

PRESIDE OR LEAD? THE ATTRIBUTES AND ACTIONS OF EFFECTIVE REGULATORS

by Scott Hempling, NRRI 2010

Reviewed by William A. Mogel*

This slim paperback (144 pages)¹ by Scott Hempling² packs in lots of provocative ideas in a collection of six essays.

Preside or Lead?'s lodestar is the following from *Scenic Hudson Preservation Conference v. FPC*:

[The] Commission[']s . . . role does not permit it to act as an umpire blandly calling balls and strikes . . . ; the right of the public must receive active and affirmative protection at the hands of the Commission.³

Preside or Lead?'s underlying assumption is that regulated companies often operate in ways inconsistent with the public interest. Consequently, regulators always must be on the alert to align "the utility's private behavior with the public interest."⁴ In Hempling's words,

The purposeful regulator does not seek to "compromise" . . . among private interests . . . [Instead the] effective regulator . . . establishes a centrifugal force [the public interest] . . . that disciplines private expectations and hems in private behavior.⁵

Preside Or Lead? is divided into six parts:

- I. Attributes of Effective Regulators: Purposefulness, Education, Decisiveness, Independence;
- II. Actions of Effective Regulators: Effective Regulators Don't "Balance" and "Preside;" They Set Standards and Lead;
- III. Obstacles to Effective Regulation: Politics, Conversational Confusion, Resource Differentials, and Framing;
- IV. Turf: Jurisdiction Is a Means, Not an End;
- V. "Five Minds for the Future": Can They Help Us Achieve Regulation's Purpose?; and
- VI. Effectiveness in Action.⁶

Part I suggests a unique definition of public interest - "a composite of economic efficiency, sympathetic gradualism, and political accountability."⁷ How that standard (especially sympathetic gradualism) would be applied by regulators asked to determine, for example, the "justness and reasonableness" of

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1. SCOTT HEMPLING, *PRESIDE OR LEAD? THE ATTRIBUTES AND ACTIONS OF EFFECTIVE REGULATORS* (NRRI 2010).

2. Mr. Hempling was the Executive Director of the National Regulatory Research Institute, a nonprofit organization created by U.S. regulatory commissions.

3. *Scenic Hudson Pres. Conference v. FPC*, 354 F.2d 608, 620 (2nd Cir. 1965) *cert. denied sub nom.* 384 U.S. 941 (1966).

4. HEMPLING, *supra* note 1, at 1.

5. *Id.* at 5.

6. Each section of *Preside or Lead?* opens with quotes from those not usually associated with utility regulation. In one instance, Mr. Hempling paraphrases President Kennedy: "Ask not how regulation can advance your private interest; ask how your private behavior can serve the public interest." *Id.* at 13-14.

7. *Id.* at 4.

a specific rate is unexplained. But like many of the other concepts in *Preside or Lead?*, this seeks to stimulate a re-thinking of what is the public interest.

Part II's thesis is that regulators should not act like judges, who preside, but should "lead." According to *Preside or Lead?*, acting like a judge undermines a regulator's effectiveness by *inter alia*: 1) "[i]nducing intellectual passivity" by allowing the proceeding to become "party-centric" rather than "public centric;"⁸ 2) "imposing the wrong time horizon (the parties' short-term desires rather than the public's long term needs);"⁹ and 3) "reducing the regulator's objectivity (because the regulator 'learns' the issues from the parties' arguments rather than impartial sources)."¹⁰ In Hempling's view, regulators should organize proceedings by asking, "[h]ow do we advance the public interest?"¹¹

Part III discusses two "obstacles to effective regulation"¹² - politics and legislatures. As for the latter, it is observed that regulators should "make the legislature-commission relationship a team relationship."¹³ How a regulatory commission can achieve a "team relationship" with the body that supervises it, approves the commission's budget, and often is responsible for confirming a commissioner's appointment, may be good theory but a goal difficult to implement.

