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**Introduction**

There is little doubt that Judge Robert Bork’s reputation as a constitutional scholar depends in large measure on his passionate defense of the general doctrine of judicial restraint on all constitutional matters, both large and small. One remarkable departure from that basic posture was his notable 1987 decision in *Jersey Central Power & Light Co v Federal Energy Regulatory Commission.* The opinion followed on the heels of two earlier decisions on the same question, both of which were subsequently vacated. At issue in the case was the question of whether Jersey Central was entitled to include in its rate base the $397 million of investment that were lost when the utility suspended construction of a nuclear power facility at Forked River, New Jersey. The project had been previously authorized some ten years earlier when both state and federal authorities feared an energy shortage brought on by a combination of the rising price of oil in the aftermath of the formation of OPEC and the high demand for energy to fuel the expanding economy. It was understood that, given the long lags between the time that a project is approved and the time it goes online, planning had to be done in...
advance.5 “All parties agree[d] that Jersey Central’s investment at Forked River was prudent when made.”6 For a variety of reasons those predictions did not pan out. In part, conservation efforts reduced the demand for power.7 “Furthermore, the protracted litigation and political controversy which attended the construction of nuclear power projects resulted in extensive delays and dramatic increases in their ultimate cost. Thus, many investments [including Forked River] which were prudent, indeed considered essential, when made, have now by necessity been cancelled.”8 Clearly, no one factor drove the decision to cancel the project.

In dealing with this issue in Jersey Central I,9 a unanimous panel upheld the Federal Energy Regulatory Commission’s denial.10 But in Jersey Central II,11 Judge Bork and then-Judge Ruth Bader Ginsburg switched course and held that Jersey Central was entitled to constitutional protection not only with respect to the proper rate of return, but also with respect to the definition of the rate base on which that return was to be calculated.12 The great question in the eyes of many was how Robert Bork could have written this decision given his passionate defense of the principle of judicial restraint on constitutional matters. But a close look at Jersey Central’s relationship both with Lochner v New York,13 a case so often the subject of Bork’s ire, and the more general question of judicial restraint, largely exonerates Bork from the charge of a fatal intellectual inconsistency.

I. BORK ON JUDICIAL RESTRAINT

Bork made no effort to conceal his general hostility to judicial activism. As a personal matter, I can recall attending in December 1983 a conference held at the University of San Diego School of Law on constitutional law that dealt with a variety of economic issues. I presented at the conference what eventually

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5 Id at 1170–71.
6 Id at 1171.
7 Jersey Central, 810 F2d at 1171.
8 Id.
9 730 F2d 816 (DC Cir 1984) (Jersey Central I).
10 Id at 824.
11 768 F2d 1500 (DC Cir 1985) (Jersey Central II), vacd 776 F2d 364 (1985).
12 Jersey Central II, 768 F2d at 1502 (“After re-examining the issue, we are now persuaded that the end result test applies to both the calculation of the rate of return on invested assets and to the calculation of the proper rate base.”).
13 198 US 45 (1905).
became an article that I wrote for The University of Chicago Law Review entitled Toward a Revitalization of the Contract Clause.\textsuperscript{14} The article essentially attacked the dominance of the rational basis standard of review in cases testing the limits of the Contract Clause of the United States Constitution, which provides simply: “No State shall . . . pass any . . . Law impairing the Obligation of Contracts.”\textsuperscript{15} My own views are not my concern here. What was of interest at the conference, however, was Bork’s response to the effort to salvage some measure of constitutional protection.

There was a sharp disjunction between Bork’s views of antitrust laws\textsuperscript{16} and his views of constitutional law, where during his years at the Yale Law School he fell under the influence of his generation’s most distinguished defender of the principle of judicial restraint, Professor Alexander Bickel, whose constitutional masterpiece was The Least Dangerous Branch, published in 1962.\textsuperscript{17} Bork often encapsulated his objection to constitutional overreach in his fierce opposition to the majority opinion of Justice Rufus Peckham in Lochner, a case sustaining a challenge to a sixty-hour maximum-hour law. Indeed, at the San Diego conference I remember vividly the verbal formulation that Bork articulated in stating his standard of review in these Contract Clause–type settings: so long as some defender of the statute could utter with a straight face a rationale for the law that he knew to be wrong, the statute was in Bork’s view constitutional. His views on this subject never diminished, and he took the occasion in his 1990 bestselling book (which had some choice

