PUCs in Year 2000: Mixed Mission, Clear Challenge

You can look at the title in two ways: (a) “The sky is falling,” or (b) “There’s nothing new under the sun.” But both views are wrong. Let me explain.

No one doubts that state public utility commissions (PUCs) must change. But we need not throw up our hands in despair or smile and pretend we’ve seen it all before. Yes, PUCs have seen major changes before. The 1930s expanded PUC authority from advisory, sunshine role to serious oversight. The 1970s ended a long run of rate decreases and challenged PUCs to cope with financial distress at energy utilities. The 1980s broadened PUC regulation to include social concerns like environmental policy, conservation, safety nets, privacy, and health. And I believe that PUCs successfully accommodated all three trends with resilience, as I expect they will this latest round of change. But make no mistake: Current forces are so dynamic as to mark a difference in kind—not just in degree.

Looking Inward

Outward changes in regulated industries naturally occupy a good bit of attention at state PUCs. Introspection and self-reflection about internal changes at the PUCs themselves seem less common. Nevertheless, one can discern a few stirrings here and there.

The New York Public Service Commission recently underwent a major reorganization. The Wisconsin Public Service Commission now has a Strategic Business Plan. The Washington Utilities and Transportation Commission has called for agency renewal for several years. In July 1993, the National Regulatory Research Institute (NRRI) completed a report on total quality management (TQM) for the executive directors of the agencies that make up the National Association of Regulatory Utility Commissioners (NARUC). That report also cited TQM efforts in Colorado, Michigan, Oregon, New York, and Florida, and noted plans to consider TQM in Maine, South Carolina, and Texas, with Iowa and Missouri perhaps to follow. In April, the NRRI board of directors will convene a summit conference of state commissioners in Denver, dubbed “PUC 2000,” to consider what PUCs should do at the turn of the century.

In tackling the changes that must be made, PUCs should prefer gradualism over a “flashcut” approach. Several reasons argue this tack.

First, virtually no one envisions complete deregulation. Rather, the debate centers on the degree and timing of relaxed regulation. Second, traditional regulation with modest adaptive modifications has served tolerably well for many decades, some of us believe. Regulation has suffered a number of bum raps; some comparisons are obviously unfair (for example, perfectly functioning Smithian markets vs. imperfect rate base regulation). Third, the persistent rhetoric from some quarters about utility regulation having “outlived its usefulness” is seriously flawed. Many of the original tasks of public utility regulation remain (such as guarding against the abuse of economic power). Even with customer classes bifurcated into core and noncore groups, the former still needs protection. And yet a fourth argument supports gradualism: Deregulation is asymmetric. Once regulators relinquish authority, they find it difficult to regain.

Looking toward 2000, PUCs must define a mission and a set of tasks to deal with “core” customers, competitive services, utility managers and shareholders, and social objectives. Along the way, they must define the configuration, size, structure, and skill set they need to do the job.

Defining a Mission

First, the mission and concept of a PUC. As mentioned, two elements define the task: 1) the distinctions between core and noncore customers, and between monopoly and competitive services; and 2) what is to be done about the social agenda (conservation, environmentalism) that traditional regulation has recently acquired.


Public Utilities Fortnightly, February 15, 1995
In general I do not picture commission regulation with respect to core customers as requiring great change. While price caps, rate freezes, and the like may increasingly replace rate-setting and force a decline in general rate cases, the conventional tasks of ratepayer protection remain for core customers. These tasks include 1) setting reasonable prices and returns, 2) prohibiting undue discrimination, and 3) ensuring adequacy and reliability of service. These things historically have been subsumed under the rubric of protection from the abuses of monopoly power. I predict that pervasive arguments by neoclassical economists—calling for “consumer sovereignty” and “allocative efficiency”—will not overwhelm commission considerations of equity, improper risk-shifting, and some preferential treatment for core customers. Institutional economic thought has always been important in PUC regulation, as was a focus on abuses of economic power, real and potential.

Nevertheless, the growing universe of noncore customers will force a rethinking of mission and concept at the PUCs.

Here’s one helpful approach. Frame noncore services into new classes—“workably competitive,” “emerging competitive,” and “noncompetitive”—but keep in mind that these boundaries are imperfect and that migration can and should take place. To carry out this strategy, PUCs should continue a selective regulatory retrenchment (sometimes practicing outright forbearance) and rely increasingly on antitrust law, public jawboning, and invidious yardstick comparisons to remedy utility excesses. PUCs should also shift their emphasis from financial regulation to quality-of-service regulation, while widening commission oversight of promotional and developmental (as opposed to regulatory) activities.

Other changes in self-perception of mission would seem to follow logically. In a competitive world, most industrial and commercial customers presumably can “take care of themselves” (certainly the large ones can). As we have already seen, The Electricity Consumers Resource Council (ELCON) has become a familiar player before PUCs and utility companies. With noncore customers persistently driving hard bargains with utilities on all fronts, PUCs can give proportionately less attention to these customers, except for worrying about the undue price discrimination and concomitant cost-shifting that can be involved in utility responses.

And the same goes for shareholders. The concept of the PUC sitting as impartial arbiter midway between consumers on the one hand and stockholders on the other appears to have eroded. A financially healthy utility is, of course, desirable, but PUCs may not need to work so hard to make it happen.

