. 80, 81, 86, 87, and 88
- DUSSAN, MANUEL (1996). "Competitive Power Markets: The Colombian Experience", September 9th, Presentation to World Bank.
- EU (1994). "Infrastructure Development in Latin America", Economist Intelligence Unit, *The Economic*.
- ESTACHE A. (1993). "Decentralizing Infrastructure: Advantages and Limitations", *Working Paper*, World Bank.
- FOSTER C.D. (1992). *Privatization, Public Ownership and the Regulation of Natural Monopoly*, Blackwell, Oxford.
- FRISCHTAK, C., ed. (1993). *Regulatory Politics and Reform: A Comparative Perspective*, World Bank.
- GALAL, A., L. JONES, P. TANDON and I. VOGELSTANG (1994). *Welfare Consequences of Selling Public Enterprises: An Empirical Analysis*, Oxford.
- GOVERNMENT OF AUSTRALIA (1996). "Commonwealth Competitive Neutrality Policy Statement", Canberra, June.
- GUISLAIN, P. and M. KERF (1996). "Concessions - The Way to Privatize Infrastructure Sector Monopolies", *Public Policy for the Private Sector*, June.
- JACOBS and VON GERSDORFF (1994). *Building Regulatory Institutions: The Search for Legitimacy and Efficiency*, OECD.
- KLEIN, M. (1996). "Competition in Network Industries", *Policy Research Working Paper* 1591, World Bank, April.
- LANDIS, JAMES M. (1960). "Report on Regulatory Agencies to the President Elect", December, unpublished memo.
- MONTENEGRO, ARMANDO (1995). *Economic Reforms in Colombia: Regulation and Deregulation, 1990-94*, Economic Development Institute, The World Bank.
- OECD (1995). "Telecommunications Infrastructure - The Benefits of Competition", Paris.
- RIVERA, DANIEL (1995). "PSP in the W&S Sector: An Overestimated Harvest? Lessons From Six Experiences in Developing Countries", *Working Paper*, World Bank.
- WORLD BANK (1994). *World Development Report: Infrastructure for Development*.