Principles of Public Utility Rates

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COMPETITIVE PRICE AS A NORM OF RATE REGULATION

Before turning in the next chapter to those unorthodox principles of rate making often called "social theories," we may consider the merits of a general standard of reasonable rates that has received at least verbal support both from public service commissions [1] and from public utility spokesmen.[2] This is the standard of the hypothetical competitive price. Regulation, it is said, is a substitute for competition. Hence its objective should be to compel a regulated enterprise, despite its possession of complete or partial monopoly, to charge rates approximating those which it would charge if free from regulation but subject to the market forces of competition. In short, regulation should be not only a substitute for competition, but a closely imitative substitute.

[1] "The purpose of regulatory policy, in the protection which it is designed to afford the consumer, is to simulate and substitute the effects of competition and give the consumer the benefit which he would derive from a system of competition." From National Association of Railroad and Utility Commissioners, Report of the Committee on Progress in Public Utility Regulation, *Proceedings of the 53d Convention* (Washington, D.C., 1942), p. 369. Many commission opinions and a number of judicial dicta could be cited to the same effect.

[2] "The justification for the regulation of utility rates being the absence of competition, regulation should aim to produce the same results as competition would do if competition were economically desirable and feasible—neither more nor less." Brief for the New York Telephone Company in a case insisting upon its right, under the New York statutes, to receive the benefit of a "fair value" rate base that gives weight to reproduction costs. New York Telephone Co. v. Public Service Commission, 142 N.Y. Supp. 569 (1956). The brief cites, as supporting a competitive-price standard of reasonable pricing, Walter A. Morton, "Rate of Return and the Value of Money in Public Utilities," 28 *Land Economics* 91–131 (1952) and Arthur H. Dean, "Provision for Capital Exhaustion under Changing Price Levels," 65 *Harvard Law Review* 1339 (1954). See also C. P. Guercken, "An Economic Appraisal of the Private Electric Utility Industry," 55 *Public Utilities Fortnightly* 739–754 (1955).