DEADLOCK IN PUBLIC UTILITY REGULATION

III. INEFFICIENT SERVICE

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Public service commissions have been followers rather than leaders. They have been too complacent at the people's expense. With few exceptions, they have done nothing to improve service or lower rates by developing better technical processes. :: :: :: :: ::

PREVIOUS articles in this series showed the fundamental difficulty of rate regulation to be that the commissions have not formulated exact policies and methods, that they have not determined definitely the amount of investment entitled to a return, and have not provided the machinery by which rates can be readily adjusted upward or downward according to changing conditions and requirements. The procedure is so cumbersome that prior to the war, except in comparatively few instances, rates were not reduced to the public with the cost of service; during the war they were not increased as they should have been to take reasonable account of extraordinary costs; and now with the ensuing price deflation they will not be diminished in accord with falling costs. The unwieldy practice on the one hand has failed to protect the public as was expected, and on the other has caused invisible confiscation by not granting rate increases when needed and particularly by destroying the credit of the companies.

RATES SHOULD HAVE BEEN LOWERED

The deadlock of regulation, however, applies not only to fixing and maintain-

ing reasonable rates, but also to requiring proper service. Besides fair rates, the commissions were intended to secure for the public the best possible service available under progressive standards of efficient operation. They were expected not only to require the companies to furnish adequate service, but to investigate methods of operation and to establish up-to-date economical management. In this they have failed signally; except in relatively few instances they have done nothing for the real improvement of service, such as requiring the retirement of antiquated or unsuitable plant and equipment, installing modern facilities, ordering reorganization of management, eliminating duplications and unjustified overheads, and particularly procuring economical purchase and use of materials.

The commissions are thus guilty of double neglect in the matter of rates: (1) for not providing effective machinery for direct rate making and (2) for not ordering changes in operation which would have resulted in reduction in costs to make possible the lowering of rates. I am convinced, for example, that in the state of New York, if the commissions had acted vigorously in procuring economical operation, they

could have reduced the cost of service on the average by 15 to 25 per cent. Besides their direct neglect in maintaining reasonable rates, they have not brought about large reductions in rates as they might have done, if they had exercised reasonably the duties and responsibilities entrusted to them as public bodies.

There is, of course, no definite statistical basis to show the extent that rates might have been reduced if the commissions had exercised their duty in establishing practicable economies. But among qualified technical men, who are thoroughly acquainted with the industries and who have been in close contact with regulation, the estimate of 15 to 25 per cent would be considered conservative, and that the reasonably possible reductions are considerably greater. The technical knowledge available for the reduction of costs has advanced with leaps during the past twenty years, but has been put to practical application only at snail's crawl. The companies are continuing to use out-of-date plant and equipment, to employ antiquated processes, to use unsuitable materials, and to continue waste motion and duplications.

The commissions, indeed, have been blissfully ignorant of the larger possibilities of efficiency. With few exceptions, they have neither investigated the technical processes employed by the companies, nor have known what better arrangements were available. Their technical staffs, to be sure, have understood more or less clearly the possibilities of improvement, but this has remained mostly a mental state, which has not reached the official commissions and has not resulted in action for improvements and reductions in costs.

THE CHICAGO GAS SITUATION AN EXCEPTION

There have been, fortunately, isolated instances where the commissions have shown by direct effort what might be done in the improvement of service and consequent reduction in costs and lowering of rates to consumers. A noted case is the investigation in 1918 of the production and distribution of gas in the city of Chicago. When the conditions of operation had reached a state threatening the financial collapse of the company, the public utility commission of Illinois instituted a thorough investigation, found a surprising lack of up-to-date facilities and methods, and finally succeeded in introducing improvements which resulted in a large decrease in costs and, if not in a direct reduction of rates, at least in preventing a 15 to 25 per cent increase. Moreover, incident to this investigation and to the direct effort to establish better conditions, there has been created a co-operative disposition between the commission and the company which has resulted in continuous economies, and in a better feeling between the company and the public.