\begin{thebibliography}{9}
\bibitem{15}US Const Art I, § 10, cl 1. The Clause reads in full:
\begin{quote}
No State shall enter into any Treaty, Alliance, or Confederation; grant Letters of Marque and Reprisal; coin Money; emit Bills of Credit; make any Thing but gold and silver Coin a Tender in Payment of Debts; pass any Bill of Attainder, ex post facto Law, or Law impairing the Obligation of Contracts, or grant any Title of Nobility.
\end{quote}
\bibitem{17}Alexander M. Bickel, The Least Dangerous Branch: The Supreme Court at the Bar of Politics (Bobbs-Merrill 1962).
\end{thebibliography}
words about my own misguided judicial philosophy\textsuperscript{18} to attack \textit{Lochner} as an abomination that “lives in the law as the symbol, indeed the quintessence of judicial usurpation of power.”\textsuperscript{19}

It therefore came as something of a surprise that, when faced with another claim for the constitutional protection of property, Bork ultimately came out squarely on the opposite side of the question in \textit{Jersey Central}. Bork, writing for the majority, found that the court had the power to overturn the Federal Energy Regulatory Commission when it set confiscatory rates for the public utility.\textsuperscript{20} Bork himself was keenly aware of the possibility that he would be attacked in \textit{Jersey Central II} for a supposed conversion to Lochnerism. Although \textit{Lochner} did not surface in the final decision in \textit{Jersey Central}, it had arisen earlier when Bork was attacked by his fellow University of Chicago Law School alumnus Judge Abner Mikva for falling into the \textit{Lochner} trap just by deigning to look closely at the rate challenge.\textsuperscript{21} To that challenge, Bork had responded as follows:

Unlimbering the ultimate malediction of legal debate, the dissent accuses us of regressing to the jurisprudence of \textit{Lochner v. New York}. Had we committed any such enormity, we would of course deserve the anathema pronounced upon us. But this seems disproportionate since our sin consists in nothing more than taking seriously the admonition of \textit{Hope Natural Gas}, which is quite a different thing from reviving \textit{Lochner}.\textsuperscript{22}

On this point, Bork was clearly correct. Matters of rate-making may raise many issues in common with the economic liberty cases like \textit{Lochner}, but serious differences separate them.\textsuperscript{23} In dealing with \textit{Lochner}, the issues of health, safety, and worker exploitation were never far from the surface of the debate. But the issues in all rate making cases are solely financial, without any of these explosive components. In dealing with this issue, moreover, it is clear that the major possibility for abuse

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\textsuperscript{19} Id at 44–46.

\textsuperscript{20} \textit{Jersey Central}, 810 F2d at 1178–79.

\textsuperscript{21} See \textit{Jersey Central II}, 768 F2d at 1513 (Mikva dissenting).

\textsuperscript{22} Id at 1504 (citation omitted).

lies with the government in its regulation of public utilities and not with the utility whose rates are regulated. These companies have to make extensive, irreversible investments in their facilities before they can recover any revenues from their customers. So they face the very real problem that, once the investments are completed, the legislature will set rates so low that the public utility could never, over the life of its plant, recover its initial investment with a suitable rate of return.

II. FUNDAMENTAL CHOICES IN RATE REGULATION

At this point, rate regulation has to steer a middle path. The common justification for rate regulation, which Bork accepted in Jersey Central II, is that no public utility is entitled to earn the monopoly rate of return on its invested capital, which it could acquire from its customer base who (certainly at the time) has no alternative place to look for power. Yet at the same point, public utilities have a right to be protected against confiscatory rates.24

The issue then arises of just how to accomplish this task. On this point, there were two main lines of authority, the first of which dated back to Smyth v Ames,25 which held that the utility could include in its rate base only those expenditures that were used and useful in the business.26 In effect, the basic argument was that the utility had to have incentives to behave as if it were a firm in a competitive market. Competitive firms do not recover on investments that don’t pan out, and the same should be true of a regulated public utility—hence, the Smyth approach’s possible line-by-line review of each claimed expenditure. But the quid pro quo for that proposition is that the rate of return on the assets that do qualify for inclusion in the rate base should be set high enough to offset the risk they would become unproductive, which is just what happens in a competitive market.27 So the Smyth v Ames solution featured a small rate base with an upward adjustment in the rate of return. It is worth adding, moreover, that Smyth never did address the precise point at issue in this case, namely that assets would fall out of the rate base.

