Utility Performance: Will We Know It When We See It?

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July 2010

Eight Obstacles on the Path to Performance

Docket control: Most docket items arise from utility proposals, which commissions must process within a statutory time limit. These factors combine with resource constraints to crowd out commission-initiated performance reviews.

Commissioner turnover: With terms averaging under four years, commissioners have less experience than the utility executives whose performance they must judge. That inexperience combines with humility to blunt the performance-assessment tool.

Expertise gap: A credible performance reviewer needs expertise equal to the utility. Because performance review has not had historical priority, this expertise level is not part of the regulatory infrastructure.

Resource gap: It remains regulation's unaddressed irony that commissions face hiring freezes and budget cuts to save taxpayer money, while utilities can hire the experts they need using ratepayer money. The resulting resource gap limits performance reviews. (For more on this problem, see essays Part One and Part Two of "Regulatory Resources: Does the Differential Make a Difference?")

Judicial restrictions: Some courts have limited commissions' authority to challenge or prescribe utility activities, citing the "managerial prerogative." (See the NRRI paper Are Utility Workforces Prepared for New Demands? Recommendations for State Commission Inquiries, pp. 28-38.) At their most confining, these judicial statements cause regulators to forsake standard setting in favor of cost disallowing—an action regulators hesitate to take for fear of weakening the utility.

Performance-finance tension: Utilities need capital, and sources of capital require predictable returns. Performance penalties make capital markets frown. How to signal capital markets that ratepayer dollars will flow, while conditioning that flow on high-quality performance, is a chronic struggle for regulators. The investment community's golden fleece is the "hospitable regulatory environment." Financial analysts strip-search commission decisions for evidence of dollar flow, unobstructed. There is a tendency to equate assessment with animosity, inquiry with inhospitability. This tendency, associated with short-term financial metrics, can discourage commissions from assessing long-term performance.

No consensus on standards or metrics: According to Evgenia Shumilkina's paper "Where Does Your Utility Stand? A Regulator's Guide to Defining and Measuring Performance," there is no regulatory consensus as to how to define or measure performance. Credible metrics are hard to design, and data hard to gather. These difficulties deter efforts to

compare performance among utilities, or to track their improvement or degradation over time. The problem perpetuates itself: Absent consensus on performance parameters, there is no performance conversation; absent conversation there is no progress on measuring and improving performance.

The competition-confidentiality connection: Even utilities with monopoly service rights face competitive entry—some dramatically so (such as wireline incumbents facing competition from wireless sellers). For these utilities, survival as monopoly providers can depend on their competitive success. Sharing data on their strengths and weaknesses creates competitive risk.

Five Ways to Reach a Better Balance

These eight factors cause great variation in the attention commissions pay to performance. The risk is that performance review occurs not continuously, incrementally, and professionally, but only after a major outage or cost overrun—when headlines and political intervention can distract from analysis. So—what are our options?

Define the desired performance. Performance covers many subject areas—safety, customer service, financial ratios, operating cost, plant output, innovation, asset management, management vision, workforce efficiency. Because advancing some objectives can detract from others, specifying priorities involves tough trade-offs. But the exercise produces mutual expectations, enabling the commission to hold its utilities accountable.

Condition approvals on performance. Rate increases may be required by statute, but so is performance. To grant rate increases when asked but assess performance only when things go wrong is asymmetrical. Every utility request—a certificate to build, a rate increase, a merger or divestiture—should be premised on a promise of improvement. Every commission approval, then, should be conditioned on evidence of achievement.

Embed performance in commission organization and processes. Successful businesses have divisions and processes devoted to quality control. This practice is worth replicating within commissions. A commission can put each utility on a public schedule for performance reviews, tracking improvement over time. Within a region, especially a region served by the same multi-state company, commissions can create interstate committees that construct a common vocabulary, then pool their knowledge and processes, even as the states vary in their weightings. This takes money—and statutes that enable the commission to raise that money.

Frame regulatory proceedings as performance inquiries; frame regulatory opinions as performance assessments. A commission is not a supermarket where parties shop for benefits. A commission is a regulatory agency, obligated to establish and enforce performance standards. It is true that statutes entitle parties to make requests and require commissions to respond. But the commission's response need not be confined by the party's request. That is the central difference between courts and commissions. Courts are confined to the parties' presentations; commissions are obliged to advance a larger public interest. (See the essay "Commissions are not Courts; Regulators are not Judges.") It takes extra work, but on receiving a request for rate increase, a

commission can require not only evidence of cost of operations, debt, and equity but also evidence of improvement in performance factors.

Bring Wall Street along. An Oregon utility executive once said, "Thank goodness for regulators; they save us from ourselves." In the long run, investor interests and ratepayer interests are aligned. Investors don't benefit from performance failure, or from a regulatory system that overlooks it. Because no monopoly position is permanent, strong good performance becomes market protection. If regulators send clear signals about expectations and consequences, this rigor will produce more benefit than cost.