For the most part, however, the commissions have permitted the out-of-date methods to continue and have disregarded their larger duties to the public. In gas and electric production, the companies are using generating plant and equipment which either are out of date or produce in too small units for economical output. In street railway operation, there is not only the excessive power cost, but the cars are antiquated and unsuited to their purpose. The commissions have done practically nothing toward investigating the possibilities, for example, of the light one-man cars, which promise to reduce cost in every direction—in the use of power, main-

tenance and depreciation, and particularly in cutting down the expense of labor. In most cities the old, heavy, two-men cars are continued, as are other unjustified processes, while at the same time the five-cent fare has been overwhelmed by the high costs of operation.

OBSELETE STANDARDS CONTINUED

There are also other important phases of neglected economy which do not pertain directly to the best methods under existing conditions, but involve the conditions themselves. To illustrate, in New York the statutes prescribe a standard of twenty-two candle power for the delivery of gas to consumers. This requirement was fixed in the law for the protection of consumers, at a time when the regulation was probably justified by the then preponderant use of gas for lighting and the character of the "burners" available for illumination. But gas now is used chiefly for cooking or other purposes in which heat and not illumination is needed; moreover, the heat standards are now readily applied also to lighting by use of special burners. The twenty-two candle power standard, therefore, is antiquated and, at present prices of oil which it requires, places utterly unjustified costs upon production. Gas engineers are agreed that the heat unit should replace the candle standard, which would mean an immediate reduction in cost at present prices of oil amounting at least to fifteen cents per thousand cubic feet of gas.

Now, in face of the fact that the candle standard is out of date and grossly uneconomical, the commissions have done practically nothing in bringing the situation clearly before the public and asking the legislature to change the law. The supposed pro-

tection of the candle power required is actually an imposition of excessive costs upon the public, and the larger duty of the commissions was to establish real protection. Similarly in other classes of service, the facts showing what should be done are not determined and positive action for improvement is not taken. What have the commissions done in finding the proper place of the "jitney" in local transportation and in working out a desirable policy for use of electric railways and motor buses? What have they accomplished in requiring co-operation between independent companies for more efficient production? In large cities, the elimination of small isolated companies with high operating costs? In larger systems, the simplification of the confusing and excessively costly inter-corporate relationships? In the establishment of proper labor policies? In any large matter which means improvement of service?

Instead of being positive factors in establishing better methods, there is indeed ground for argument that the commissions have actually retarded progress,—that advance in operation would have been greater without commission control, and that costs would be lower. This would be due in part to the strangling of credit which has prevented the companies from financing desirable improvements, but more particularly to the fact of rate restriction itself which has interfered with the normal and controlling force for progressive economical operation—taking away the hope of profits from skillful management.

PROFITS ELIMINATED—NO OTHER INCENTIVE DEVELOPED

In unregulated business, one of the principal factors of progress is, of course, the opportunity of greater

profit. In well-conducted business, operations are constantly studied with the purpose of lowering the cost in proportion to output and sales. There is constant investigation of plant and equipment to eliminate the antiquated and install the most economical for the lowest cost of production. This includes the location of the physical facilities, the routing of the processes, and the effective use of labor and materials consistent with quality and price. There is constant study of the financial organization, the interdependence of departments, the co-operation between the human elements, to keep overhead costs to an economic minimum and to stimulate productive activity to a maximum. This requires unremitting effort, which is sustained by the hope of profits and is rewarded by the greater gains of the business.

But the fact of rate regulation itself tends to eliminate the profit element of efficient management. The general policy is to restrict the return to a fair rate on the investment, and to the extent that this is consistently carried out in practice, the hope of gain to the company from progressive improvements is manifestly destroyed. If costs are reduced through skillful management, this would result in a corresponding reduction in rates to the consumers, and the company would get no greater return. With the reward thus eliminated, the management tends to continue on a dead level, putting into effect only such economies as can scarcely be avoided, not devoting serious efforts to such investigation and study as would characterize a private business in keeping improvements to a maximum.

