

ENABLING EXPANDED PRIVATE INVESTMENT

(TC-93-01-18-6)

EXECUTIVE SUMMARY

**BENEFICIARY/
EXECUTING AGENCY:** The Public Utilities Commission (PUC) and The Bahamas Environment, Science and Technology (BEST) Commission; Office of the Prime Minister.

OBJECTIVES: The specific objective is to render the Public Utilities Commission (PUC), and the national environmental agency, The Bahamas Environment, Science, and Technology (BEST) Commission, fully operational and effective.

FINANCING:

Modality:	Grant
Recipient:	US\$ 679,500
MIF:	<u>US\$1,342,900</u>
Total:	US\$2,022,400

**IMPLEMENTATION
SCHEDULE:**

Execution period:	24 months
Disbursement period:	30 months

**ENVIRONMENTAL
REVIEW:** The Committee on Environment and Social Impact reviewed the document on March 6, 1998, and noted its support for the systematic and comprehensive approach to development of a regulatory framework for privatization espoused by the TC, which recognizes the need to integrate environmental regulations with the economic and technical aspects of the regulatory framework.

**SPECIAL CONDITION
PRIOR TO
DISBURSEMENT:** Special condition prior to first disbursement is the appointment of the two Coordinators (the BEST Commission and PUC) approved by the Bank and presentation of a six month Action Plan.

**OTHER SPECIAL
CONDITIONS:** Disbursement exceeding 40% of the funds corresponding to Component I will require evidence of GOBH approval of the regulations of the revised PUC Act and appointment of a regulator to head the PUC; and, disbursement of funds for Component II, sub-component 2, is contingent on recruitment and contracting of two professional staff at the environmental agency within sub-component 1 activities.

I. COUNTRY ELIGIBILITY

- 1.1 The Bahamas was declared eligible for all modalities of MIF financing by the Donors Committee on May 22, 1995.

II. FRAME OF REFERENCE

A. General framework

- 2.1 The Government of The Bahamas (GOBH) wants to improve utilities' regulation and strengthen environmental management prior to further deepening economic liberalization and structural adjustments which it began in mid-1993. Policy measures during the last five years have included: divestment of hotels and a commercial bank, private sector participation in selected utilities, liberalization of domestic air transport and broadcasting, reforms of foreign investment and trade regimes, and capital market strengthening. These policy measures followed recommendations developed in a proposed Bank operation in 1992, but which the GOBH wished to implement on its own and at a self-selected pace.
- 2.2 Within the utilities sector, the GOBH has moved towards a staged liberalization of its policies with respect to water, electricity and non-basic telecommunication services. In particular, a private sector water treatment plant has been permitted in the country; electricity generation, distribution and transmission in one of the main islands is now fully privatised; and, limited private competition has been permitted in telecommunication. These liberalization efforts have resulted in the entry of new market players and has brought some limited competitive forces to operate in the economy.
- 2.3 Since re-election in 1997, the GOBH has accelerated privatization effort in the utilities sector. This effort is most advanced for the telecommunication and electricity companies, with the former expected to be brought to a point of sale by early 1999. Privatization of the electricity sector has now been delayed somewhat because of the attention being given to the telecommunication sector. GOBH is interested in promoting increased private sector participation in the water and solid waste sectors also.
- 2.4 GOBH's decision to privatize the telecommunication company was approved by Parliament in March 1998. In this connection, an Advisory Contract has been awarded to an international consultancy firm to provide, *inter alia*, advice on privatization methodologies, regulations for a regulatory authority, review and analysis of the existing tariff structure, preparation of bid documents, and assistance on evaluation of the bids received. The authorities believe that further technical assistance would be needed in the

telecommunication sector to convert the consultant reports into action-oriented policy documents.