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24 See Jersey Central II, 768 F2d at 1503.
25 169 US 466 (1898).
26 Id at 546.
because of political opposition or environmental regulation as opposed to an unwise or unsuccessful firm investment.

There are of course difficulties with this particular argument. Someone has to decide which assets are in and which are out. Once that is done, it becomes necessary to figure out the suitable rate of return on these assets. In principle, it could be claimed that the process is infected with a fatal form of circularity because no one can figure out the “fair value” of the assets without first knowing the revenues that they will generate.\textsuperscript{28} But it is just those revenues that have to be set on the basis of a fair-value determination. I do not think that this difficulty is insuperable. The initial benchmark is the risk-adjusted rate of return in competitive industries. Once that is calculated, the appropriate response is to reduce the utility’s rate of return to take into account its relative insulation from competition.

Be that as it may, Justice William O. Douglas in \textit{Federal Power Commission v Hope Natural Gas Co}\textsuperscript{29} took the position that the right way to compute rates was to avoid the complexities of these line-by-line calculations by changing both the rate base and the method for calculating the rate of return.\textsuperscript{30} The new rate base was the total capital invested in the business.\textsuperscript{31} The new rate of return was reduced to reflect that the risk of imprudent investments was now shifted to the rate payers.\textsuperscript{32} In effect the only task left for the Court was to see whether the “end result” of this process met constitutional standards of review:

The rate-making process under the Act, i.e., the fixing of “just and reasonable” rates, involves a balancing of the investor and the consumer interests. Thus we stated in the \textit{Natural Gas Pipeline Co.} case that “regulation does not

\textsuperscript{28} Justice Louis Brandeis put the point thusly:

The rule of \textit{Smyth v. Ames} sets the laborious and baffling task of finding the present value of the utility. It is impossible to find an exchange value for a utility, since utilities, unlike merchandise or land, are not commonly bought and sold in the market. Nor can the present value of the utility be determined by capitalizing its net earnings, since the earnings are determined, in large measure, by the rate which the company will be permitted to charge; and, thus, the vicious circle would be encountered.


\textsuperscript{29} 320 US 591 (1944).

\textsuperscript{30} Id at 603.

\textsuperscript{31} Id at 624.

\textsuperscript{32} Id at 622.
insure that the business shall produce net revenues.” But such considerations aside, the investor interest has a legitimate concern with the financial integrity of the company whose rates are being regulated. From the investor or company point of view it is important that there be enough revenue not only for operating expenses but also for the capital costs of the business. These include service on the debt and dividends on the stock. By that standard the return to the equity owner should be commensurate with returns on investments in other enterprises having corresponding risks. That return, moreover, should be sufficient to assure confidence in the financial integrity of the enterprise, so as to maintain its credit and to attract capital.\textsuperscript{33}

The adoption of this standard thus gives rise to the question of what standard of constitutional scrutiny should be given to these rate determinations. In one sense, the standard is pliable because it allows both methods of rate making to be used at the discretion of the legislature. But it is critical to note that the choice is between two internally consistent methods. It is not a rule that tolerates the selection of the narrow rate base coupled with the limited rate of return. The rule therefore rests on a composite of two distinct standards. There is a lot of slack on the way in which the end result is reached, but there is far less slack on what that end result must be. In this regard, the second component almost looks like a strict scrutiny standard, which sets this case apart from the standard view that rational basis review governs rate regulation. The instructive contrast on this part is between \textit{Hope Natural Gas}, which has some teeth, and \textit{Yakus v United States},\textsuperscript{34} decided some two months later, which reverted to the lower rational basis test for a comprehensive system of national price controls.\textsuperscript{35} In \textit{Yakus}, the regulated parties did not have any invested capital, which triggered the rate-of-return inquiry in \textit{Hope Natural Gas}.\textsuperscript{36} Similarly, Justice Douglas in \textit{Hope Natural Gas} also distinguished \textit{Nebbia v New York},\textsuperscript{37} which adopted a rational basis standard of review for state laws