That rate regulation has had such direct retarding influence upon operation is undoubtedly true, but the extent cannot be measured accurately or even approximately, and is easily exagger-

ated. For one thing, as complained in previous articles, regulation has not been at relentless attention to reduce rates at every possible occasion. While on paper it was expected to get for the benefit of consumers constantly the lowest possible rates, actually it has followed reductions in cost only tardily and partially, so that with improvements the companies have not been kept down to the bare bones of mere interest on investment. They have been able to get the benefit of a large proportion of the savings of management where such gains were actually realized.

Moreover, efficient management does not depend solely on the hope of direct financial reward; there are other fundamental factors of progress. Most of these, however, are of such intangible character that they are beyond the scope of this article and will not be further considered. But with all due allowance, rate regulation has undoubtedly produced a widely held feeling that vigor for the improvement of operation is not worth while, and the companies have unquestionably not maintained the greatest zeal to keep the business to the maximum possibilities of scientific operation. A wide-pervading psychology has tended to keep operation on a dead level, permitting the continuance or even the accumulation of undue costs in proportion to the possibilities of sincere and reasonable effort by the operators.

If it is true that rate regulation has had a substantial influence in retarding the development of economical management, the commissions should have exercised all the more their duty to keep track of operation and to require directly the installation of modern facilities, the employment of the best processes, the use of the most suitable materials, and the elimination of unjustified expenses. They should have

been constantly engaged, just as the leaders in private business, in examining the methods used by the companies and determining what, in fact, are the best practices, and then insisting upon all desirable changes. They should thus have kept informed of the progress of invention and have been constantly concerned with the practical application of scientific advance, acting as a clearing house of progress, enabling all the companies to install the best methods without vast duplication of investigation and experiment. They could doubtless have performed this great service chiefly through tactful co-operation with the companies, without direct use of authority, but if not they should have required outright the installation of the best plant and equipment and the use of the most economical processes of operation.

WHAT THE COMMISSIONS CAN DO

In justification of the inaction in these important matters of operation, it may be urged that, except as to ordering necessary service, the commissions for the most part have not had the legal power to interfere with operating methods. The actual management, it may be argued, was reserved to the companies, not subject to regulation. It is of course true that the commissions have not always had enough power to act adequately in matters of operation, and particularly have not been vested with the direct duty of requiring the companies to install the best facilities and most effective processes. Unfortunately, in some cases where they have sought to perform their larger duties in requiring economical service, they have met legal obstructions and tactical obstacles to frustrate their efforts.

But, with due allowance for lack of power, the clear purpose back of

all public utility legislation has been, unquestionably, to get for the people reasonable service at the lowest possible cost. For this purpose, the commissions have been endowed particularly with broad powers of investigation, being free to examine almost without limit the plant and equipment and the technical processes, and to determine in what respect these matters are below the best practicable standards. With such determination of facts, they could have obtained the desired improvements, in most instances through suggestions, pointing out clearly where economies may be instituted, and indicating a helpful disposition to bringing them about.

But even where commissions have not had final power to order desirable improvements and cannot obtain the voluntary co-operation of the companies, they can employ the pressure of publicity by placing the facts clearly before the public and awaiting the reaction upon the management. In any event, however, they are not absolved from the fundamental responsibility of procuring reasonable service at the lowest possible rates, and if they cannot obtain practicable efficiencies through co-operative ways or force of publicity, they should place the facts squarely before the legislature and ask for requisite power to deal adequately with the situation. They are intended to be expert bodies not only to administer the specific terms of the law, but to carry out its spirit, and to make recommendations where the law should be changed for the public interest.

The commissions are inevitably the repository of the public interest and are responsible for the development of desirable policy in a difficult technical field of economic service. They cannot dodge responsibility for their woeful neglect by pleading lack of specific power under the law.