Secrecy and Utility Regulation

A utility regulator must comply with laws that require regulatory transparency, administrative justice, and freedom of information. Unfortunately, regulators are sometimes reluctant to operate in the sunshine. Administrative rules, such as requirements that ex parte *contacts be disclosed after the fact, are an essential part of the process of achieving administrative justice.*

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"Sunlight is said to be the best of disinfectants; electric light the most efficient policeman."
—Justice Brandeis[1]

I. Background

In the United States, the focus of industry practitioners is, and should be, on the substance of utility regulation. Because of the legal safeguards flowing from the U.S. Constitution down to the administrative law processes used in utility regulation, the basic fairness of the regulatory process can nearly always be taken for granted.[2] With credible regulatory institutions and processes in place, the focus can be on substantive regulatory issues, such as utility ratemaking, mergers, and competition.

Outside the U.S., however, administrative justice cannot be assumed. In many countries, it is not possible to judge the substance of regulation—only "insiders" to the regulatory process have access to the needed information and they may have incentives to use that knowledge strategically.[3] When policymakers establish regulatory

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institutions in those places, the first task is to eliminate the culture of secrecy. A regulatory agency that is well positioned to act in the public interest must be set up before the substance of utility regulation can proceed.

U.S. utility regulation provides an excellent model because of its emphasis on transparency and accountability. As new regulatory agencies are established, the first generation of utility regulators will have a crucial role in establishing administratively just regulatory procedures.

This is not to say that regulators are not tempted to make policy, but

> [r]egulators have traditionally walked, and must continue to walk, the fine line between pandering to public opinion and recognizing that decisions that lack broad public support (at least of the process by which those decisions were reached) are ultimately unsustainable.[4]

II. Administrative Justice

Utility regulation exists because of the need to protect utility customers from the harms that can result from an unregulated monopolist exercising monopoly power, providing inadequate, unsafe, or unreliable service, or blocking entry to its markets. The regulated entities must be treated reasonably as well given the need for efficient investment in utility infrastructure. Utility regulation is often described as a "balancing of interests," reached by "reference to common sense considerations of fairness between investors and consumers."[5]

The process of regulation matters. In the 1940s, in response to concerns about administrative "absolutism" and calls for greater openness in government, the existing administrative procedures were studied and reforms were recommended, culminating in enactment of the Administrative Procedure Act (APA) of 1946. Sen. Daniel Patrick Moynihan explained that:

> The APA rests on a constellation of ideas: government agencies should be required to keep the public informed of their organization, procedures, and rules; the public should be able to participate in the rule-making process; uniform standards should apply to all formal rule-making and adjudicatory proceedings; and judicial review should be available in certain circumstances. Taken together with the Freedom of Information Act, an amendment to the APA that was enacted in 1966 and added to in 1974, 1986, and 1996, the APA was intended to foster more open government through various procedural requirements and thus to promote greater accountability in decision making.[6]

The regulatory decision-making process must be "transparent" and "in the sunshine."

Regulation must be conducted in a reasonable manner, consistent with sound economic principles and applicable legal standards. Procedures must be fair. First, regulatory processes must be open, which can be accomplished by ensuring that the regulator's decisions, draft decisions, and record evidence are readily available to the public. The regulatory decision-making process must be "transparent" and "in the sunshine"—regulatory processes that are conducted in secrecy are not credible. Regulators should deliberate their final decisions in public and there should be workable constraints on *ex parte* communications, especially near the time when a final regulatory decision is being deliberated. Among other things, transparent regulation will provide a major constraint against corruption.[7]

Second, evidence in opposition to that provided by the utility is needed. The public interest is not likely to be served if the utility's position is the only evidence before the regulator.

Given the reluctance of many countries to create a consumer advocate, newly established regulatory agencies need to set up ways for the public to organize, intervene, have access to the utility's filing, attend pre-hearing conferences, and prepare written comments. Regulators need to be

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pro-active, finding ways to group like-minded intervenors together (perhaps by requiring them to appoint a spokesperson) in order to make them more influential participants in the regulatory process.

