REMARKS OF COMMISSIONER JOHN A. CARVER, JR., FEDERAL POWER COMMISSION, BEFORE THE PACIFIC COAST GAS ASSOCIATION IN LOS ANGELES, CALIFORNIA, SEPTEMBER 7, 1967, 10 a.m.

My predecessor on the Commission spoke to this group three years ago under the title "Producer Regulation--Its Impact on the Retail Distributor." Few, I think, would remember exactly what he said here; but that he did speak here and discussed a public issue candidly is now legal history. His Coronado speech was the basis for a producer motion in the Permian case 1/ to disqualify him for having prejudged that case, which motion was pursued in the courts. It was dismissed in the Tenth Circuit, but Supreme Court certiorari has been granted in that case (although certainly not on this point). Still, the issue he discussed remains a central one: is the producer market effectively competitive?

A week after Dave Black spoke to you, Chairman Swidler spoke to the Independent Natural Gas Association of America (INGAA). His title was "The Public Interest in Effective Natural Gas Regulation," and thereafter he, too, found the Court of Appeals urged to reverse the Commission for his alleged prejudgment.

The annual convention cycle has turned a time or two, and now your group and INGAA are again listening to FPC Commissioners in the same week. Carl Bagge was at San Francisco a few days ago, speaking on competition in regulated industries.

With an eye to history, I note that your program people also feel that this is a currently important subject--and I too shall discuss the subject. I hope both our remarks are sufficiently sanitized of the prejudgment taint leveled at Commissioners Black and Swidler.

What I have to say about competition I will bury in the middle of the speech stew which I've concocted for you today. The quality of its ingredients are my responsibility, but the recipe was furnished to me by your Mr. Joe Rensch. His list of five topics from which I might choose was at first discarded, and for six weeks I labored over a topic which I thought superior. But I concluded that while my labors might possibly eventually lead to something of interest to the editor of a law review desperate for something in utility law, they weren't producing anything that would pass muster here. So, at the last minute, I returned to the five topics and found them good--I'm going to talk about all of them.

1/ 34 FPC 158; 35 FPC 639; 375 F.2d 6 (CA 10).
Here they are: First, Should Regulation be Active or Passive? Second, What can be done about Regulatory Delay? Third, Discuss the Role of Competition in FPC Regulation. Fourth, What Responsibility does FPC have as to Availability of Adequate Energy Supplies? Fifth, What can be done to Improve the Gas Industry Image to the Investor?

I've been with the Commission one year. If I weren't a Federal Power Commissioner, my answers to each of these questions at best would be interesting, and at worst dull—in neither case of much importance. However, I am a Commissioner and these questions, when presented to me and my colleagues in actual cases, call for answers or views which count because they are expressed in the process of deciding.

The first question asks whether regulation should be active or passive.

In regulation, as in conservation and some other fields, people react in a conditioned way to verbal stimuli. Some words are bad—not for etymological or philological reasons, for words are neutral—but because they evoke bad associations.

In this sense, in the American political tradition, "active" is a good word, and "passive" is a bad word. All of us would rather be called active than passive. We must lay aside the adjectives "active" and "passive" and examine what issues really exist.

I see a real issue in an idea which has surfaced in opinions and dissents, and have expressed my reluctance to expand the Commission's jurisdictional reach by the process of interpretation. In Florida Gas, 2/ the contention that "commingling" brought a producer sale to an electric utility within the sale for resale clause of the Natural Gas Act was rejected by the Commission in an opinion I signed for the majority. This might be characterized as "passive" but the conditioning efficacy of the interstate transportation clause of the same act was restated and reinforced in the same case. In Florida Power & Light, 3/ a dissent which I signed for a 2-member minority, I refused to join in the application of the electrical equivalent of commingling to bring a Florida utility within the reach of the Federal Power Act, thirteen years after its passage. I said that in my view "our adjudicative responsibilities do not turn upon what the law ought to be, but upon what it is."


Again in dissent, in Algonquin, 4/ (whose fact situation I sketch briefly later in this speech), I decried an interpretative extension of our statute. And in El Paso, 5/ I said that the Commission was applying an improper test of the public interest in imposing an in-line concept to reduce the price of gas imported into the United States.

The bedrock upon which that peculiar institution, the regulatory commission, must anchor its actions is its legislative charter. If commissions are not bound to honor this principle meticulously, if they tack and shift to the exigencies and opportunities of the day, they contribute to the erosion of principles more fundamental than the supposed merit of regulatory activism, namely the principle that we are a government of laws. If our statutes are outmoded, or ineffectual, it is up to us to recommend the appropriate changes to the elected Congress.

