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THE USE OF ACCOUNTING INFORMATION IN GOVERNMENTAL REGULATION AND PUBLIC ADMINISTRATION: THE IMPACT OF JOHN R. COMMONS AND EARLY INSTITUTIONAL ECONOMISTS

Abstract: This paper examines the socio-political process by which an ensemble of such calculative practices and techniques as accounting came to be developed, adopted, and justified within turn-of-the-century public administration. We are particularly concerned with examining the influence of John R. Commons and other early institutional economists during this Progressive era. Using primary and secondary archival materials, our purpose is to make three main contributions to the literature. First, the paper explores Commons' contribution to the debates over "value" which seems to be somewhat unique in that he explicitly recognized that there exists no unproblematic, intrinsic measure of value, but rather that it must be socially constituted as "reasonable" with reference to common law. To illustrate this point, this paper explores Commons' role in the historical development and implementation of rate of return regulation for utilities. Second, the paper describes the contradictory role accounting played during this period in ostensibly fostering administrative objectivity while accommodating a more pragmatic rhetoric of "realpolitik" in its development and deployment. The third contribution is to establish a linkage between current work in economics and accounting concerned with utility regulation and the debates of ninety years ago, noting that

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Commons' contribution has not been fully explored or recognized within the accounting literature.

INTRODUCTION

A myriad of such social innovations as workmen's compensation, social security, unemployment insurance, and utility and industrial regulation had their origins within the combined intellectual/political base of John R. Commons' institutional school of economics at the University of Wisconsin, and Governor Robert La Follette's Progressive party in the State of Wisconsin. Wisconsin's efforts, in turn, became the epicenter of socio-public administrative experimentation and served as a model for reform by other states and the federal government [Roosevelt, 1912, pp. v-ix; Kolko, 1963, pp. 212-216]. The stated purposes of this combined intellectual/political base were to modify the government's role in response to changing social as well as technical/industrial conditions, and simultaneously engender and benefit from the efficient administration of the American political economy.

Hays [1959, pp. 261-276] has suggested that the turn-of-the-century Progressive movement attracted institutional economists like John R. Commons who advocated the "rational" deployment of public resources, supported by a complex of such rationalizing techniques as accounting, to solve broad social problems. This movement served to legitimize a system of decision making based on calculated criteria thought to be objective, rational and above the give-and-take of political maneuvering. It made the political seem apolitical [Rose, 1977, pp. 68-71]; it took the debatable beyond the realm of open debate [Hopwood, 1984, pp. 170-176]; and it differentiated the political and immoral from the objective and merely factual [Zucker, 1977, pp. 733-738; Miller and O'Leary, 1990, pp. 492-498]. This movement sought to substitute and legitimize one system of decision-making — the one inherent in the spirit of modern science, technology and business — for another — the one inherent in stylized but subjective exchanges among overtly political social actors. Decision making and control became a more calculative, procedurally-oriented process, involving measurement and prediction, that invoked business techniques for directing the course of events toward predictable and stable outcomes [Kolko, 1963, pp. 1-10]. This shift moved decision making away from the local government to the larger networks of human interaction, and it achieved more than legitimate a new form of decision making; it also transferred power to the central executive office [Wilson, 1956, pp. 88-117]. As Hays [1959, pp. 261-276] suggested, an examination of the Progressive movement illuminates not so much the *content* of public policy, but the *nature* of the resulting political structure and the *types* of interactions peculiar to it.

The primary purpose of our paper is to trace the intellectual underpinnings of John R. Commons' institutional economics in order to appreciate the impact of Commons' work on the use of accounting information in turn-of-the-century governmental regulation and public administration.[1] It is proposed that John Commons joined such other pragmatists of the era as John Dewey [1910, 1922] and Thorstein Veblen [1904, 1919] to critique the inequities created by the concentration of wealth during the late nineteenth century, as embodied in such monopolies as railroads and utilities. However, departing both from pragmatists who contended that the "pecuniary calculus of accounting" was dysfunctional to the interests of society [e.g., Merino, 1993, p. 164] *and* from propriety theorists of the era who disclaimed responsibility for the concept of "value", Commons [e.g., 1907a, pp. 1-18; 1910, pp. 215-217] sought to abstract accounting practice from the private sector, transform it by developing the concept of "reasonable value" and the corresponding "rate of return," and then apply them to the regulate private sector monopolies which he saw as harmful but necessary.

