

Executive Summary

Brazil has now entered a more advanced phase of economic development, with the need to strengthen the institutional foundations for a market-based economy. After a long period of state intervention, the country experienced a move towards liberalisation and privatisation in the early 1990s. The Real Plan (Plano real) created a more favorable environment for regulatory reform with greater economic openness, institutional reforms and stable inflation. The competition framework was modernised with the 1994 Law. In this context, a number of regulatory authorities were established.

Access to core services such as transportation, telecommunications, energy, and water significantly improves the human development index, and also lays the ground for future economic growth. These are critical inputs in the provision of goods and services and they significantly affect the productivity, cost and competitiveness of the economy. In Brazil, the hope was that further private sector participation in infrastructure would help to increase investment, improve performance and coverage, and facilitate access to services in a market context. Two key roles for the economic regulator in the Brazilian context are to minimise regulatory uncertainty, which can reduce investor confidence, and to stand out as an impartial and autonomous manager of the market players. Significant portions of the busiest highways were offered as concessions, improving conditions on those roads. The private sector took control of large portions of the telecommunications infrastructure which was modernised.

Regulatory authorities and the challenges of economic and social regulation

The new regulatory agencies (ANEEL, for the electric energy sector, and ANATEL, for the telecommunications sector) were created after 1996, inspired by international experience. Since 1996, ten federal regulatory agencies have been created: ANEEL (1996), ANATEL (1997), ANP for Petroleum (1997), ANVISA for Food and Drug Admission to the Market (1999), ANS for private health insurance (2000), ANA for water (2000), ANTAQ for ports (2001), ANTT for land transport (2001), ANCINE for the movie industry (2001) and ANAC for civil aviation (2005). In addition, the Administrative Council for Economic Defense (CADE) created in 1962, was transformed into an independent governmental body, with clear powers for competition policy enforcement with the new Law 8 884/94.

This review takes a closer look at regulatory governance in four sectors: Power with ANEEL, transport with ANTT, private health insurance with ANS, and telecommunications with ANATEL. These bodies are part of the framework for indirect administration, but are subject to specific legal regimes aimed at ensuring a greater level of independence. The power sector, where the State still has a major shareholder responsibility, differs from

other markets that are largely run by private operators. The private health insurance market is also different as it does not involve essential facilities or a network infrastructure.

Agencies have often contributed to improved economic and social outcomes. The private health insurance sector has been regulated, offering improved conditions for consumers, compared with the previous lack of regulation. Similarly, railroad transport and bus transport have improved. In the energy sector, corrections made to the regulatory framework and effective management of the new framework have helped to address the 2001 crisis. In terms of telecommunications, Brazil's achievements are largely consistent with its relative development, and it can boast significant penetration of mobile services.

However, the challenges of raising the rate of investment remain. In the energy sector, stronger economic growth may imply further pressures in terms of energy supply in the future. In this context, clear and stable priorities for diversifying power technologies will serve to offer a predictable signal for investors, particularly in relation to natural gas. An increased contribution of natural gas to energy supply depends on further major efforts to improve security and diversity of gas supply, but also in ensuring that corresponding efforts are made to the regulatory framework. The rationing of natural gas for some users has reappeared in the Southeast of Brazil, due to the sustained growth experienced in recent years. This illustrates the challenges of building infrastructure for diversified power supplies. Another issue which has emerged in this report is environmental licensing, as it can delay, sometimes for many years, authorisation for a new power facility. Providing true universal service is also a challenge in some sectors, such as telecommunications, where access to services remains an issue for significant groups of the population.

In terms of transport, Brazil is one of the world's top exporters of a number of agricultural and primary products that must be carried to the coast, but its domestic transport infrastructure is currently overloaded and unbalanced, which increases the costs of logistics. Many of these issues go beyond the pure mandate of the agency or its regulatory framework. A broader perspective is required, integrating the whole transport sector. Much of the hesitation around the new highway concessions reflected how difficult progress has been in this field and the agency faced the difficult task of resolving conflicting interests. The recent auction for highway concessions will apparently benefit Brazilian consumers through reduced tariffs. It is important that the result should not be undermined by further renegotiations.