Third, a mix of informal and formal administrative processes are needed, beginning with workshops, conferences, and informal inquiries, and resorting to adjudicatory litigation, legislative-style hearings, and rulemaking processes when needed.[8]

Regulators have some discretion, limited by their statutory mandates, with regard to how they organize themselves, how they go about developing record evidence, and how they make their decisions—and they should use that discretion in ways that promote regulatory transparency and administrative justice.

III. Organizing a Regulatory Agency

A regulatory agency must be organized in a way that promotes administrative justice. Wilson explains that the "best time to achieve a mission-jurisdiction match is when the organization is created. An organization is like a fish in a coral reef: To survive, it needs to find a supportive ecological niche."[9] Policies aimed at promoting competition must be accompanied by reforms aimed at building credible regulatory institutions. From a very practical standpoint, the Global Corruption Report 2005 points out that "[c]ountries need good institutions that minimise the incentives public officials face to take bribes."[10]

Regulation is often described as a "quasi-judicial" process, with the regulator acting as a "judge," basing its decisions on the record evidence that is before it.[11] Regulatory agency staff may, in certain litigated cases, act as expert witnesses, providing record evidence in an advocacy/prosecutorial role. Meanwhile, other staff members will be acting in an advisory role to the regulator, administering regulatory hearings, assisting with the drafting of decisions and, generally, providing staff support to the regulator as it makes its decisions. The danger is that too much informal contact between advisory and advocacy/prosecutorial staff within the regulatory agency will reduce the fairness of the regulatory process. There is less structural separation between the "judge" and the "prosecutor" in a regulatory agency than would be the case in the judicial system. The role of staff is not to be a consumer advocate but rather to provide technical recommendations to the regulator. Regulatory staff is not acting as a "party" when it testifies, but rather is acting in an advisory role to the commissioners and providing that advice in public where its views can be examined and tested. Conflicts are inherent in this "quasi-judicial" context and must be dealt with in order to ensure that administrative processes are procedurally fair. After all, prosecutorial staff should not be the ones that assist in preparing the draft decision. Organizational separation of prosecutorial/advocacy staff is desirable.

Nor should the regulators be "lobbied" by parties or interested persons in the days immediately before a major decision is to be made.

IV. *Ex Parte* Communications

Secrecy and corruption go hand in hand—and, in many parts of the world, corruption is a major obstacle to fair utility regulation. Constraints on *ex parte* communications are a crucial part of ensuring that the regulatory process is credible.

In major rate case/tariff reviews, for example, where regulatory agency staff performs an advocacy/prosecutorial role by filing record evidence that analyzes the utility's positions and takes issue with them, where appropriate, the staff's expert witnesses should not be able to talk informally to the regulator about their positions, where witnesses for

parties in the proceeding cannot do so.

Nor should the regulators be "lobbied" by parties or interested persons in the days immediately before a major decision is to be made without, at an absolute minimum, disclosure of the *ex parte* communication after the fact. One of the very first things that a government will have to do when a regulatory agency is being established is to develop procedurally fair rules of practice and administrative procedure that detail the *ex parte* rules that the regulator will be required to use.

V. Checks on Regulatory Discretion

James Q. Wilson explains that the difference between U.S. regulatory agencies and their European counterparts stems, in part, from the Europeans' "more secure base of authority," with the U.S. institutional governance structure providing greater checks and balances on regulatory discretion.[12] Limits on regulatory discretion, which make clear the difference between policymaking and the implementation of policy, are necessary to provide the proper balance of autonomy and accountability.[13]

VI. The Long Walk to Freedom

A utility regulator must comply with laws that require regulatory transparency, administrative justice, and freedom of information.[14] Unfortunately, regulators are sometimes reluctant to operate in the sunshine. In South Africa, for example, the Truth and Reconciliation Commission, in its landmark 1998 Report, recognized that "[p]erhaps all governments are, to a greater or lesser extent, uncomfortable with the notion of transparency, preferring to operate beyond the glare of public scrutiny."[15] Administrative rules, such as requirements that *ex parte* contacts be disclosed after the fact, are an essential part of the process of achieving administrative justice.