The remainder of this paper is organized into three sections. Within the first section, Commons' work is briefly contextualized with reference to neo-classical economics, and other pragmatists and accounting theorists of the Progressive era. This contextualization of Commons' work also details Commons' approach to institutional economics and its relationship to the Social Gospel Movement. In section two, we describe and problematize Commons' concepts of physical valuation and rate

[1] Although a comprehensive analysis is beyond the scope of this paper, Commons' writings span a range of matters which may be broadly classified as dealing with the question of *governance*. In *Proportional Representation and Representative Democracy* [1900] he dealt with the question of political order (i.e., representation in government); in *A Sociological Theory of Sovereignty* [1965], *Social Reform and the Church* [1894], and *Races and Immigrants in America* [1920], he dealt with the question of social order (i.e., institutional modifications to the corrosive aspects of self-interests, etc.); in *The Distribution of Wealth* [1893], *Legal Foundations of Capitalism* [1924], *Institutional Economics* [1934], and *Industrial Goodwill* [1919], he dealt with the question of industrial/economic order (i.e., transactions, private property, regulations).

of return as applied to the regulation of utilities; this section concludes with a theoretical interpretation of Commons' regulatory efforts in terms of the "orthodox administration" and "realpolitik" forms of political rhetoric. Finally, section three offers concluding comments.

INSTITUTIONAL ECONOMICS AND ACCOUNTING THEORY

The institutional approach to addressing economic problems was concerned with overcoming the limitations of the neo-classical model and its inability to provide insight as to the crucial social and organizational problems of the time. In particular, institutional economics stressed the dynamic socio-political, institutional factors influencing economic life in the belief that the neo-classical model was almost totally inappropriate to the analysis of social change and the role of institutions in society [Jepperson, 1992, pp. 150-156].[2] In response to the limitations of neo-classical economics, institutional economists sought to understand the mechanisms by which social and economic actions were carried out, but saw political, social and economic behavior as something more than merely the aggregate consequences of individual activities. The institutional school of economics was united by a common conviction that institutional arrangements and social processes matter. It is the analysis of change, particularly analysis of the changing social and organizational forces at the turn-of-the-century, which motivated the institutional approach to the study of economic problems.

On this theme, and specifically related to accounting, Merino [1993, pp. 163-165] credited institutional economists, and such related Progressive era pragmatists as Dewey [e.g., 1910, 1922] and Veblen [e.g., 1904, 1919], for recognizing that the

[2] Basically, in neo-classical economics, price equals exchange value, which results from the interaction between demand and supply. Monopolies are inherently anti-competitive and charge monopoly prices, thus subverting the public good: private vices do not lead to public benefits. In contrast, for Commons, price equals "reasonable value" which results from the interaction between demand and supply as augmented by negotiations. Thus, to correct monopolistic ills, negotiation between monopolies and regulators and/or its judicial system is necessary in order to produce a "reasonable value" [Commons in Dorfman, 1964, pp. 18-35]. Moreover, this distinction is parallel to DR Scott's [1931, pp. 34-61] notion of market control versus accounting control, since the latter is the basis for the courts' decisions.

"pecuniary calculus of accounting" provided economic generalizations which served as systems of rationalization for the ongoing system of economic power embedded in the oligopolistic markets of the time. This recognition stands in stark contrast to that of traditional accounting theorists who, as Merino [1993, pp. 163-165] argued, faced a formidable task: they had to reconcile traditional accounting profit measurement, based on individualistic economic theories, with an emerging corporate economy. Traditional accounting discourse as to profit measurement revealed an unquestioning acceptance of neo-classical economic theory and implicitly supported the premise that competition would ensure survival of the fittest, as faithfully represented by accounting profit. Accounting sought scientific status by claiming to be an objective reporter of economic reality, depicting exchange prices, the basic data of accounting, as factual. Institutional economists, in turn, proposed that such notions as accounting profit were flawed by the implicit embedding of organized interests, and that neo-classical economics had taken for granted the very phenomena that needed to be systematically examined: the role of institutional structure, such as economic or accounting information, in preserving the status quo in power relations, or in the creation and legitimization of alternative social and organization ideologies and processes.

