# The Regulatory Mission:
# Do We "Balance" Private Interests, or Do We Align Them With The Public Interest?

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A newly appointed assistant to a newly elected commissioner, both new to utility regulation, told me she'd asked veteran commission staff, "What is our mission?" The answer she received: "We balance the interests of customers and investors." This notion of regulation as private interest balancing, so deeply embedded in regulatory conversation, practice, and psyche, has five main problems. Can we recast the regulatory mission?

## Five Problems: Ambiguity, Nearsightedness, Presumption of Conflict, Passivity, and Legal Looseness

***Ambiguity:*** "We balance the interests of consumers and investors." Which consumers—large or small? Today's or tomorrow's? Our state's, our region's, or our nation's? Which interests? Short-term or long-term? The interest in low rates, or the interest in a viable supplier? Which investors? Buy and hold shareholders, pension funds, hedge funds, short sellers, current owners, or future owners, bondholders? Which interests— this year's profits or next decade's viability? What balance? "Balance" implies equivalence—the precise midpoint between two interests of equal weight. Are the customer investor weightings exactly equal? At all points in time? Or can they vary from equivalence at any point in time, provided the variations "balance" over some longer period of time?

***Nearsightedness:*** If utility service were merely a commercial transaction between sole supplier and captive customer, then "balancing the interests of customers and investors" would be a logical mission (provided we resolved the dozen ambiguities just discussed). But utility service is more. It is the infrastructure supporting our economy—schools, hospitals, streetlights, manufacturing. It is a means of sustaining life and its quality (think water shortage, electricity outage, no phone service, no streetlights, no movies). Utility service also produces the 1,000 year detritus of today's consumption decisions: nuclear waste and carbon emissions from electricity generation, chemical residue from telephone pole treatment, gas pipeline leaks. The regulatory lens must be both wide angle and long distance. "Balancing" interests misses this point.

***Presumption of conflict:*** A balance presumes opposites. (Picture the "scale of justice.") The presumption is wrong. Consumers' and utilities' legitimate aims—viable suppliers, satisfied customers, no waste, no free lunch, reasonable prices and reasonable returns—are consistent and mutually reinforcing. High quality performance and efficient consumption benefit everyone: customers, shareholder, bondholder, employees, the environment, the nation's infrastructure.

Conflict among opposing goals arises only from illegitimate aims: the cost-causer seeking to shift costs, the shareholder asking for excess returns. If regulation regularly exposed illegitimacy, its assumption of opposites would self correct. But some regulatory forums do the reverse, by embedding opposition into the core of regulatory procedure: Each party positions itself at the poles, aggrieved and relief seeking, testimonially swearing to its opponents' errors. Then comes the wheel dealing in private, the "settlement" (with boilerplate forbidding commission amendment on pain of undoing the deal), and the "approval" stamped by a boxed in commission. (For more on regulatory overdependence on settlements, see essay, "Regulatory 'Settlements': When Do Private Agreements Serve the Public Interest?") The presumption of conflict embodied in the "balancing" mission leads to compromises, but they can be compromises of private interests rather than advances of the public interest.

***Passivity:*** A commission that balances private interests risks presiding rather than leading. Outcomes are defined by the parties' desires, not the public's needs. The forum then serves the parties, rather than the parties serving the forum. The midpoint of two private interests is still a private interest. This regulatory passivity leaves the public unserved.

***Legal looseness:*** Regulatory proceedings are legal proceedings, bounded by statutes and constitutional law. Those legal sources do not address "interests"; they create rights and obligations. The regulatory responsibility, therefore, is not to balance "interests," but to (1) define the rights and obligations; and then (2) honor the rights and enforce the obligations. A mission of "balancing the interests of customers and investors" diverts the commission from its legal obligations. (Caveat: The occasional statute does contain a balancing type phrase in its preamble. In that limited context, my legal argument has less force. But even in those situations, the interests requiring balance are the rights and obligations created by statute (which the commission must define), not the self-interests advanced by the parties.)

## Regulatory Strategy: Determine How the Private Interests Diverge from the Public Interest, Then Shape Regulatory Solutions that Convert Divergence to Alignment

A regulator cannot ignore private interests. Administrative law gives everyone a voice. So how can regulators use private interests—rather than the other way around?

Start with skepticism. Private interest always claims the mantle of the public interest. A developer of wind farms, a builder of nuclear power plants—both promise "clean" and "green," but their real interest is profit from wind and nuclear construction. The industrial customer criticizes energy efficiency investments as impractical, but its private interest is to keep rates low. Private interest arguments also downplay public interests: Does the wind developer discuss transmission cost? Does the nuclear developer mention her federal loan guarantees, her statutory limit on accident liability, and her absence of answers on waste disposal?

Exemplifying the necessary private interest analysis is Stephen G. Hill's paper, "Private Equity Buyouts of Public Utilities: Preparation for Regulators" (NRRI 07 11). Hill analyzes the

motivations of each player (acquirer's investors; target's shareholders, bondholders, and management; acquisition lenders). He demonstrates their divergence from the public interest, then recommends regulatory actions that preserve the public-interest wheat but remove the private-interest chaff.

Regulators can move from balance to alignment by modifying traditional practices. Consider the typical "pre filing" meeting. Usually it begins like this:

Lobbyist: "I'm here to explain how my proposal advances the public interest."

Try substituting this:

Regulator: "First let's discuss my vision for the public's needs. Then let's explore how your private interest diverges. Then we'll take a look at your proposal."

Two different meetings, two different outcomes.

Another example: The typical regulatory opinion begins with recitations of parties' positions. One purpose of these pages is to satisfy reviewing courts that intervenors have been "heard." But the optical impression is that the proceeding's purpose is to serve these parties' interests. How different would be the impression if accompanying the required listing of intervener interests was an analysis of how each interest diverges from the public interest?

Over time, these two examples of procedural change can produce behavioral change. They can induce parties to educate rather than advocate, while encouraging regulators to probe rather than preside. The focus becomes molding a public-interest policy rather than "balancing" a private-interest conflict.