Modernising the institutional framework for a market-based economy

In broader terms, after ten years of institutional experience, the macroeconomic situation has improved and the progress made by the sectoral regulatory agencies has also paid off. Regulatory risk has tended to decrease. There is also more widespread agreement on the need for further private capital, as was illustrated for the first time in a decade by the highways concession in 2007. However, ministries have lost some of their staffing resources, with implications for the institutional framework. The lack of consensus on the institutional design has also had significant implications on the perception of regulatory risk.

The issue of choosing the best institutional options for regulatory governance in a market-based economy remains open. The new Law 3 337 has stimulated the policy debate related to agencies in the last three years. Brazil still has to improve its capacities for regulatory quality and increase transparency and accountability for public governance. Choosing the right balance between independence and accountability while delegating regulatory competences reflects strategic public policy choices. While the main focus was initially on privatisation, as well as on balancing the public budgets, institutional design issues are now receiving broader attention, together with the need to establish a government-wide regulatory policy.

This shifts the focus towards the broader context of quality regulation in a modern market-based economy. The debates over a new bill on agencies discussed in Congress reflect the variety of views in the country. If Brazil is to further close the gap with OECD countries, there is a need to ensure that the agencies will be “put to work”, fulfilling the mission for which they were originally created, with stable resources and staff, clear objectives paying attention to both investors’ and consumers’ needs and to less political interference.

Broader regulatory policy challenges

While much of the focus of the policy debate is still on agencies, a broader policy perspective is emerging reflecting trends in OECD countries. Improving the legal system of a country as a whole and its different instruments are key to ensure sustained economic growth and to provide a clear framework for citizens and private sector stakeholders. While relatively structured frameworks exist for preparing core laws, with informal consultations and some quality control procedures, Brazil however lacks a systematic use of different regulatory quality tools. Consultation could be more fully utilised. Beyond ensuring access through electronic means, effective participation of citizens in consultation procedures remains a challenge. Social participation is low as civil society can be difficult to represent. There is also a need to build up a voice for consumers. Other issues include compliance, relations with the judiciary, as well as further efforts for administrative simplification. Simplifying the legal framework requires intensive work to improve the quantity and the quality of the regulation currently in force.

A systematic strategy is required, with a framework for regulatory review that will ensure transparency, social participation and economic efficiency, with explicit responsibilities at both political and administrative levels. The discussion over a standardised process for preparing new regulations including impact assessment is starting to take place. There is a need to build regulatory capacities inside the administration in the medium and long term. The Brazilian government, through the Civil House and in conjunction with the Ministry of Finance and the Ministry of Planning, Budget and Management, is setting up a Programme for the Strengthening of the Institutional Capacity for Regulatory Management (PRO-REG) to contribute to the improvement of the regulatory system and increase co-ordination among the institutions that participate in the regulatory process. In addition, PRO-REG envisages the establishment of an oversight body for regulatory quality and the introduction of Regulatory Impact Analysis (RIA) as a policy tool to support decision making. The implementation will take time.

Strengthening capacity for quality regulation

The first challenge for Agencies has been to operate as autonomous bodies within the policy environment to promote confidence and transparency for the private sector and civil society. Establishing autonomy in the broader policy debate has been fraught with many discussions and contradictions. Some of them were linked with the issue of separating broader policy design and planning, which should remain a ministerial remit, from enforcement and execution which are tasks delegated to the agencies. On the whole, agencies have been operating at arms' length from government and have been fulfilling their mission since they were created. They have a different status and some of them leave less room for autonomy than others

A middle income country such as Brazil has to build and consolidate public service institutions while facing resource constraints in terms of staffing. These have at times affected the ministries and agencies. In general, agencies have built a reputation for integrity and have generally contributed to significant improvements of the regulatory framework in their sectors. Several of the agencies examined in this report are regarded among the best in Brazil in terms of perception by potential foreign investors and consumers, as well as according to World Bank assessments. These include, ANEEL and ANTT. ANTT faces a more difficult challenge in terms of co-ordination as it is more recent. Until recently, its resources were not consistent with its broad regulatory responsibilities.