I like being active, and as a regulator, the kind who keeps abreast of technological, economic and social changes in our country and who tries to understand all of the energy picture, for nothing less will permit the true understanding of that part of it which is committed to our jurisdiction. All five of us, in different ways and times, question old and entrenched ideas and precedents and our meetings are lively, intense, and contribute to airing the most elusive aspects of uniformly difficult cases submitted to us.

In such a general framework, let me turn briefly to the specific questions which were presented to me in connection with this general subject:

Is there an increasing trend towards modification of contractual arrangements and applications before the Commission, and towards substituting Commission judgment for that of the contracting parties?

Finding "trends" is an exercise for economists and statisticians. It is demonstrable that the conditioning authority of the Commission is applied with greater attention to details of operation, and greater intrusion into "management prerogative" than was the case five, ten, or twenty years ago. But this "trend" is, in my view, quite unrelated to the question of a trend toward more active regulation, and is much


more related to the completion of the phase of getting natural gas service to the whole country, the increasing population, growing urbanization, greater affluence, and like factors. In this context, even though I may complain about over-extended regulation in specific cases, I would not want to infer that I feel that the exercise of the Commission's powers generally have gone too far. I believe that the Commission not only properly has extended the depth of its activities, but will continue to extend it. Such is the price we pay for the complexities of our technological age.

Several questions are posed about the effect of Scenic Hudson, 6/ including whether it is applicable to gas certificate cases?

In Scenic Hudson Preservation Conference v. FPC, the Commission had licensed Consolidated Edison to construct a pumped storage generating project in New York. On appeal from a citizen group concerned with the aesthetic impact of that decision, the Commission was reversed, and ordered to consider certain alternatives posed by the citizen-intervenors. The Court said:

If the Commission is properly to discharge its duty in this regard, the record on which it bases its determination must be complete. The petitioners and the public at large have a right to demand this completeness. It is our view, and we find, that the Commission has failed to compile a record which is sufficient to support its decision. The Commission has ignored certain relevant factors and failed to make a thorough study of possible alternatives to the Storm King project. While the courts have no authority to concern themselves with the policies of the Commission, it is their duty to see to it that the Commission's decisions receive that careful consideration which the statute contemplates . . .

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In this case, as in many others, the Commission has claimed to be the representative of the public interest. This rule does not permit it to act as an umpire blandly calling balls and strikes for adversaries appearing before it; the right of the public must receive active and affirmative protection at the hands of the Commission. . . . The Commission must see to it that the

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record is complete. The Commission has an affirmative duty to inquire into and consider all relevant facts.

The language of the Court of Appeals was general, and applies to gas certificate cases as well as electric licensing cases, to other administrative agencies as well as the FPC. It has been reinforced by Supreme Court language in another electric licensing case, Udall v. FPC (High Mountain Sheep), 7/ and in my mind amounts to the addition of a new dimension to the administrative process. It is of particular importance, I think, for you to be aware that executive, legislative and judicial branches of the government are responding to the public's heightened awareness of environmental quality considerations in public and quasi-public decision-making.

Should the Commission work toward master planning of a national pipeline grid to avoid cross-hauling and duplication?

A little later in this speech, I shall discuss duplication under the title of competition in regulated industry. I may have partially answered the question by mentioning our responsibility to act, but also to make recommendations to Congress. Still, our certification responsibilities have always carried the seed of this issue. The FPC and every regulatory agency gives much thought to the desirability of better planning.

Regulatory delay, question number two, is the most vexatious of the frustrations of regulation. It is the hardest to justify and the easiest to apply of administrative techniques. It costs money, probably more than we dare count; the taint of staleness contributes to further staleness, as regulators postpone ever further the day of making decisions on stale records; and when economic or other pressures become irresistible, the oldest case paradoxically may be the least considered.

The Senate Judiciary Committee and the House Government Operations Committee, among others, have labored valiantly to quantify and analyze administrative delay. It is my own view that the problems are more substantive than procedural, and likely to get worse rather than better.

For example, we can show in the FPC remarkable progress in the streamlining and expediting of noncontested cases; but the ratio of contested to uncontested cases is increasing, and the time delays of the contested cases is getting inexorably longer.

This is because the issues are more complex and the competition is keener. More interests have both the standing and the resources to intervene, and raise ever-more sophisticated issues.

7/ Udall v. FPC (High Mountain Sheep), U.S. Supreme Court Nos. 462 and 463, October 1966 decided June 5, 1967.
The scope of the concept of "aggrievement" has been judicially broadened, reflected in the Scenic Hudson case which I mentioned earlier, and the United Church of Christ 8/ case. Intervention raises its own issues, requiring determination by the agency of the nature of the aid to be rendered in the solution of a public interest question--itself a controverted factual issue.

