

Role of the Regulator in Encouraging Investment in the Natural Gas Sector

The Value of an Independent/Impartial Regulator
Conflicting Regulatory Signals/Investors Expectations

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Presentation 11 -- Role of the Regulator in Encouraging Investment in the Natural Gas Sector

The Value of an Independent/Impartial Regulator Conflicting Regulatory Signals/Investors Expectations

- The regulator functions independently while balancing the interests of the public and the regulated.
- The regulator must resist influences or persuasive arguments that are inconsistent with this balance.
- The regulator must have the ability to utilize experience, education, and training to reach clear regulatory decisions.
- The regulator must have the strength to make decisions that may be unpopular.

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- The better regulatory environment is one in which the regulator is independent.
- Regulators must be prepared to receive different types of arguments that attempt to direct regulatory judgment, such as:

“our company must receive a favorable decision to remain viable”

“a decision along those lines will adversely impact our bond rating”

“we need this relief to remain competitive”

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- Investors need clear signals from the regulator in order to properly proceed with certain investment and infrastructure.
- Regulatory decisions regarding investment may be guided by certain statutory restrictions, such as preapproval statutes or siting laws.
- Regulators may decide that certain internal management decisions are best left to the utility.
- The regulator should consider performance based incentives in the regulatory process.

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- In setting rates for public utility services, a regulatory commission must consider both a utility's financial integrity and the consumer's right to dependable and reliable service at reasonable rates. (Accounting for Public Utilities, Hahne-Aliff)
- Utilities must be able to demonstrate that certain plant investments are used and useful and prudent.
- Rate of Return (when multiplied by rate base) should provide a return that is intended to allow a utility (1) to meet its obligations to present capital investors (interest and dividends) and (2) to compete on reasonable terms in the financial markets for future capital requirements. Bluefield Water Works & Improvement Co. v. West Virginia Public Service Commission, 262 US 679 (1923) (fair rate of return); Federal Power Commission v. Hope Natural Gas Co., 320 US 591 (1944) (end result doctrine)



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- “A public utility is entitled to such rates as will permit it to earn a return on the value of the property which it employs for the convenience of the public equal to that generally being made at the same time and in the same general part of the country on investments in other business undertakings which are attended by corresponding risks and uncertainties; but it has no constitutional right to profits such as are realized or anticipated in highly profitable enterprises or speculative ventures. The return should be reasonably sufficient to assure confidence in the financial soundness of the utility and should be adequate, under efficient and economical management, to maintain and support its credit and enable it to raise the money necessary for the proper discharge of its public duties. A rate of return may be reasonable at one time and become too high or too low by changes affecting opportunities for investment, the money market and business conditions generally.” (Bluefield case at pg. 692)

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Bluefield Principles

- Capital attraction
- Credit
- Financial soundness (financial integrity)
- Efficient management
- Comparable Companies (corresponding risks)
- Currently Earned Returns

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- Cost of Capital Concepts
- Cost of Debt Concepts
- Cost of Preferred Stock Concepts
- Return on Common Equity Concepts

The Value of an Independent/Impartial Regulator Conflicting Regulatory Signals/Investors Expectations

- “Independence is happiness” (Susan B. Anthony)
- “Solitude is Independence” (Herman Hesse)
- “Independence is loyalty to one’s best self and principles” (Mark Twain)
- “Let all your views in life be directed to solid, however moderate, independence; without it no man can be happy” (author unknown)