Merino [1993, pp. 175-176] made the provocative point that the key issue is not institutional economists' critique of neo-classical economics, per se, but whether the traditional accounting theorists' neo-classical framework merely represented a failure to recognize the inconsistency between uncritical acceptance of laissez-faire economics and their claim to objectivity, or whether the acceptance of this framework stood for something more insidious — the possibility that neo-classical economists and related accounting theorists consciously devised a discourse that supported the position of stockholders/owners and strengthened the authority of those who controlled financial resources (for example, monopolies), and consciously relied on an assumption they knew was false in order to justify traditional profit measurement.

This question which Merino [1993, pp. 175-176] posed as to neo-classical economics and traditional accounting theory also needs to be asked of institutional economics to fully appreciate its influence as well as the specific work of John Commons. On this point, Hoksbergen [1994, pp. 705-708] reasoned that institutional economics suffers from a failure to recognize its own internal inconsistencies. As stated earlier, institutional economists were united by their common conviction that institutional arrangements and social processes matter, and their related critique of neo-classical economics' adherence to universal objectivity, facts and certainty. Hoksbergen [1994, p. 707], however, argued that despite their criticism of neo-classical economics for staking claim to universal objectivity, there has been a tendency for institutional economists "to see itself as a rival and potentially a superseding competitor to neoclassical economics . . . trying to call on some meta-theoretical extrinsic criterion to prove to itself and others that its economics is superior to others. . . ." This point of view is indeed evident in Richard T. Ely's [1931, p.9] (early University of Wisconsin institutional economist, and colleague and mentor of Commons) reflection on his work:

> I have always recognized that we do not have "natural law" in the economic world, but rather "social law". . . . Nevertheless, I felt that I had discovered an economic law which closely resembled the laws of nature in the regularity with which it operated. I thought that we could predict how some of these economic laws would operate with almost the certainty with which we could predict the operation of the laws of the physical universe.

Thus, as Hoksbergen [1994, pp. 705-708] suggested and consistent with Merino's [1993, pp. 175-176] position, institutional economics may also suffer from problems in its failure to recognize the inherent contradictions in the development of its intellectual base. Similarly, Kolko [1963, pp. 212-216] was quite critical of institutional economists on this point, arguing that Veblen was the only institutional economist who recognized this contradiction and that institutional economics itself served the conservative political capitalism of the Progressive era. Therefore, institutional economics is more than just a voice of dissent against neo-classical economics and related traditional accounting theory. It is instead an important intellectual base which itself needs clarification in an effort to understand its impact on the development of accounting theory and practice.

John R. Commons' Approach to Institutional Economics

John R. Commons' theory of institutional economics attempted to define social behavior in terms of how we create institutional structures and techniques to resolve conflicts of interest, as well as establish regulations concerning governmental-industrial relations [Harter, 1962, p. 212]. A common thread between the work of Commons and other pragmatists of the era such as Dewey and Veblen was that their respective works can be characterized as voices of dissent. Both Commons and Veblen were concerned with the rapid economic changes they and their generation witnessed, and both believed that the tasks of economics included the explanation for, the development of monopolies, and how they might be directed toward serving society. While Commons evolution stressed institutional adaptation to changing conditions, Veblen emphasized the reverse — that institutions actually inhibit adaptation to change. Commons evolutionary view provided him with incentives to be an active reformer within government, while Veblen largely remained an external critic [Horwitz, 1992, pp. 145-167].

The reformist approach can be found in Commons' earlier, predominantly industrial relations work. Because he believed monopoly was inevitable, Commons did not intend to have society suppress it; rather, he intended to protect members of the community from its abuses through regulation. Commons' strategy for social reform consisted of formulating adaptations of economic institutions within capitalistic systems in such a way that the business community would have economic incentives to improve the conditions of the working class. For example, in his book *History of Labor* [1921, pp. 40-64], and as influenced by his contacts with such labor leaders as Samuel Gompers who opposed radical change, Commons generally portrayed unions as organizations which are compatible with the capitalistic system, while unions having revolutionary posture were pictured as deviations from the norm.

One of the critical aspects of both Commons' and Veblen's work pertained to the evolutionary theory of value founded on the habits and customs of social life. Although Veblen had not used court decisions in his work, Commons found them a rich source. Commons maintained that in the development of common law, many customs are tested for survival. In an economic evolution, new forms of behavior develop in response to new needs and opportunities. Many of these new forms give rise to conflicts which must be settled by the courts. Those that are "reasonable" or "good" in the eyes of the law are accepted, while those that are "unreasonable" or "bad" are suppressed. Thus, case by case, common law produces standards for social and economic behavior [Horwitz, 1992, pp. 145-167]. Hence, Commons' study of the development of the country's economic system was to a considerable extent a history of common law, and involves examination of the social construction of norms, laws and regulatory mechanisms, as opposed to the identification of universal intrinsics [Horwitz, 1992, pp. 145-167; Hoksbergen, 1994, pp. 705-708].