- 2.5 With the exception of the telecommunication sector, the GOBH has not formulated its privatization policy for the utilities. Nevertheless, the GOBH wants to begin training regulatory staff as it develops privatization options and environmental standards (see below). GOBH recognizes the value of having an independent and effective regulatory agency in the privatization process, and is keen to establish a full fledged regulatory agency before the privatization process is further advanced.
- 2.6 Within the environmental sector, GOBH has already established an environmental umbrella coordinating agency which needs support in policy development and institutional strengthening to ensure that the environmental implication of economic developments are institutionally incorporated in policy. The urgent need for strengthening environmental management is re-inforced by the impending privatization of selected utilities, in order to regulate future activities as well as to assess current environmental conditions that may require mitigative measures. Moreover, while environmental degradation is not serious in the country, the *ad hoc* physical development, growth of tourism, significant expansion of tourism-related investment, water resource issues, and institutional capacity problems are beginning to strain environmental and natural resources.
- 2.7 Effective utilities regulatory and environmental agencies would strengthen economic competitiveness and enable expanded private investment. An independent utilities regulatory agency that approves the tariff and issues licenses, together with environmental audits, will make investing in the utilities attractive. Moreover, an effective environmental agency will also make investments more attractive in other areas across the islands which make up The Bahamas because of the assurance of environmental protection this will provide. Together with the geographical information system under development (see below), the proposed operation will also help in the eventual development of a land use planning program and provide a basis for environmental information.
- 2.8 The Bank group is assisting the GOBH in a number of complementary operations in the privatization process. Technical assistance with respect to privatizing the basic telecommunication service has been provided. Under a Bank-funded loan, an international consultancy firm submitted a report in January 1996 recommending options on the regulatory framework for privatization of the electricity sector. GOBH has not taken a decision as they now await the outcome and experience of privatizing the telecommunication company. A recently approved technical cooperation operation will develop the geographical information system in the country, which will include information on infrastructure and environmental resources. The Bank is also preparing two investment loans in the water and solid waste sectors which would help to better define privatization

options for the Government. Both these loans are expected to be approved in 1998, and the proposed operation could leverage action on independence of the regulator from the service provider by supporting the establishment of an umbrella regulatory agency which is autonomous and has an independent budget.

B. The regulation of public utilities

- 2.9 The GOBH wants to embark on a program to enable expanded private investment in the utilities with a view to promoting efficiency, competition and improved service quality while continuing to protect the environment. With the privatization of the telecommunication monopoly imminent, the GOBH wants to operationalise the Public Utilities Commission (PUC) that will assume legal and economic regulatory responsibility for energy, telecommunications, water and sewerage, and solid waste management. In mid-1993, legislation to establish the PUC was enacted and was to have become operational when the Minister of Finance so determined, which has not yet occurred. The Act needs to be revised and its scope expanded to include regulation of solid waste management.
- 2.10 Economic and legal regulation of utility companies and service providers are presently diffused in the country. The legislation providing the regulatory authority often dates back to the establishment of the relevant agency. In certain utilities the legislation has become outdated and has created a grey area of jurisdiction. In the telecommunication sector, for example, the self-regulated service provider is also a regulator of private sector operators in areas where competition is permitted -- such as paging and Internet services.
- 2.11 A number of utilities-related pieces of legislation will be updated soon. As the GOBH proceeds with the privatization of the telecommunication company, it will be revising the legislation to update definitions and separate the regulator from the service provider. A proposed Bank operation in the water sector will address the legislation and regulatory aspects of ground water abstraction. A second Bank operation will have components developing legislation and regulations for solid waste management.
- 2.12 With respect to economic regulation, there is no systematic analysis of rates or quality of services provided. New tariff rates require Cabinet approval and, in at least one case, the rates must be approved by Parliament. Where private sector participations have been allowed, the present regulatory arrangements in an environment of oligopolistic markets encourage rent-seeking behavior by the service providers and do not promote efficiency. As a result, social and economic costs probably remain high.