Part IV opens with the following observation:

The U.S. Constitution gave America split-level government. Early-twentieth-century regulatory statutes reflected that eighteenth-century decision. Enacted when utilities were local, those states made most utility regulation local. In the ensuing decades, federal and state legislators layered new goals, rights, and obligations . . . without reexamining . . . the federal state relationship. Complicating the jurisdictional picture are two other factors: ideological shifts that accompany elections, and regulators' natural desire to use their powers to benefit constituents. The risk is that policymakers focus more on . . . turfism than on utility performance, on allocating costs rather than reducing costs.¹⁴

Agreed, but the challenge still remains cost allocation even if costs are reduced. Significantly, *Preside or Lead?* does not advocate that consumers get a "free ride" or be subsidized by the utility or its shareholders.

Part V is derived from Howard Gardner's 2006 book, *Five Minds for the Future*,¹⁵ with which I am not familiar. Hempling's discussion of the five minds identified by Gardner and their applicability to public utility regulation fill nearly twenty pages. Intended as advice for regulators, this essay is more philosophical than specific to issues confronting regulators.

Lastly, Part VI is devoted to a recent Order by the Maryland Public Service Commission¹⁶ which, according to *Preside or Lead?*, exemplifies

8. *Id.* at 23. It also is noted that "[a] settlement culture can induce regulatory passivity." *Id.* at 30.

9. *Id.* at 23.

10. *Id.*

11. *Id.* at 24.

12. Hempling notes that "[p]rivate and public interests are like Boolean circles with blurry boundaries." *Id.* at 60.

13. *Id.* at 67.

14. *Id.* at 93.

15. HOWARD GARDNER, FIVE MINDS FOR THE FUTURE (2006). The "minds" are disciplined, synthesizing, creative, respectful, and ethical. HEMPLING, *supra* note 1, at 115.

16. *Baltimore Gas & Elec.*, Case No. 9208, Order No. 83410 (Md. Pub. Serv. Comm'n, June 21, 2010).

“effectiveness” and employment of “all of Gardner’s five minds.”¹⁷ *Baltimore Gas and Electric*, Case No. 9208 (June 22, 2010) unanimously denied the utility’s proposal to recover \$858 million for deployment of smart grid initiatives via a tracker.¹⁸ The Maryland Commission held:

The Proposal asks BGE ratepayers to take significant financial and technological risks. . . all in exchange for savings that are largely indirect, highly contingent and a long way off. . . . The tracker virtually guarantees that the Company will recover . . . [the] costs associated with the Proposal, a profit for investors. . . . [With] the tracker in place, the Proposal is a “no lose proposition” for the Company and its investors.¹⁹

Preside or Lead?’s endorsement of the Maryland Commission’s decision is because it: 1) conditioned recovery on cost effectiveness; 2) did not ignore that before costs are “sunk” they should be compared with total benefits; 3) was not “snowed” by non-verifiable financial claims; 4) provided an open door for a modified proposal; and 5) gave meaning to “just and reasonable” by aligning benefits with costs.²⁰

In summary, *Preside or Lead?* is thought provoking. Not intended to be a primer or handbook on public utility regulation, it is a paean to regulators who are professionals, often out-manned and underappreciated.

17. HEMPLING, *supra* note 1, at 137.

18. I have written about the same case. William A. Mogel, *What Happened in Maryland: State Case Has National Implications for Grid Modernization*, PUB. UTIL. FORTNIGHTLY, Nov. 2010, at 8. In my article, I concluded that initially the PSC did not fairly consider all stakeholder interests, the impact on the utility, and the national policy favoring the “Smart Grid.” The Commission, however, asked that the Company submit an alternate proposal, which it later approved.

19. *Baltimore Gas & Elec.*, Case No. 9208, Order No. 83410, at 1, 3 (Md. Pub. Serv. Comm’n, June 21, 2010).

20. HEMPLING, *supra* note 1, at 142.