Regulatory agencies need to have a clear mandate to perform their assigned regulatory tasks, while being required to:

> [T]ake a tough line: Insist that everything be on the public record, insist that everything be done "by the book," insist that "everybody be treated the same," and insist that the full force of the law fall on every violator.[16]■

Endnotes:

1. Louis D. Brandeis, *What Publicity Can Do*, in OTHER PEOPLE'S MONEY AND HOW THE BANKERS USE IT (Boston: Bedford Books, 1995) (1913–1914), at 89. First published in HARPER'S WEEKLY, Dec. 20, 1913.

2. In the rare exceptions, the U.S. Court system provides credible paths of appeal.

3. Max Weber explained that "[e]very bureaucracy seeks to increase the superiority of the professionally informed by keeping their knowledge and intentions secret. Bureaucratic administration always tends to be an administration of 'secret sessions': in so far as it can, it hides its knowledge and action from criticism." *See*: DANIEL PATRICK MOYNIHAN, SECRECY: THE AMERICAN EXPERIENCE (New Haven, Conn.: Yale Univ. Press, 1998), at 143, citing MAX WEBER, ECONOMY AND SOCIETY (M. Rheinstein, Ed. & Trans., Cambridge, MA: Harvard Univ. Press, 1954).

4. *Id.*

5. JAMES C. BONBRIGHT, PRINCIPLES OF PUBLIC UTILITY RATES (New York: Columbia Univ. Press, 1961), at 149.

6. Moynihan, *supra* note 3, at 157.

7. Francis Fukuyama explains that "[i]mproving governance by fighting corruption has institutional, normative, and political dimensions." Francis Fukuyama, "Foreward," *Global Corruption Report 2005*, Transparency International (London: Pluto Press, 2005), at xii. Available at http://www.globalcorruptionreport.org/download.html#download.

8. Wilson argues that the "institutional incentives to adopt a formalistic and adversarial mode in managing agency-interest relations are very strong." Wilson, *supra* note 4, at 301.

9. Wilson, *supra* note 4, at 188.

10. Fukuyama, *supra* note 8, at xii.

11. Stephen Breyer states that "most procedural requirements arise out of lawmakers' viewing the [regulatory] agency as a 'little court,' engaged in adjudication, or as a 'little legislature,' engaged in making rules." STEPHEN BREYER, REGULATION AND ITS REFORM (Cambridge, MA: Harvard Univ. Press, 1982), at 379.

12. Wilson notes that "[n]o agency head can ever achieve complete autonomy for his or her organization; politics require accountability, and democratic politics implies a particularly complex and all-encompassing pattern of accountability." JAMES Q. WILSON, BUREAUCRACY: WHAT GOVERNMENT AGENCIES DO AND WHY THEY DO IT (New York: Basic Books, 1989), at 188 and 301.

13. Tom Welch notes that "[r]egulators are creations of their

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legislatures, and should therefore resist the temptation to identify themselves as the makers—as distinct from the implementers—of public policy." THOMAS L. WELCH, REINVENTING ELECTRIC UTILITY REGULATION (Vienna, VA: PUR, 1995), at 199.

14. Thus, transparent utility regulation has a role to play in the long walk to freedom. Nelson Mandela points out that "[f]or to be free is not merely to cast off one's chains, but to live in a way that respects and enhances the freedom of others." *See* NELSON MANDELA, THE ILLUSTRATED LONG WALK TO FREEDOM: THE AUTOBIOGRAPHY OF NELSON MANDELA (London: Little Brown, 1994), at 202.

15. *Truth and Reconciliation Commission of South Africa Report*, Vol. 1 (London: Macmillan, 1998), at 207.