C. Environmental management

- 2.13 To strengthen environmental management, the GOBH created The Bahamas Environment, Science and Technology (BEST) Commission

within the Office of the Prime Minister in the early 1990s as a national coordinating agency with responsibilities for developing and guiding environmental policies, procedures and programming, and coordinating the review process of development proposals. However, the organization is not funded or staffed to a level that will allow it to carry out its broad mandate.

- 2.14 One of the greatest demands placed on the BEST Commission since its inception has been the coordination and rapid summarizing of environmental impact assessment (EIA)-related comments among many government departments. The environmental agency is ill-equipped to perform adequately in this role and lacks the full legal authority and mechanisms necessary to play a central role in the EIA process. The BEST Commission currently acts on the strength of its position within the Office of the Prime Minister and lacks a clearly defined and legally constituted mandate. There are no policies, legislation, regulations or guidelines to direct action in a coordinated manner. Moreover, it lacks adequate staff and financial resources, the lack of a sound database on which to make informed decisions, and appropriate procedures and mechanisms for planning, policy and quality control.
- 2.15 In the meantime, due to the absence of guidance to the private sector regarding government EIA-related expectations, developers are submitting a wide range of EIA assessments, some much more detailed than necessary, others too cursory. In addition, many development applications, particularly those submitted by Bahamian developers, never reach the BEST Commission for comment, and may be approved via the physical planning process with little or no review for environmental impacts. Similarly, local councils can approve developments under a minimum size without further review, making it difficult to avoid the potentially serious cumulative impacts of a series of small developments. In some cases, government capital works initiatives have not been subject to any meaningful EIA process either.
- 2.16 In order for BEST Commission to fulfill its mandate, and provide support to GOBH goals with respect to establishing sound procedures, policies and management tools to guide development while protecting environmental resources, the BEST Commission must be strengthened, its operational capacity enhanced and its mandate, including in the EIA review process, clarified and well articulated.
- 2.17 The GOBH recognizes that successful environmental management and sustainable development depend upon a fully functional coordinating agency. To this end, the GOBH has requested assistance in strengthening environmental management through development of relevant policies, and the institutional strengthening of the BEST Commission to ensure that environmental quality control and EIAs are sufficient to promote sound private sector-led economic development.

D. Government strategy

- 2.18 Economic liberalization and structural adjustments pursued by the GOBH have been in line with a proposed Investment Sector Loan (ISL) developed in 1992 in response to a request by the GOBH, following negative growth rates during 1991-92. The proposed ISL was elaborated with a view to strengthening the economy's competitiveness, promoting a more favorable climate for private investment, and preventing further environmental damage. A new Government, elected later in that year, subsequently advised the Bank that it wished to implement the reforms on its own.
- 2.19 In recognition of the benefits of creating an independent regulatory institution for utilities and corresponding regimes that should precede major moves towards private sector participation or privatization, the GOBH wants to establish a fully functioning PUC before decisions are finalized on the future structure of each individual utility. In particular, to improve efficiency and increase private investment in utilities, with due consideration for the special problems associated with small communities on remote islands, the GOBH recognizes the need to prepare a core group of staff who can provide legal, safety and economic regulation of utility companies.
- 2.20 The GOBH recognizes that, prior to privatization, it is important to develop effective economic and legal regulations of the utilities, and agree on environmental mitigation measures for those utilities scheduled for privatization. It is also recognized that where outright privatization is not imminent, the operation of public services may sometimes be in conflict with wider national objectives such as the protection of the environment. In particular, the utilities must be integrated within a framework of environmental regulation which is compatible with the economic circumstances of the country.
- 2.21 Moreover, the GOBH wants to extract socio-economic benefits by separating the policy formulator, regulator and the service provider in public utilities. In particular, it recognizes that potential abuses of market power on the part of the service provider is reduced by establishing a mechanism for economic regulation and by establishing and enforcing quality and customer service standards; that development of a sound framework is prerequisite for quality of service regulation; and, that even when circumstances do not permit competition, efficiency gains can still be enhanced through a variety of institutional and regulatory incentive mechanisms.