This report has identified a number of issues which deserve attention. Securing autonomy may be an issue in terms of resources and governance, to ensure that Brazilian regulators have the capacity and technical competence to carry out their functions without being challenged. Guaranteeing resources and clarifying the implications of the new Law 3 337 is a necessary first step. Recently, significant resource increases have been observed for some agencies such as ANTT or ANS. A proposed constitutional amendment, PEC 81, may help to further consolidate the position of the agencies in the future. Similarly, regulators need to operate in an institutional environment where ministries can play their role. In this regard, the recent strengthening of the capacity of Brazilian ministries through an increase in the administrative and engineering staff is welcome. It will help set the debate at a technical level, and reduce the scope for ideological disputes.

Ensuring accountability is crucial, if regulators are to perform their mission and enjoy some independence in their relations with their parent ministry. Clear gaps exist in the current framework, in terms of ensuring broader accountability in the social sense, and reassuring citizens that regulators will defend the public interest, consumers' needs and the individual citizen. In such a large country, where social access to essential goods remains somewhat diffuse and uneven, the perception exists that some regulators may not have paid sufficient attention to the needs of individuals, such as those who have private health care insurance, or those unable to understand the clauses of their mobile phone contracts. While other regulators have less to do with the public directly, ANS and ANATEL are facing challenges in consolidating their legitimacy and balancing their approach between individual consumers and service providers. While it has been demonstrated that consultation did allow ANATEL to integrate the consumer perspective, processes for ANS are lagging behind. While the agency's work does benefit consumers, the public perception in Brazil that the relationship between health insurers and the privately insured is often so

imbalanced, a situation similar to that observed in many OECD countries, may have generated the impression that more could be done.

At present, Brazil seems well positioned to address current challenges. A broad consensus tends to emerge among political actors, the different parts of government and businesses and academia, that the country requires changes to improve its capacities for regulatory quality. There is a growing understanding of the need to increase transparency and accountability in the system, to introduce new tools for regulatory performance and to make necessary adjustments to the judiciary. There is also, in spite of all the recent political debate, a growing domestic consensus as well as understanding of main trends across OECD countries, of the functions and roles of regulation.

Closing the gaps with a forward looking perspective

While the new bill helps to address a number of challenges in terms of closing the social gap and improving conditions for consumers, some aspects have also been a matter of concern. The debates over the last year have led to significant modifications of management contracts that had been proposed initially. Over the years, the policy perspective has also been modified. The current environment has been one of reduced regulatory risk, as illustrated by the recent auctions for highways in October 2007. Other issues still remain at stake: clarifying the economic and social consequences of the concessionary power transfers to respective ministries. This may have different implications for the different sectors depending how it is envisaged and taken forward.

The diversity of experience offered by OECD countries provides a wide range of possible solutions that could be adapted to the Brazilian context. They offer both broad general directions in terms of setting up a framework, balancing independence with accountability, but also illustrates cross country variations in terms of powers delegated to agencies and the range of options for universal service.

Brazil is now confronting its economic and social challenges with strengthened regulatory institutions and a more consistent approach to its framework. The need for a broader perspective, increasing social inclusion, involving consumers and building trust in the regulatory framework has met with an intense domestic policy debate on the regulatory frameworks and the agencies. If Brazil is to continue to take advantage of the benefits of globalisation, it also needs to further modernise some of its core infrastructure, as well as ensure adequate future supply of core services. Setting up a clear regulatory framework, and drawing the lessons from OECD countries in terms of quality regulation and performance, will help to further adapt domestic institutions. This may only represent the start of a long process, given the size of the country and its unique geographical, economic and social diversity. The progress made in recent years bodes well for the future. Consolidating the fundamentals of a market-based economy is very important if Brazil is to build on its current achievements and increase economic opportunities for all its citizens. Transparency, consultation and evidence-based decision making will all help to improve the conditions of the public debate and help the country to better serve the needs of its citizens. This will also help to develop the institutional capacity for sustained long term economic growth that will increase economic resilience and maintain appropriate incentives for investments in core infrastructures.