16. Wilson, *supra* note 4, at 300.

Discussing regulation approaches, James Q. Wilson has cited the Europeans' "more secure base of authority,"

market offering that, while at its early stages, is increasingly competitive with traditional telephone service.

25. In the Matter of Vonage Holdings Corporation Petition for Declaratory Ruling Concerning an Order of the Minnesota Public Utilities Commission, Memorandum Opinion and Order, 19 FCC Rcd 22404 (2004), *appeal docketed*, No. 05-71315 (9th Cir. Mar. 4, 2005).

26. *See generally* Matter of IP-Enabled Services, Notice of Proposed Rulemaking, 19 FCC Rcd 4863 (2004).

27. See Texas Office of the Attorney General, Press Release, Texas Attorney General Abbott Takes Legal Action to Protect Internet Phone Customers, Mar. 22, 2005 (announcing lawsuit against Vonage Communications, country's largest VoIP provider, for failing to make clear to consumers that the company's current service does not include access to traditional emergency 911 service), available at http://www.oag.state.tx.us/oagnews/release.php?id=850; Michigan Office of the Attorney General, Press Release, Cox Takes Action Against Vonage to Protect Internet Phone Customers, Apr. 29, 2005 (reporting that Vonage faces legal action for misleading consumers about the company's emergency 911 service), available at http://www.michigan.gov/ag/0,1607,7-164-34739-116865–,00.html; Communications Daily, Apr. 28, 2005 (reporting that FCC Chairman Martin testified at House Appropriations Subcommittee hearing that he directed FCC staff to accelerate timeframe for developing proposed regulations to make VoIP compliant with 911 service).

28. 47 USC § 1001, *et seq*.

29. Communications Assistance for Law Enforcement Act and Broadband Access and Services, Notice of Proposed Rulemaking, 19 FCC Rcd 15676 (2004).

30. *See generally* Availability of Advanced Telecommunications Capability in the United States, Fourth Report to Congress, 19 FCC Rcd 20540, 20555 (2004).

31. *See, e.g., AT&T Communs. of the Southwest, Inc. v. City of Dallas*, 52 F. Supp. 2d 763, 773 (D. Tex., 1999); *AT&T Communs., Inc. v. City of Dallas*, 52 F. Supp. 2d 756 (D. Tex., 1998).

32. *See, e.g.*, City of Portland, Oregon, Utility Franchise Management, available at http://www.portlandonline.com/index.cfm?c=33148.

33. 47 U.S.C. § 253.

34. See *Qwest v. City of Berkeley*, 146 F. Supp. 2d 1081, 1094-95 (D. Cal. 2001) (Section 253 applies only to the activities of common carriers).

Clarification:

Moynihan's Many Fine Sentiments Did Not Include This One

Recent contributor Wayne P. Olson writes:

In the hurly-burly of revising proofs, a quotation in my paper, *Secrecy and Utility Regulation* (May'05), was attributed to Sen. Patrick Moynihan rather than to Tom Welch, former chairman of the Maine Public Utilities Commission, in his book, *Reinventing Electric Utility Regulation* (Vienna, VA: PUR, 1995). Now, having his words credited to a distinguished policymaker, ambassador, academic, and author may not necessarily be a bad thing. But, to give credit where credit is due—and in the interest of accuracy and completeness—an expanded quotation and citation is provided below.

> [r]egulators are creations of their legislatures, and should therefore resist the temptation to identify themselves as the makers—as distinct from the implementers—of public policy. There is, nevertheless, such a broad area of discretion within which regulators have a free hand with respect to public policy that it would be foolish and disingenuous to pretend that public utility regulators are not integral to the process of government in the broad—and not merely the narrow—sense. Regulators have traditionally walked, and must continue to walk, the fine line between pandering to public opinion and recognizing that decisions that lack broad public support (at least of the process by which those decisions were reached) are ultimately unsustainable.

It is (perhaps) not inappropriate, at this juncture, to note that Chairman Welch did an exceptional job, during his tenure in Maine, in following this advice. Actions speak louder than words.