Much of Commons' interest in the legal aspects of economics goes back to his teacher at Johns Hopkins University, Richard Ely, and German scholars. His focus was placed on the entire social environment of an economy. One fellow classmate of Commons in the late 1870s, Woodrow Wilson, initially considered Ely "somewhat too radical" in terms of his progressive ideas, ideas which Wilson later espoused in the beginning of his political career at the turn-or-the-century [Wilson, 1956, pp. 88-117]. Not only did Ely send Commons on extensive projects as a caseworker for charitable organizations, but he also convinced him to study problems from an historical perspective using "facts".[3]

Specifically, Ely's views on monopolies are critical and prove particularly influential when Ely moved to and later hired Commons as a faculty member at the University of Wisconsin. As Ely [1931, pp. 3 &6] stated:

> I propose now to state my views, not only in regard to municipal ownership of public utilities, but the ownership of other industries like railways which are, by reason of their inherent qualities, monopolies. For industries of this sort, I used at first the term "natural monopolies". . . . Now, what were we to do with natural monopolies? Public regulation of private monopolies did not look to me at that time very promising. On the other hand, it [regulation] appeared to me to be a source of great evil because there was always danger that those who were to be controlled would, themselves gain control of the agency of control. . . . It seemed to me that if we sharply defined the field of our industries into those that were competitive and those that were monopolies; and left to private ownership and initiative the competitive industries and had public ownership

[3] Ely had studied economics in Germany under the German Historical School, emphasizing that historical, statistical and other studies accumulating facts should be given more attention. Commons adopted both Ely's inductive approach as well as Ely's humanitarian attitudes.

> and operations of the natural monopolies, we would have an ideal situation. That would establish, I thought, a harmony of interests.

Two important aspects of Ely's view and their relationship to Commons' work are worth noting. First, is the acceptance of monopolies as "natural", which, in turn, argues for their control, not dissolution — a view which permeates Commons' later regulatory efforts. Second, Ely advocates public control and public ownership of these natural monopolies — a view which might be considered more liberal than Commons' eventual view which advocated public control and *private* ownership.[4] However, Ely's efforts to import Germany's approach into the U.S. gave way to the reality of American culture, much in the manner advocated by Commons. As Ely [1931, pp. 15, 16, 20] stated:

> Now when it comes to public ownership of natural monopolies things have not turned out as I anticipated they would. . . . Government becomes more and more significant on its economic side, but there is not a corresponding general interest in public administration, and a correspondonly increase in comprehension of its significance. The great mass of the people are interested in games, base-ball especially and foot-ball. . . . It is obvious that the American people are determined, first of all, to try out the commission control of private industry, rather than public ownership.

Ely's views were also influenced by socialist efforts in England at the time. Extensive, twenty-seven years of correspondence between Sidney Webb reflect this influence. Much of Ely's correspondence with Webb revolved around Ely's book *Political*

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[4]Clearly Ely's [1931, p. 15] views were very much influenced by his German background as he stated:

> I thought that human nature, such as it is found in our country and in modern civilization, would respond to public ownership of natural monopolies with all its implications. I thought that we would remove the source of corruption, and certainly at the time I was writing, these sources of corruption were very largely connected with private ownership of natural monopolies. I thought that if we could have public ownership and operation of natural monopolies, we would have pure government; we would have excellent operation of these natural monopolies through a highly trained and capable civil service in the nation, state, and city . . . I had it in mind that we would approximate the excellence of the civil service in Germany where . . . they enjoy security of tenure and where special excellence is honored by generous recognition of those in control of government.

Economy [1889]. Webb gave Ely much feedback on the chapter on Socialism, and Webb was also instrumental in finding a publisher in England [*Correspondence archived at the Wisconsin Historical Society*, 12/21/1888; 2/1/1889; 3/3/1889; 3/19/1889; 3/31/1891; 1/22/1892; 9/19/1892; 2/21/1894]. As Webb [12/21/88] wrote to Ely on a planned trip to Baltimore with Edward Pease of the socialist Fabian Society:

> [The Fabian Society] would be glad to permit some conversation with you, especially as to the progress and prospect of the Socialist idea in America, and as we are both in the center of the English Socialist movement we could perhaps give you some details of interest.