E. The environment and investment

- 2.22 Recent policy measures, together with mostly prudent macroeconomic management, have contributed to increased foreign private investment in the order of 10-20% of GDP annually, mainly in tourism-related businesses in New Providence and in a number of

Family Islands, of which about 27 are inhabited. Increased investment, particularly in the Family Islands, could adversely impact the environment in the absence of adequate environmental safeguards and enforcement. The authorities recognize an urgent need to formulate environmental regulation and develop enforcement capabilities in order to sustain the investment trend while protecting the natural resources.

- 2.23 There is a recognition that there are strong and strategically important linkages between environmental and economic interests in The Bahamas, particularly in the context of the tourism industry, which is based strongly on the maintenance of a healthy and aesthetically pleasing environment. Yet, there is a lack of private sector participation in environmental management activities. Both because the private sector can be the primary source of degradation and because it may also be affected by environmental management decisions, increased private sector participation is deemed vital to the success of future sustainable development.

III. THE PROJECT

A. Objectives

- 3.1 The general objective of the project is to assist the GOBH in establishing a fully developed legal and regulatory framework for the energy, telecommunications, water and sewerage, and solid waste sectors, and help to strengthen the institutional capacity for managing and enforcing environmental protection policies and measures. Achievement of both objectives will foster a sustainable private sector-led development in The Bahamas. The specific objective is to render the Public Utilities Commission (PUC), and the national environmental agency, the BEST Commission, fully operational and effective. In so doing, the project will address the distribution of responsibilities for environmental regulation in order to clarify and/or rationalize them and avoid duplication of functions.

B. Project components

- 3.2 The project will consist of: (a) legal and regulatory framework for utilities; and, (b) strengthening of environmental management. Both components have general terms of references, available in the files.

1. Component I: Establishment of a Regulatory System for Utilities

- 3.3 Objectives. This component will provide assistance to develop all the legal instruments and a fully functional and autonomous PUC -- properly organized and staffed with an independent budget -- to

fulfill the responsibilities assigned by the legislation, followed by tariff studies and preparation of operational manuals, and procedures required for supervision and enforcement of regulations governing public and private operators engaged in providing services, as well as commercial, industrial, and residential users in the energy, telecommunications, water and sewerage, and solid waste disposal sectors.

3.4 Activities. Under this component, consulting services will be hired to perform the following tasks:

- a. Review of existing legislation, proposals for amendments, and preparation of regulations for all PUC Act provisions.
- b. Preparation of operational guidelines, dealing with key regulatory functions, methodologies, and information requirements for each of the regulated services.
- c. Design of the internal organization of the PUC, staffing requirements, budget, and information systems.
- d. Complete utilities' tariff, quality-of-service, and competition/efficiency promotion studies for each of the regulated utilities.
- e. Mount a training program for the PUC staff consisting of relevant short work studies abroad to familiarise new regulators on economic and legal aspects of regularization, and funded from counterpart resources, followed by workshops, on-the-job training, and visits to regulatory agencies.

2. Component II: Strengthening of Environmental Management

3.5 Objectives. The objective of Component II is to ensure sustainable private sector development by supporting the GOBH in setting in place a fully operative BEST Commission properly organized, staffed and equipped to be able to fulfill its mandated duties; and to assist in establishing an appropriate operational strategy between the BEST and the Public Utilities Commissions.

3.6 Specifically, Component II will support development of:

- a. Sustainable environmental policy and associated strategies, including management tools and interim EIA guidelines; and counterpart development in the BEST Commission. Under this sub-component, additional staffing needs at the BEST Commission will also be identified, new personnel hired and the Terms of Reference for sub-component 2 (see below) will be refined.
- b. An institutional strengthening program to support the BEST Commission's fulfillment of its overall mandate, as well as its capability to follow-through the adoption of proposed policies and strategies; and, establishment of an environmental quality

control and monitoring system, based upon the environmental impact assessments and permits, directed towards preventing negative impacts from public and private sector development projects.

