1921

Importance of the accounting department under Commission regulation

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THE IMPORTANCE OF THE ACCOUNTING DEPARTMENT UNDER COMMISSION REGULATION.


Never in the history of the world was the Accounting Department of a Public Utility, or for that matter the Accounting Department of any business or industry, more important than at present. Volumes could and have been written regarding the importance of accounting. Our subject is, however, confined to “The Importance of The Accounting Department under Commission Regulation.”

Perhaps, therefore, it would be well for us to study somewhat the last two words of our subject “Commission Regulation” so as to get the full connection between them and the Accounting Department.

Regulation, in a broad sense, is not new. Before the dawn of the Christian Era the grain trade was rigidly regulated in Rome, even as to price. The butcher and the baker were held in check by regulation as far back as the Middle Ages, and the innkeepers and common carriers have been regulated from the beginning of Anglo-Saxon civilization.

The old law of self-preservation, or self-preferment, is the fundamental cause for regulation. Since man was created, each one of us prefers his own advantage—it is the natural inclination with any combination of men. It asserts itself in
competitive business. Perhaps it is just as apt to assert itself in a public utility which is essentially monopolistic. In the absence of restraint and regulation the public utility has, and naturally enough, become the jury and the judge between itself and its patrons. It was because of this tendency that Commission Regulation was established, and originally the entire object of Commission Regulation was to enforce fair dealing between the monopoly and its patrons. But for a long time the regulating bodies insisted only on the "fair dealing" by the monopoly and ignored similar dealing by its patrons. Thanks be, both the regulating powers and the public utilities have broadened their vision and a fine spirit of co-operation is beginning to exist. Gone forever is the old popular idea that the only function of the Regulating Commission consisted of protecting the public against the utility so that the customers will pay the least possible amount for the product supplied by the public utility. It is indeed most fortunate that the tendency of all Public Utility Commissions today is to recognize that public utilities are entitled to similar rates of income as other industrial business and that the function of a regulating body is two-fold: not only must it protect the public from paying rates that may be in excess of the requirements of the company but the regulators have a duty toward the company to protect it and secure for it such rates as will not only pay operating expenses and fixed charges but yield a reasonable return upon investment, thus insuring and encouraging capital to invest and develop the business. A growing appreciation of this latter function is distinctly shown in the tenor of the language used by many of the Commissions when handing down recent decisions on requests for increased rates.

It is only within comparatively few years that the importance of accurate accounting has been given the place it deserves. This is probably more true in the case of public utilities than in that of privately owned industries.

The general power of regulation of a Public Utility Commission is stated in the most comprehensive fashion by the Illinois Public Utility Commission Law. The following is an
excerpt quoted from that law:

“The Commission shall have general supervision of all public utilities, shall inquire into the management of the business and shall keep itself informed as to the manner and method in which the business is conducted. It shall examine such public utilities and keep informed as to their general condition, their franchises, capitalization, rates and other charges, and the manner in which their plants, equipments, and other property owned, leased, controlled, or operated, are managed, conducted and operated, not only with respect to the adequacy, security and accommodation afforded by their service but also with respect to their compliance with the provisions of this act and any other law, with the orders of the commission and with the charter and franchise requirements.”

The following quotation from the Wisconsin Public Utilities Act is found in most jurisdictions and sets forth the nature of the powers invested in Commissions in so far as they are essential to the proper performance of their duty.

“The commission or any commissioner or any person employed by the commission for that purpose shall, upon demand, have the right to inspect the books, accounts, papers, records and memoranda of any public utility in relation to its business and affairs.”

In at least twenty-eight jurisdictions there are provisions for the regulation of accounts. And the Commissions are given authority to examine as well as to prescribe accounts. Further, the Commissioners and their duly authorized agents or examiners, may have access to the accounts of utilities and may at all reasonable times examine and inspect them.

A just and proper regulation of any utility can be achieved and maintained only when and where it is based upon complete information relating to the utility regulated.

The financial statements and reports emanating from the Accounting Department are the best sources of information the Public Utility Commission has to enable it to act wisely on any question of finance which may be presented to it.

The importance of the Accounting Department under Com-
mission Regulation is, therefore, almost self-evident; for from the Accounting Department issues practically all of the information from which the Public Utilities Commission may judge and inform itself of the general condition, capitalization, just and equitable rates; yes, even to the management of the Company, for good or poor management is absolutely sure to be reflected in the accounts of the Company. The Commission are also able to judge from the figures and reports presented by the Accounting Department how the plants, equipment and other property are conducted and operated as well as the service rendered by the Company.

As almost every Public Service Commission is empowered to inspect the books, accounts, records, etc., of any public utility, it is absolutely necessary that the personnel of the Accounting Department be of a high order. The accountants must be positive that their figures are correct; that they reflect facts without equivocation, and that these facts are so correlated that they are readily understood. Further, it is of the utmost importance that the Accounting Department of any public utility have the respect and full confidence of the Commission. Only by accurate, clear and honest accounting can this confidence be gained and retained.