This relationship between Webb and Ely, revolving around a sharing of socialist ideas, and later with a more conservative Commons, contributed to the basis of the "Wisconsin Idea" which advocated the expansion of the State's functions to safeguard the well-being of its citizens and the conscription of experts to identify the needs of the people, and then devise and administer reform policies to serve these needs.[5]

The Social Gospel and Progressivism

Early expressions of Progressive thought were based upon and yet extended beyond conceptualizations of morality within organized religions. Like many Progressives, John Commons and Richard Ely were part of the Social Gospel movement which rejected the orthodox Christian position that man is innately sinful. It maintained that human nature is essentially good, but is undermined by a corrupt society. The social gospelers generally sought to restore, if not reverse what they thought were the unnecessary consequences of industrialization, urbanization and the expansion of technology. Their avowed goal was to "christianize business, industry, politics, and the city's immigrant populations, all of which [were] regarded as the major, unregenerated spheres of society" of which "business was declared to be the most significant unregenerate institution within

[5]Concerning Progressivism's reliance on experts, we do not mean to imply that only to Progressives or the U.S in general relied on expertise. For example, slightly predating John R. Commons' work, Sidney and Beatrice Webb [1902a, 1902b], who entertained Commons during his National Civic Federation work [Commons, 1934, p. 114], were espousing a theory wherein experts drawing upon an impartial, scientifically derived knowledge-base, could assist labor in elevating its stature and financial well being.

the American social order" [Mills, 1943, pp. 168-173; Greek, 1992, pp. 56-58]. The gospelers believed that man [*sic*] "by using his intellect can remake society, that he can become the creator of a world organized for man's advantage" [Woodrow Wilson, in Waldo 1948, p. 16], and that conscious social action would eradicate sin and hasten the coming of God's kingdom, and, consequently, would promote social reforms to "purify American society" [Woodrow Wilson, in Waldo, 1948, p. 58].

It is with this emphasis of the social that the moral dimension of the Progressive interventionist strategy of changing the processes of government was founded [Hamilton and Sutton, 1989]. After having established the preeminence of social salvation, the next step in legitimating the interventionist strategy was to displace the importance of natural law, God or the ethical, responsible behavior of the individual, in favor of an experiential grounding in such social groups as organizations. In turn, social reforms comprising the interventionist strategies could express societal values and goals in a way amenable to their accomplishment by bureaucracies. But here, the operationalization or encoding of societal goals and values within the formal structure of organizations could be accomplished only by such experts as public administration scientists and sociologists "who took up the idea of organization as a banner" during this era [Hamilton and Sutton, 1989, p. 13]. In turn, the act of organization was seen by Progressives as an ethical act and hence organization became a goal in-of-itself [Hamilton and Sutton, 1989, p.15].

Indeed, the melding of the religious and the political by the Progressives led Hofstatder [1955, p. 320] to remark that "the key words of Progressivism were terms like patriotism, citizen, democracy, law, character, conscience, soul, morals, service, duty, shame, disgrace, sin, and selfishness." The resulting ethos, in turn, directed such Progressives as Commons to channel their energies towards the common goal of forming an ideal democracy populated by an informed and sovereign citizenry, and guided by conscious and redemptive human action, wherein business and politics were harnessed in the service of society and the individual [Kolko, 1963, pp. 34-61].

Summary

Merino [1993, pp. 163-165] credits institutional economists for recognizing the limitations of neo-classical economics and related traditional accounting theory. She also asked the question of whether traditional accountants were oblivious to the inherent contradiction in their claim to objectivity and uncritical acceptance of neo-classical economics, or whether this contradiction represented an effort to preserve the status quo in power relations among competing interests. Hoksbergen [1994, pp. 705-708], in turn, recognized that a major part of the development of institutional economics was accomplished by a faction that claimed superiority over neo-classical economics by searching for universal laws able to gauged by external criteria or "facts". This faction is most apparent in the "Wisconsin School", the reformist Progressive party, and the Social Gospel movement — with which John Commons was also significantly involved. Hoksbergen [1994, pp. 705-708] also identified an inherent contradiction in the reformist effort of institutional economics and the intellectual underpinnings of institutional economists. This apparent inherent contradiction in the efforts and work of John Commons begs Merino's query as to the power and politics of the development of a significant knowledge base be re-visited. As Kolko [1963, pp. 15, 214, 215, 3] argued:

> Richard T. Ely, for example, maintained that large-scale business was inevitable, but that, save for certain types of services, monopolies in the pure sense were not preordained; the burden of his writing was concerned with the desirability of government regulation of "artificial" monopolies that had sprung up rather than with regulation as a means for restoring purely competitive conditions . . . [t]he idealization of the state was also the result of the peculiar training of many of the American academics of this period. At the end of the 19th century the primary influence in American social and economic theory was exerted by German universities. The Bismarckian idealization of the state, with its centralized welfare functions designed to preserve capitalism and the status quo in its more fundamental aspects, was suitably revised by the thousands of key academics who studied in German universities in the 1880s and 1890s. . . . Conservative in their ends, as were big business advocates, the academics who proposed economic reforms failed to understand the process of political capitalism. Instead, the pressures and leverage created by their ideas helped make political capitalism possible. . . . It is business control over politics rather than political regulation of the economy that is the significant phenomenon of the Progressive era. Political capitalism

is the utilization of political outlets to attain conditions of stability, predictability, and security — to attain rationalization — in the economy.

A key question is whether Commons also fell prey to the positive quest for universal laws of economics reliant on "pure facts", or whether his involvement with regulatory reform was more reflexive in nature.

PHYSICAL VALUATION AND RATE OF RETURN REGULATION

Relying upon the landmark *Munn v. Illinois* [1877] case in which the U.S. Supreme Court upheld Illinois' right to regulate the "exploitive" prices charged to customers by a private sector company, Governor Robert La Follette attempted to regulate two major Wisconsin industries — railroads and utilities.[6] Concerning the former, La Follette introduced an eventually successful Railroad Regulation Bill in 1905 that established the Railroad Commission. This commission based its efforts on the earlier work of Henry Carter Adams [for example, 1887, 1903, 1918], the first statistician of the U.S. Interstate Commerce Commission who devised an accounting system that detailed railroad revenue, expenses and earnings which served as a basis for much subsequent federal regulation [Churchman, 1976, pp.

[6]Another lawsuit of this era having a less effect on Wisconsin's regulatory efforts though it is relevant to contextualizing Commons' work is Smyth vs. Ames [1898]. This case related to a de-physicalized notion of property wherein government regulations were adjudicated as to the "reasonableness" of railroad rates using "fair' value measures, increasingly market values. The focus of the court was to balance granting government enough power to regulate while guarding against implicit confiscation of property. Smyth vs. Ames specifically established a set of multiple factors for ascertaining reasonableness values, although these factors proved unwieldy in their application [Horwitz, 1992, p. 160]. Alternatively, Siegel [1987, pp. 243-247] interpreted this case as serving as the foundation for adopting "reproduction cost" (or market value) applied in the 1920's, a concept Commons [1924, pp. 64-82] later criticized as circular in that assets associated with higher rates of return will have higher reproduction costs, or market value, which will in turn justify higher rates. Another related case following Wisconsin's 1907 law was the Mann — Elkins Act of 1910 which empowered the Interstate Commerce Commission to effectively regulate railroads. In part, the act placed the burden of persuasion on carriers to establish the "reasonableness" of the amount sought for rates; however, the I.C.C. had difficulty in imposing this act on industries other than railroads [Smith, 1958, pp. 239-242, 363].

42-65]. Milo Maltbie [1901, pp. 39-51] eventually transformed this system into the pioneering uniform system of accounts, which served as a tool for the general social control of private enterprise [Trebing, 1984, pp. 232-239; Ulen, 1980, pp. 306-308]. In Wisconsin, La Follette's Railroad Commission sought to regulate rail pricing by devising an "accounting rate of return" mechanism for gauging what would be a "fair" return on invested capital for railroads.