Subcomponent 1: Sustainable environmental policy and associated strategies

3.7 This sub-component will finance technical expertise to develop, in conjunction with technical staff from the BEST Commission and other pertinent agencies, a proposal for a national sustainable environment policy aimed at conciliating the country's economic, social and environmental priorities. The policy and strategy statements will suggest means to integrate environmental policy objectives with the country's overall macroeconomic and development policies, suggesting alternative incentives and other economic instruments for the purpose. The proposed policy statement will also cover strategic actions that would be required to make sectoral (tourism, industry, transportation, urban development, health, and so forth) policy consistent and coherent with environmental objectives.

3.8 Activities under sub-component 1 will include:

- a. Review of existing national policies, proposals for assignment of natural resource management responsibilities and feasible economic instruments, preparation of environmental policy proposal, and assistance with negotiations as required.
- b. Designing the interim EIA guidelines and procedures.
- c. In-house training of BEST Commission staff.

Sub-component 2: Strengthening of organizational capacity.

3.9 The project will finance one long-term technical advisor (at least 18 expert-months) specialized in environmental management to provide sustained support to the BEST Commission, and a number of specialist short-term consultants. The consulting team will help in the Commission's day-to-day work, and will develop institutional strengthening programs directed towards priority areas where the Commission is weak.

3.10 Activities funded under this sub-component will include:

- a. Detailed institutional and organizational assessment and recommendations for the BEST Commission and other agencies involved in environmental management.
- b. Development of a long-term financial plan for the BEST Commission.
- c. Refinement of EIA guidelines and procedures, and circulation to relevant private and public agencies for comments.

- d. Assessment of capacity in the government agencies for quality control, monitoring and enforcement; definition of needs; and design of a conceptual proposal.

C. Cost and financing

- 3.11 The estimated program cost is US\$2,022,400, of which the MIF is requested to finance US\$1,342,900 and the balance of US\$679,500 provided as local counterpart funding by the GOBH. A detailed budget is available in the technical files upon request.

D. Procurement

- 3.12 The GOBH will follow normal Bank group procedures in procurement of goods and services.

PROJECT BUDGET

COMPONENT	MIF	LOCAL	TOTAL
I. Program coordination, management and administration	72,000	210,000	282,000
II. Regulatory system for utilities	605,000	346,000	950,000
1. Legal framework, development of regulatory systems, establishment of PUC, and related studies	482,300	226,000	708,300
2. Training of PUC staff	122,200	120,000	242,200
III. Environmental Management	665,900	123,500	789,400
1. Development of sustainable environmental policy and strategies	102,700		
2. Development of an institutional strengthening program for the BEST Commission, establishment of an environmental information system, and establishment of an environmental quality control and monitoring system	563,200	123,500	686,700
TOTAL	1,342,900	679,500	2,022,400

E. Reports

- 3.13 The PUC component would generate the following technical reports:
 - a. Recommended changes to the 1993 PUC Act and draft regulations for a revised Act.
 - b. Recommended organizational structure for the PUC.
 - c. Report on financing options for the PUC to ensure its financial independence.

- d. Reports on tariff rates, competition promotion measures, service quality standards and environmental impact of providing utility services.
- 3.14 The environmental management sub-component 1 would generate the following technical reports:
- a. A comprehensive review and analysis of existing environmental policies, legislation and regulations.
 - b. Feasibility analysis of economic incentive/disincentive measures to promote sound environmental practice.
 - c. A sustainable environmental policy and associated strategies report.
 - d. Evaluation report of the information management system and recommendations for improvement.
 - e. Staffing needs identification report and terms of reference for sub-component 2.
- 3.15 The environmental management sub-component 2 would generate the following technical reports:
- a. Needs assessment of the BEST Commission.
 - b. Early development of a workplan covering the period of project implementation.
 - c. Documentation of the current mandates, roles, responsibilities, skills, budgets, staffing, activities, etc., associated with each relevant government agency.
 - d. Report on financing options for the BEST Commission.