During the past few years the cost of operating public utilities has mounted to so high a figure as to be almost unbelievable. Even the managers of the business have hesitated to accept the Accounting Department's figures. And at no time in our history has it been so important to know positively the cost of operation as during the last two or three years.

I cannot refrain from setting down here in order to illustrate the point which I have just made, a story I once heard Charles Schwab tell.

When Charlie Schwab was first made manager of the Carnegie Steel Works he came to Andrew Carnegie one day in great glee and said, "Mr. Carnegie, we made $600,000 net profit last month!" Mr. Carnegie replied, "I don't care how much you made. Show me what it cost you to make it."
While it is certain in our minds that Public Utility Commissions do care "how much we make" it certainly has been borne in upon us that they want to be shown what it cost.

To gain these ends public service regulation has been made to cover three great subjects:—capitalization, rates and service.

**Capitalization**

Capitalization embraces the authorization by the Commission to issue stock, bonds and other long-term securities for the purpose of obtaining money for proper capital purposes. Many States now give the Public Utility Commission or regulating body the authority to supervise the issue of stocks and bonds. Capital issues, of course, must be based upon capital expenditures of the company and here again the Accounting Department is of the utmost importance. It must be in a position to furnish conclusive evidence to the Commission in clear-cut statements of the exact amount expended, properly subdivided into the different plant accounts. This is not only necessary from the point of the financial condition of the company but from the point of the judgment of the Commission in rendering decisions as to the right to issue against these expenditures.

**Rates**

All of the States now give Public Utilities Commissions mandatory powers with respect to rates.

Let me quote from a recent decision of the Wisconsin Commission:

"Every effort honestly put forth, every dollar properly expended, and every obligation legitimately incurred in the establishment of an efficient public utility business must be taken into consideration in the making of rates for such business."

It is self-evident that nowhere but in the Accounting Department is found the *record* of every honest effort, every dollar properly expended and every obligation legitimately incurred.
The rate a public utility receives is its life-blood. We all know that it has been almost impossible during the past four or five years to receive a reasonable rate for our product. We may differ in opinion at times with our Public Utility Commission as to what constitutes a reasonable rate but in general we can all agree, I think, that a reasonable rate under normal conditions is a rate that will provide for all operating expenses, including depreciation, and interest on borrowed money, all overhead charges, and a fair return to those persons whose money made it possible to build and equip the plant—commonly called stockholders.

Rates are not regulated either upward or downward by any present-day Commission just for the asking. The burden of proof of the justice of a rate, however, always lies with the utility. This proof must come from the Accounting Department. Therefore, if the utility is to maintain constantly a reasonable rate the Accounting Department must be ready at any time to supply indisputable figures as to the costs.

The importance of the Accounting Department under Commission Regulation cannot be too strongly urged upon the management, and those who have realized this fact have been able to sail their craft through much less stormy seas than those who have not.

Service

In the matter of service it should be plain that no service should be required which the revenues of the Company do not justify. By this I do not mean that no service should be required which does not give a return equal to its cost included in this cost of proper overhead charges. It might be that the Company is bound to furnish some service irrespective of the profit or loss resulting therefrom. However, in the long run, unless the Company can reimburse itself for operating expenses out of that particular service, it should never be required. It is, of course, of the utmost importance that accounting should be so performed that an accurate cost of service can be ob-
tained. To find the exact cost of a given service is, however, one of the most difficult operations with which an accountant has to contend. The injuries wrought by inadequate service to the public may be as serious as those caused by unjust rates.

Publicity

One of the most important elements of regulation is that there should be complete publicity of all corporate financial transactions. The operations of a public utility must and should be an open book to both the Commission and the public. This publicity is essential for the general public as well as for the stockholders and creditors of the Corporation. Few there are, now, who dispute either the propriety or necessity of publicity of financial transactions of public utilities. However, there can be no true publicity without accurate and correct accounting. Therefore, it follows that to make publicity of substantial value the accounts of public utilities must be kept accurately, skillfully, scientifically, honestly and according to a prescribed system. If this is done the Commissions, the public and the management will have implicit faith that the figures prepared by the Accounting Department set forth "the truth, the whole truth and nothing but the truth."

Conclusion

Perhaps in this paper I have not presented any really new facts nor have I so eloquently expressed the ideas that I could apply to them the lines of Lowell:

"Though old the thought and oft expressed,
'Tis his at last who says it best."

I have striven in this short paper to write down a few principal reasons for "The Importance of the Accounting Department under Commission Regulation."

That Department is, it seems to me, the workshop where are fashioned the tools, in the form of cold, hard, honest facts, on which every Commission must depend in the attainment of a just and equitable regulation of affairs between the public utility and the public which that utility serves. In striving for
the ideal of such regulation the high water mark attained by any Commission will be determined to a large extent by the skill and intelligence of the Accounting Department. Lack of skill, slip-shod methods or other incompetence there, will vitiate and nullify in large degree the honest efforts of the most competent Commission and thus rob both the public and the utility of that last full measure of fair dealing to which they are entitled and which Commissions are created to achieve.