In turn, this basic approach was specifically emulated and mobilized by Commons, who La Follette chose to draft what would become the Wisconsin Public Utility Law of 1907 [Commons, 1934, p. 126].[7] As eventually administered by the Railroad Commission, the Public Utility Law employed an "objective rate of return model" (which subsequently became known as the "cost plus pricing regime") for regulating rates charged to customers of Wisconsin's electric utilities. Because of Commons', La Follette's, and Wisconsin's visibility and success in the Progressive reform efforts, components of the 1907 Law vis-a-vis accounting rate of return regulation gained rapid acceptance in at least 29 states and the federal government by 1913, and indeed impacted utility regulation for most of the twentieth century [Trebing, 1984, pp. 232.239].

It is perhaps important to note that Commons and Adams saw such monopolies as utilities and railroads as "natural" in the sense that they embodied the economic "law" of increasing returns from economies to scale. In this view, monopolies could not be abolished because this would ultimately harm the public. Instead, they must be regulated. Thus, Commons and Adams saw as necessary a dismantling of the liberal ideal of a strict partitioning of civil society from the state in the sense that the state had to regulate the private sector. According to Adams [1887, p. 64], "For all industries which conform to the principle of increasing returns, the only question at issue is whether society shall support an irresponsible, extra-legal monopoly, or a

[7] Commons had earlier been part of the National Civic Federation which had investigate the operations of public utilities in the United States with reference to prior efforts in England. Commons' part in the investigation centered on examining labor issues, but he had visited so many utility companies that he had acquired both the interest and knowledge in the public utility field. Commons came to think of his reform efforts as institutional adjustments that could make the economic system of utilities more workable [Commons, 1934, pp. 112-130].

monopoly established by law and managed in the interest of the public."[8] In order to effectively regulate such natural monopolies, it was necessary to render the private public, i.e., visible to public sector regulators if not the public. It is in this capacity of rendering the private public that accounting was to be invoked.

The Regulation of Utilities

The notion of "reasonable value" was the critical element in the *Wisconsin Public Utility Law of 1907*. Here, an accounting rate of return on a company's assets (or rate base) is based upon the concept of "physical valuation" which Commons [1907b, pp. 221-222; 1910, pp. 215-217; 1913, pp. 291-292] saw as essential in drafting the Wisconsin law. The concept of physical valuation serves as the foundation for setting prices, which are intended by regulators to allow utilities to earn their cost of capital on the depreciated, original cost of their assets, as well as recover their operating costs [Mereba, 1994, pp. 52-65]. In Commons' opinion, the best method would be to tie the rates to a *"reasonable return"* on the value of invested capital. As such, "the accounting system is the central endogenous variable available to regulators in the context of rate of regulation. [I]t is through accounting procedures that wealth is distributed [among] groups and electricity rates are set" [Jarrell, 1979, p. 105]. Accordingly, accounting could no longer disclaim responsibility for the concept of valuation by claiming to be merely representing "natural" facts relating to "natural" monopolies. Indeed, Commons' definition of "fair rate of return" remains a basis for industry regulation and a focus for academic research in economics and accounting

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[8] As suggested earlier, this view and perpetuation of monopolies as "natural" economic entities has a legacy in the work of Commons' mentor — Richard Ely. In turn, Ely was also a colleague of economist Henry C. Adams as the two of them were co-founders of the American Economic Association in their efforts to find an outlet to accommodate their intellectual perspective [Kolko, 1963, p. 15]. Furthermore, this view as to the natural status of monopolies predates the work of Ely, Commons and Henry C. Adams in the work of Charles Francis Adams, Jr. As Kolko [1963, p. 14] points out, at least a decade before the work of those institutional economists:

> Charles Francis Adams, Jr., president of the Union Pacific railroad from 1884-1890 [and founder of the Massachusetts Railroad Commission which influenced the formation of the I.C.C.], was announcing that "the principle of consolidation . . . is a necessity — a natural law of growth. You may not like it; you will have to reconcile yourselves to it." "The law is invariable. It knows no exceptions."

[illustrative of recent works include, Sappington, 1980, pp. 363-370; Baron and Myerson, 1982, pp. 911-915; Abdel-khalik, 1988, pp. 44-62; Lanen and Larcker, 1992, pp. 208-228].