The many kinds of delay in the administrative process are difficult to categorize. The producer certificate cases, prior to the adoption of the area approach, were so numerous as to have required decades to unravel by old procedures. An enduring monument of the administration of Chairman Swidler was the devising and implementation of a subordinate regulatory system to apply while the primary system of producer regulation was being worked out.

If I am right in believing that substantive, not procedural or administrative problems are at the root of the lengthening of the time lag in our cases, then it must be conceded that something more than getting more people and working them harder is required to keep regulation responsive to the demands of modern society upon it. For example, if society demands a review of right-of-way plans which encroach upon aesthetic values, and the state agencies either do not do it, or don't do it satisfactorily, then a federal agency is likely to find itself with a new substantive issue as to which it must devise new procedures, admit new kinds of witnesses, and otherwise contribute to a more complex, difficult, and time-consuming process.

It is in this direction that the problems of FPC and most administrative agencies are proliferating.

I firmly believe that the independent agency approach to these problems is both wise and sound. A single administrative czar might be able to handle some of them more quickly, but the checks and balances of the agency approach in my views more nearly correspond to the ideals of fairness and of competitive interplay than such an alternative.

I've also been asked about the effect of amendments to the Administrative Procedure Act now before the Congress.

Some of these amendments are designed to ameliorate some of the problems of delay, but the Commission, and most practitioners before the Commission, question this premise.

I have mixed feelings about this subject, for I sympathize both with the objectives of those who would amend the Act, and those who object that the proposed amendments will not serve the objective. What we have is a paradox: It is in procedures, what we call due process, that rights are protected, but it is also in procedure and process that rights are stifled by delay. Procedures are both a sword and a shield. The challenge to all regulatory agencies is to understand this paradox, and to keep in mind always the objective of doing justice as promptly as the circumstances permit.

The third question concerns competition in a regulated industry, the subject which I mentioned in opening this talk. Traditional utility regulatory theory has no trouble with this question for under traditional theory, competition and regulation are antithetical. Of course, this theory is inapplicable: in a whole array of ways, competition is applied in regulation—intramodally and intermodally. It is both a situation to be dealt with, and an objective to be sought.

The Algonquin case divided the Commission. In that case, the long-time supplier of the Hartford, Connecticut, gas needs was denied a requested certificate to construct facilities to serve a new suburban area and to upgrade its service in the northern portion of its service area. Instead, a new supplier was brought in to the proceedings on the Commission's motion, and ordered to connect and serve some of the Hartford requirements. Competition in regulation is what that case was about.

Whether the objective of competition was served by the Commission's order, is discussed in my dissent. That dissent discloses my concern about preserving real competition in a regulated industry.

One paragraph of my dissent contains general views about how the question of competition ought to be approached:

No challenge faces regulation greater than that related to recognizing and accommodating to competitive forces, both within the natural gas industry and from other fuel sources. This challenge will require the broadest perspective, the greatest vision. Now is not the time to return to the simplistic test of cheaper rates, or formulary views about the wisdom of having multiple supply sources. The problem is really a great deal more complex than the Commission today recognizes.

A subordinate question you have asked me on this subject is whether in the light of increasing competition with other sources of energy, management should be permitted
greater freedom of rate design. I have found the rate design question to be central to the problem of regulation within the gas industry. In Atlantic Seaboard, 9/ I said the Commission "must recognize that it is possible for adverse and discriminatory results to follow if regulatory concern does not go beyond the mere opening of markets to second suppliers, to look at the real problem, namely rate design."

Not just in utilities, but in transportation and communications, rate design is the responsibility of management in the first instance. I am perhaps not fully qualified to render critical judgment, but on a preliminary basis I think I would have to say that I think that management has not fully exercised the tool of rate design.

The Federal Power Commission, as you know, regulates production and transportation, but not distribution of natural gas. Producers are regulated on the premise of an absence of effective competition. In Permian, the prescribed remedy was the fixing of ceiling prices for gas at the well head. At the other end of the pipeline, where sales of gas for resale also take place under regulatory scrutiny, the desirability of effective market competition is met with a quite different remedy, namely the conscious fostering of competition by certificating new facilities by new suppliers.

The Federal Power Commission, besides regulating production and sales for resale at the market end, also regulates transportation of gas in interstate commerce. Under section 7(c), which requires a finding of public convenience and necessity before new facilities can be installed in jurisdictional situations, the Commission has had to consider the relative advantages of competition versus facilities duplication in major pipeline projects.