\textsuperscript{33} \textit{Hope Natural Gas}, 320 US at 603 (citations omitted).
\textsuperscript{34} 321 US 414 (1944).
\textsuperscript{35} Id at 457.
\textsuperscript{36} See id at 431; \textit{Hope Natural Gas}, 320 US at 604–05.
that set minimum prices for dairy products.\textsuperscript{38} That decision represents the inveterate progressive impulse to foster cartels and monopolies. But that criticism is beside the key point, which is that the regulatory protection of these dairy farmers could not pose any risk of confiscatory rate making that did not allow them to recoup their cost of capital.

\section*{III. Bork in \textit{Jersey Central}}

It was against this background that Bork had to decide what should be done given the decision of the New Jersey rate makers to disallow the recovery by \textit{Jersey Central} of the investment that it lost when the utility cancelled its project. On this score, Bork got the first point correct when he wrote as follows:

\begin{quote}
At oral argument before the \textit{en banc} court, counsel for the Commission indicated that the "end result" test did allow a court to set aside a rate order when the company would otherwise go bankrupt and the Commission had refused to take that into account. The source of this constricted standard is elusive, not to say invisible. \textit{Hope Natural Gas} talks not of an interest in avoiding bankruptcy, but an interest in maintaining access to capital markets, the ability to pay dividends, and general financial integrity. While companies about to go bankrupt would certainly see such interests threatened, companies less imminently imperiled will sometimes be able to make that claim as well. \textit{Jersey Central} alleges that it is such a company. The contention that no company that is not clearly headed for bankruptcy has a judicially enforceable right to have its financial status considered when its rates are determined must be rejected.\textsuperscript{39}
\end{quote}

The point is of no little significance because it protects those public utilities that have low debt-to-equity ratios from confiscatory rates. Ideally, in a competitive industry, a firm will have full control over its debt-to-equity ratio, at least if it can get its lenders to go along. There is, moreover, no reason to think that the firm will not move to get the right amount of borrowed capital. But once rate protection is tied to the threat of bankruptcy, the entire calculus switches: the astute firm will increase its borrowing to the maximum level allowed, which in turn will

\textsuperscript{38} \textit{Nebbia}, 291 US at 537.

\textsuperscript{39} \textit{Jersey Central}, 810 F2d at 1180.
increase the risk of bankruptcy. Liquidation for a public utility does not work, as it must be kept as a going concern. A transfer of control does not work because there is no way to foreclose on the utility’s assets, given that banks do not know how to run these operations. Hence the high debt service allows the utility to increase its rates to service the debts. The higher leverage in turn helps increase the return on the smaller equity base. There is, however, no reason at all to allow this form of strategic behavior, which the Bork decision neatly blocks.

It is therefore evident that Bork did some real good in curbing his own natural instincts toward judicial restraint. But the question still remains whether he went far enough. On this issue, I would fault him on two separate grounds. The first, hinted at above, is that I do not think that he, or for that matter the dissent, came to grips with the reason that the Forked River project cratered. In traditional rate-making hearings the business risks that public utilities declare are their estimated costs of construction or the demand for their services. These declared uncertainties are reflected in the approved rate. In this instance, the source of uncertainty did not lie in these traditional marketplace activities, but in the entire set of political protests and general regulations that came quite literally from nowhere. If these had been anticipated correctly, the choice between the Hope standard and the Smyth standard would not have mattered. The risk would have been factored in from the beginning so that the overall rate structure would have moved upward to compensate the utility for that risk.

The entire situation is completely unnerving because there is no reason to think that any public utility can control future political or regulatory risks to the same degree that it can control the costs of its own construction. The purpose of “used and useful” is to incentivize the firm to make prudent investments in its own business. In the Forked River project, the party who needed disciplining was not the utility but the political activists and the various regulators at the federal, state, and local levels who could inject huge uncertainties into the project. Figuring out where the blame lies is no easy decision, but rather is a matter of complex apportionment that no one dealing with the case was prepared to undertake. Would the plant have operated in a less politically charged environment? The answer to that question

40 See id at 1171.
has to be yes, which is not to say that the fundamental economics had nothing to do with this particular decision. But it does indicate that the consideration of changed circumstances cannot be put to one side in thinking about these issues.