Finally, what happens to the broader agenda that PUCs have fostered over the last decade. Despite assertions to the contrary, some of the gains in the areas of environmental protection, conservation awareness, demand-side management, integrated resource planning, and corporate community citizenship may well lie at risk if they can depend only upon market forces for their survival.

Forging a Role

Some say that the forces of change (technological, structural, and attitudinal) are so strong and pervasive that PUCs can no longer control or shape them. I disagree.

Commissioners have always faced a choice: Whether to pursue a passive or an activist role. In a passive role, PUCs would largely limit their attention to valuing the rate base, setting the rate of return, and perhaps looking in on rate design. As interventionists, commissioners would be found always operating at the outer edges of their statutory authority. While either stance is appropriate, the trend has been moving toward activism. Moreover, some simultaneous contradictory forces are now at work.

“Relaxed regulation” implies abstinence by regulators; but if we define our goal as more competition, PUC participation may well prove essential.

Seven Forces that Affect PUCs

- Technological change
- Academic and journalistic attacks on public utility regulation
- Less faith in government
- More faith in markets
- A feeling that it’s time for a change
- High turnover (lost institutional memory)
- Privatization efforts elsewhere that offer interesting results
Five Ideas that Will Survive

- Prevention of undue discrimination
- Rate base regulation
- Fair rates of return
- Cost-based ratemaking
- Obligation to serve

workable markets, then adroit and sustained PUC participation may well prove essential to speeding up the process. Phrased differently, even if deregulation marks the ultimate objective, it will take high-order public policy skills to get from here to there. Still, the interventionist role should decline over time.

Beyond the debate over activism, we find PUCs changing their decisionmaking style from quasijudicial to quasilegislative. As we know, most PUC cases used to be adversarial; PUCs acted mostly as a sort of judicial panel. Now, formal adversarial proceedings arise less frequently. Generic policy prescriptions of various kinds increasingly occupy the time and energies of regulators.

A major worry for PUCs is what will happen to their traditional independence in 2000. Always having required vigilance to maintain, PUC independence finds itself sorely challenged by the subtle breakdown of arm's-length dealing with utilities and the rise of "collaboration" and "consensus building" as the primary modes of operation. The task becomes even more trying as the turnover rate increases at commissions, wiping away some institutional recollection of the value of independence. Governors' offices, state development offices, and state legislatures can be expected to insinuate themselves more frequently into commission business as a natural consequence of the dejudicialization of PUCs. Finally, ex parte prohibitions and standards of ethical conduct would appear more difficult to observe and enforce in the new environment of quasilegislative policymaking.

Administrative Functions

Then there is the question of what a PUC might look like in 2000 if the above perception of change in mission, concept, rules, and practices is anywhere near the mark. At issue, specifically, are matters of commission size, configuration, and skills to do the new/old job. Again, my view that PUCs will serve two different constituencies (core ratepayers and noncore customers) defines my answers.

The dejudicialization of PUC activities should provoke some streamlining of operations and further experimentation with alternatives to trial-like behavior. More reliance will be placed on some older procedures like stipulations and on newer varieties like industry/regulator workshops, panels of scientists, negotiated settlements, and new methods for alternative dispute resolution. We may also find that PUC technical staff stop intervening as formal parties in commission cases, returning instead to their earlier role as advisors.

Setting aside agency resistance, it is not certain that PUC staff size will be reduced in the years leading up to the millennium. Some are already too small to perform their assigned tasks; others have already downized to an irreducible minimum. As mentioned, PUC protection of core customers may be characterized generally as "business as usual," with some modifications for price caps and performance-based features. But, although fewer in number, captive customers can be expected to command continued close attention to safeguard their welfare. This attention will require familiar staff resources. Moreover, when periodic reviews and "true-ups" come along, most traditional analyses of earnings levels, rate structure, investment decisions, and service quality will still be necessary. Shrinking and expanding staff size to fit these cycles would prove expensive.

Deciding which services move into the workably competitive category—those that are emerging and those that are not—demands a good deal of high-order staff analysis. Some level of surveillance is needed as utility services migrate among the various categories.

Changes in the skill mix and responsibility of PUC staff form another matter entirely. With markedly fewer general rate cases and a focus on competition, one might expect fewer staff attorneys and rate design experts, and more economists focusing on industrial organization. PUC retrenchment from participating in utility planning would shrink the need for engineering staff, but greater emphasis on quality-of-service regulation (replacing financial regulation) will offer a counterbalance. Similarly, accountants and financial analysts (perhaps fewer in

PUBLIC UTILITIES FORTNIGHTLY, February 15, 1995
number) may shift their attention to the impacts of utility ownership structures, affiliate transactions (domestic and foreign), and mergers and acquisitions.

Finally, PUCs will have to decide what organizational arrangements best suit the old and new tasks. Which organization chart is better—hierarchical or flat? Do you make the PUC sector-specific (communications, water, and so on), or organize by discipline (law, engineering, economics) or customer category (core vs. noncore). The final result will reflect how well PUCs manage their agency environment amidst the tugs and pulls of legislators, utility managers, industry vendors, academics, journalists, governors' offices, and PUC staff.

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