Each case has to be considered on its own merits. In a dissent, Commissioner Ross points up Commission failure (in his view) to give sufficient consideration to the alternative of ordering the competing parties to share a line. This was Northern Natural 10/ and the Commission's majority assured that it was not deciding "that joint transportation facilities can never be shown to be more in the public interest than separate facilities."

In Great Lakes, 11/ a unanimous Commission emphasized

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enhancement of competition as a desirable off-shoot of certifying facilities to take Canadian gas across the United States.

These are not unique dilemmas. Every state regulatory agency has to deal with equivalent situations on a bread-and-butter daily basis.

The fourth question asks what responsibility the Commission has as to the availability of adequate energy supplies? Certainly not the whole responsibility, but a most vital one.

The Federal Power Commission has several kinds of considerations to take into account. It has the responsibility of providing a producer price adequate to assure a level of exploration that will meet the needs of an expanding market for natural gas. It requires pipelines to show reserves and deliverability and this contributes to the incentive for further exploration. Natural gas supplies almost a third of the energy needs of the United States. By no means all of this is "jurisdictional" but enough of it is either jurisdictional, or is associated with jurisdictional situations (most importantly in the supplies expected to come from the Offshore areas under federal control) to make it perfectly safe to say that the role of the Federal Power Commission in assuring an adequate supply is vitally important.

Not to be overlooked, of course, is the role which natural gas plays in the generation of electricity, also a concern of the regulatory activities of this Commission.

On the other hand, it can never be forgotten that gas is often associated with oil, as to which a totally different regulatory pattern exists. It has been said that while in the case of crude oil, production is controlled and prices are free, in the case of natural gas, production is free and prices controlled.

This paradox oversimplifies a complex situation. The Federal Power Commission, though it has wide responsibility, has no authority over the petroleum industry as such, and it is in the context of the petroleum industry that most investment decisions to yield the necessary supplies of natural gas are made.

This bring us to the fifth and last question on the list, which is what can be done to improve the gas industry image to the investor. The investor is the key man, because in our free enterprise economy, we have so far looked to the private money market, not to public money, for this effort. The regulators can certainly polish up the image of the industry to investors by eliminating as much of the uncertainty surrounding regulatory actions as is humanly possible.
Industry can help by fostering the recognition of itself as aggressively and intelligently managed.

To avoid the pitfalls of my predecessor, let me turn the discussion of this subject away from FPC, and direct it to the recent decision of one of our sister agencies, the Federal Communications Commission. It, too, accepts the responsibility of fixing a rate which will "sustain the financial integrity of [the] business and enable [it] to attract capital" but without giving weight to the ambitions of the speculator. 12/ This is not the same as fixing the price, as the FPC must do in producer cases, but it comes out to the same thing in the sense of which we are now speaking.

In the AT&T case, the FCC Commissioners were not divided in result on establishing a rate of return in the range of seven to seven and one-half percent, but they expressed divergent views about how they had respectively reached this conclusion. One commissioner, for example, complained that the FCC had not reached the heart of the matter, which in his view lay "in devising an approach that will provide the maximum incentives to the regulated company to achieve efficiency and economy in operation." 13/ This, he said, "is not achieved by imposing the strictest regulatory oversight or the most detailed regulatory supervision and control." 13/ He called for close supervision of the rate base and operating costs, but a wide range of fluctuation in the rate of return.

This puts a finger on the essential nature of the argument. In a talk to the Midwestern Association of Rail and Utility Commissioners, I analogized the variations of view on rate of return to a spectrum, ranging from a "hands-off approach, which would open the question of rate of return infrequently" to the "eagle-eye" Commission "poised to pounce".

I am grateful to FCC Commissioner Loevinger for straightening me out on a lapse in reasoning. If I understand his statement correctly, a more accurate description of the spectrum would recognize that firm regulation can succeed as well by concentration on the components of the rate base as on the control of profits. In this redefinition commissioners with a rigidity of view about how high the rate of return might go might indeed be the lax regulators.

13/ Concurring Opinion of Commissioner Loevinger at p. 5, American Telephone & Telegraph Co., supra.
It is inevitable that the Federal Power Commission will be traversing the road just negotiated (even if only preliminarily) by the Federal Communications Commission. The policy, or mystique, on rate of return and matters associated with it, will be opened again for public scrutiny and comment, as well as for court review. Consequently, it is not appropriate for me to suggest what I would decide, beyond repeating the generalities I've already indulged: one of them is that regulators have a vital role in the economic well-being of our complex system. We owe it to ourselves to develop and use analytical techniques which will test, reinforce, or destroy old theories. Boldness and inventiveness in this area are not conventional virtues, but being in the kitchen of regulation is a privilege worthy of the pain of the heat.