Bork did not reach that conclusion in this case. Rather, what he did was remand the entire matter back to the lower court for an evidentiary hearing on how the rate-base issue should be decided. 41 Indeed, one serious difficulty with this result is that it meshes only imperfectly with the Hope Natural Gas test, a point that became clear two years later when the Supreme Court faced the same issue of cost recovery for canceled projects. In Duquesne Light Co v Barasch, 42 Chief Justice William Rehnquist concluded that no separate adjustment had to be made for these cancelled expenditures so long as the bottom-line rate of return was within the band of reasonableness under Hope Natural Gas, which in that case it was. 43 From the record, it appears as though he would have reached a different conclusion in Jersey Central, where the underlying financial position was a lot more perilous. 44 It is worth noting, moreover, that after the public utility lost the case, the state reversed the outcome by statute to allow the inclusion of these expenditures in the rate base. 45

CONCLUSION

The entire episode shows something about the difficulty of the rate-making problem, and about Bork as a judge. Although he was often transfixed by the rhetoric of judicial restraint, he was not a prisoner to his own doctrine, and in at least one case

41 Id at 1187–88.
43 See id at 310, quoting Hope Natural Gas, 320 US at 602.
44 Compare Duquesne Light Co, 488 US at 312 (noting that “[n]o argument has been made that these slightly reduced rates jeopardize the financial integrity of the companies”), with Jersey Central, 810 F2d at 1198 (noting that Jersey Central “faced financial distress”).
45 The Pennsylvania electric-generation market has since been restructured to more effectively resemble a competitive market. However, the new law still includes references to a utility company’s ability to continue to recover in their rate base “transition or stranded costs” that “traditionally would be recoverable under a regulated environment but which may not be recoverable in a competitive electric generation market.” 66 Pa Cons Stat Ann § 2803. See also 28 Pa Cons Stat § 2804(4)(v) (“[T]he utility shall not be required to reduce its capped rates below the capped level upon the complaint of any party if the commission determines that any excess earnings achieved under the cap are being utilized to mitigate transition or stranded costs . . . .”)
pushed back against the dominant practice of denying any serious constitutional review in rate-making cases. I for one think that he did not get to the bottom of a very difficult problem, but he is nonetheless to be commended for seeking to place principled limits on government power. He was right, of course, that the case was distinguishable from *Lochner* in terms of its judicial pedigree. But it is very much an open question whether his harsh and habitual denunciations of *Lochner* had any intellectual heft behind them. As the *Lochner* Court saw the matter, the New York state maximum-hour laws were a disguised effort to stifle competition in labor markets.\footnote{See *Lochner*, 198 US at 64.} Bork’s own extensive contributions to antitrust law should at least have led him to ask whether the anticompetitive issue really mattered. David Bernstein’s recent book *Rehabilitating Lochner: Defending Individual Rights against Progressive Reform* shows just how powerful those anticompetitive instincts were, and how unholy the alliance was between the unions and the large bakeries that sought to drive recent-immigrant bakers from the market.\footnote{David E. Bernstein, *Rehabilitating Lochner: Defending Individual Rights against Progressive Reform* 30 (Chicago 2011): [T]he bakers’ union conceived of and promoted the hours legislation not simply to address health concerns, but also to drive small bakeshops that employed recent immigrants out of the industry. The union also encouraged selective enforcement of the law against nonunion bakeries. Large corporate bakers, meanwhile, supported and also benefited from the maximum-hours legislation invalidated in *Lochner*.} The clear anticompetitive impact of this legislation cannot be ignored by anyone who takes the antitrust law seriously. Yet somehow Bork never put the two pieces together. Nor was he able to see the manifest tension between his devotion to judicial restraint and the cause of open markets and free competition. In *Jersey Central*, Bork made a solid effort to work out one facet of this problem. But it is unfortunate that, owing to his strong priors, Bork did not integrate *Jersey Central* with any larger vision of constitutional interpretation.