F. Execution and monitoring

- 3.16 The overall execution of the project will be under the direct responsibility of the Office of the Prime Minister. The Office of the Deputy Prime Minister and the BEST Commission will each appoint a Coordinator, respectively, for the utilities and environmental components. The two component Coordinators will each select the consulting services required to perform the tasks under their respective responsibilities in accordance with terms of reference approved by the Bank. A detailed work plan is available in the technical files upon request. The Executing Agencies will submit progress reports at six monthly interval. A mid-term evaluation will be carried out after 12 months of effectiveness and a project completion report produced within six months of the final disbursement.

- 3.17 The period for project execution will be 24 months and the corresponding disbursement period will be 30 months.

IV. MIF ELIGIBILITY CRITERIA

- 4.1 The proposed project is fully consistent with the MIF general objective of promoting private investment and facilitating private sector participation in support of accelerated economic and social development. The proposed project also fully meets the Project Eligibility Criteria for the Technical Cooperation Facility, in accordance with Article III, Section 2 of the MIF Agreement, which establishes that MIF resources can be used for the design and implementation of projects helping to establish more favorable conditions for private investment.

V. BANK COUNTRY STRATEGY

- 5.1 The Bank strategy for The Bahamas is to support the efforts of the GOBH in restoring sustained, private sector-led growth by improving competitiveness, diversifying the economy, improving intersectoral linkages, and strengthening of environmental regulation. Establishing a fully developed and reliable regulatory system is essential for attracting private capital and entrepreneurship to assist in improving productivity and efficiency in the provision of basic services serving the tourism sector, the principal industry of the country. Environmental programs and regulations are also equally essential for addressing the short- and long-term natural resources requirements of development especially given the natural resource limitations and tourism-dependency of The Bahamas.

SIMPLIFIED LOGICAL FRAMEWORK

OBJECTIVES	INDICATORS	MEANS OF VERIFICATION	ASSUMPTION
OVERALL GOAL To enable expanded private investment.	Increased domestic and foreign private investment in the public utilities.	Published information on privatization of the utilities.	Government's privatization efforts are not continued.
	Increased and geographically diverse investment across islands.	Published data on domestic investment, and unpublished but available data on foreign investment inflows.	GOBH's investment regime remains competitive with the other countries in the region.
To establishing a fully developed legal and regulatory framework for the utilities.	An operating public utilities regulatory agency with appropriate regulatory functions.	Information supplied by the Executing Agency.	Timely implementation of program components.
To strengthen the institutional capacity for managing and enforcing environmental protection policies and measures.	Appropriate EIA guidelines in place, environmental audits completed, and inter-institutional coordination established.	Information supplied by the Executing Agency on the implementation of program components.	Timely implementation of program components to achieve an institutionally and organizationally strengthened environmental agency.

PROPOSED RESOLUTION

BAHAMAS. NONREIMBURSABLE TECHNICAL COOPERATION FOR
ENABLING EXPANDED PRIVATE INVESTMENT

The Donors Committee of the Multilateral Investment Fund

RESOLVES:

1. That the President of the Inter-American Development Bank, or such representative as he shall designate, is authorized, in the name and on behalf of the Multilateral Investment Fund, to enter into such agreements as may be necessary with the Commonwealth of the Bahamas, and to take such additional measures as may be pertinent for the execution of the project memorandum referred to in Document MIF/AT- with respect to a technical cooperation program for enabling expanded private investment.
2. That up to the amount of US\$1,342,900, or its equivalent in other convertible currencies, is authorized for the purpose of this resolution, chargeable to the resources of the Technical Cooperation Facility of the Multilateral Investment Fund.
3. That the above-mentioned sum is to be provided on a nonreimbursable basis.