The “Public Interest”: Who Has A Definition?

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September 2017

Regulatory statutes direct commissions to act in the “public interest.” Rarely do statutes, commissions or applicants define the term. Lacking definition, this statutory phrase risks becoming, in utility applications, a label attached to an applicant’s desires rather than a discipline on those desires; and in regulatory decisions, a label attached to a commission’s preferred outcome rather than principles that produce the right outcome.

Without a common definition we cannot have a common purpose. I suggest defining “public interest” as a composite of five goals: economic efficiency, alignment of shareholder and ratepayer interests, replication of competitive outcomes, respect for legitimate expectations, and diversity among each utility’s employees. The first four are entirely conventional, rooted in the elementary economic principles and longstanding regulatory practice. The fifth is an immediate necessity because of our national emergency. All five are mutually consistent and mutually reinforcing.

Economic efficiency: Economic efficiency means biggest bang for the buck. It means no waste. Investors seek the highest return for a given level of risk. Consumers seek the lowest price for a given quality of product. Business managers seek the highest possible output for a given level of input. As long as all bear the costs they cause, these rational actions lead to these results: benefits go to benefit-creators, costs are borne by cost-causers, and rewards repay risks. Each action makes someone better off and no one worse off; no benefit-creating opportunity is foregone.

Alignment of the shareholder and ratepayer interests: Shareholder and ratepayer interests, if legitimate, are not opposites. Shareholders want satisfied customers; customers want healthy companies. In regulating public utilities, the public interest is served when shareholder and ratepayer interests are aligned; that is, when pursuit of the shareholder interest simultaneously advances the consumer interest. That is how competition works: When a market has low entry barriers and no anticompetitive behavior, the most successful businesses have the most satisfied customers.

Replication of competitive outcomes: Economic regulation seeks to replicate the outcomes of effective competition. This goal is necessarily aspirational, because in the real world both competition and regulation are imperfect. Entry barriers, externalities, oligopolistic and monopolistic market structures, customer inertia, and imperfect information make effective competition difficult to achieve, let alone measure so as to replicate. Despite these difficulties, regulation aims to replicate competition because competition, ideally, is objective. It ranks players ruthlessly, based on their merits. Regulation must do the same.

Respect for legitimate expectations: In a competitive market, customers expect products to have the quality and price levels reflecting the best practices of the best competitor. Shareholders expect profit levels consistent with their company's performance for customers. Under regulation, the expectations should be similar. In both competition and regulation, customers have no legitimate expectation of superlative service at bargain-basement prices; investors have no legitimate expectation of superlative returns at below-average risks. In regulation, those legitimate expectations are protected, for shareholders and customers, by regulatory statutes; and for shareholders, by the Constitution's Takings Clause ("nor shall private property be taken without just compensation"). All other expectations are only aspirations; regulators are not bound by them.

The necessity of diversity: Fear, hatred, ignorance and political opportunism, abetted by so many of us lucky enough to look the other way, are soiling our national nest. May this period not last past January 20, 2021. Meanwhile, what is regulation's responsibility?

Utility executives are rightly assessing ways to protect our physical infrastructure from foreign terrorists. They need also to consider less costly protections against domestic terrorists. One way is to make utility personnel—from leadership to lineworkers—look like the populations they serve.

Diversity is not some "add-on," rolled out by merger applicants or rate increase-seekers looking to gain favor with their regulator. Diversity is who we are. Thomas Friedman wrote recently in the *New York Times* of his trip to Afghanistan with leaders of the U.S. Air Force. The chief is Jewish, his civilian boss a woman, her top aide an African American woman. The base commander and his aide were of Armenian and Lebanese descent; the combat innovation team commander had parents from Cuba and Mexico. Running the control center were two servicemen who had emigrated from Russia and Ukraine; the intelligence briefer was a Captain Yang. America had the region's most powerful force, Friedman writes, because our military "can take all of those different people and make them into a fist." See "Charlottesville, ISIS and Us."

What the Air Force has accomplished, our utilities have not. If diversity is central to success, why is progress by U.S. utilities optional rather than obligatory? In any utility financial report, read the sections on executive compensation plans. They all come from the same playbook: Rewards are based on earnings and share price. What utility board bases executive compensation on diversity? What regulatory commission disallows executive compensation costs, or lowers the authorized return on equity, for failure to create and carry out a plan for diversity?

Three score years after *Brown v. Board of Education*, the lack of progress—in utilities' C-suites, board rooms, management corps and work forces—is inexcusable. It arises from lack of commitment, lack of plans, lack of discipline and lack of regulatory muscle. "Good faith efforts," "outreach," scattered appointments to the vice presidency for community outreach, will not make up for decades of indifference. The pipeline is 15-20 years long—elementary school, middle school, high school, trade school, business school. But the pipeline is there. We need utilities motivated and obligated to fill it—with people who look like the community. And that need is matched by opportunity as thousands of baby boomers retire. We can't fix this overnight. But we can over a decade, if there are annual obligations connected to each of pipeline segment. (For more discussion of diversity, see my essay "Promoting Diversity and Prohibiting Discrimination: Is There a Regulatory Obligation to Society?"

We don't need to make America great again. America is already great, because of its diversity. If our utilities want to be great, they need to start the hard work, the long-term work: the 10-year accountable plans with real executive accountability to commissions prepared to penalize those who fail to progress. Our utilities need to catch up with the customers they are privileged to serve—or have their regulators find companies that will.