As previously noted, Harter [1962] suggested that in order to learn the meaning of the concept of "reasonable value" Commons turned to the study of common law, which institutional economists maintained was the means by which many societal habits and customs become encoded in a governance structure. Commons attributed his notion of reasonable value to state Senator A. W. Sanborn from whom Commons obtained the idea that legal valuations were oriented toward the future [Horwitz, 1992, pp. 145-167]. As Commons [1934, p. 123] stated, "From this starting point, I worked for many years in making futurity the main principle of [institutional] economics, distinguished from all other schools of economic thought." In an evolving economic-political system, new forms of social behavior emerge in response to new needs or opportunities, and these new forms give rise to conflicts which must be resolved by the courts. Those forms that are "reasonable" or good in the eyes of the court are accepted, while those that are "unreasonable" or bad are suppressed. As Commons [1924, p.vii] explained,

> From the Court decisions it seemed that anything "reasonable" would be sustained, and so we had to use the words "reasonable value" . . . whether we knew what it meant or not.

Reasonable value, in turn, represents both an upper and lower limit of value as implicitly established by the American judiciary [Commons in Dorfman, 1964, pp. 18-25]. It is identifiable not as reflecting or seeking to reflect some notion of objective worth, but merely as "good" or "viable" in the eyes of competing parties in a court of law. Thus, case by case, common law produces standards for gauging economic behavior [Harter, 1962, p. 219]. According to Commons [1934, p. 156, 160; emphasis added]:

> Reasonable values and reasonable practices were entirely new words introduced into the theories of political economy. Often my students, and sometimes my economist critics, said that "reasonable" was purely subjective, and that there were as many meanings of reasonableness as there were individuals. Such a term placed the determination of reasonableness in the arbitrary mind of whatever individual happened to be in

> authority. But I considered this objection to be an inheritance from the subjective individualism of preceding economic theorists. A collectivist theory of value derived from existing best practices, from custom, the common law, and the decisions of courts, could make reasonableness "objective" and therefore capable of investigation and testimony, leading to the formation of working rules for collective action in control of individual action. . . . *So I contended that, in economic conflicts, reasonable values and reasonable practices were not the subjective opinions of anybody, but were the collective opinion, expressed in action, of those whose economic interests were conflicting, but who investigated together, and knew by experience, all of the facts.*

Thus for Commons, objectivity was defined by the degree of social-legal consensus concerning "reasonable value." Objectivity — social objectivity — and the process of developing a reasonable value were intertwined. In contrast, as argued by Merino [1993, pp. 178-180], traditional accounting theorists' notion of objectivity was markedly distanced from the notion of reasonable value in that they disclaimed any responsibility for value, and instead emphasized objective and documentable "natural" exchanges that largely involved transactions. Commons [1907b, p. 222] stated

> A significant feature of the Wisconsin legislation is . . . its reliance on the physical valuation as the first step in regulation (physical valuation means nothing more or less than the cost of construction or reconstruction of the physical property). Accompanied by a complete system of uniform accounting with special precautions as to depreciation and construction accounts, every person in the State may know at the end of each fiscal year exactly the rate of profit which each company or municipality has made on the actual property invested. With the Wisconsin idea of physical valuation as the starting point, every citizen can determine for himself just as well as the Commission whether the rates and fares charged by the corporations are yielding an excessive profit.

In the *U.S. Senate Hearings on the Physical Valuation of Property of Common Carriers* [1913, pp. 90-91], whose purpose was to develop effective "natural" regulatory policy, Commons further defined his physical valuation approach as "an accounting proposition" which recognizes both the cost of the property and a fair rate of return. Commons [*U.S. Senate Hearings on the Physical Valuation of Property of Common Carriers,* 1913, pp. 90-91] acknowledged that while

> . . . corporations have devoted their property for the public use, and therefore during their history they were entitled to a fair rate of return . . . these valuations are very liberal, [but] they were all based consistently on the principle of cost rather than value, and therefore they represent the amount of sacrifice which investors have incurred for the service of the public.[9]

During related Senate Hearings, a Senator Cummins challenged Commons on the point that Commons' physical valuation approach actually permitted an excess of capitalization of railway property, thus allowing owners an excessive return on investment at the expense of customers. Following up on this theme, Senator Lippitt [*U.S. Senate Hearings on the Physical Valuation of Property of Common Carriers,* 1913, p. 108; emphasis added] criticized the physical valuation and rate-of-return approach by telling Commons that:

> You are making the National Government in that case a private nurse to the investing public, and when they (corporations) have been wise and enterprising and efficient you are taking away their reward, but when they have been unwise and inefficient and negligent in business, you are making it up to them, *which may be good polity for the future, but it is not the case that prevailed in the past.*

Commons [1934, p. 125] later agreed, stating, "I am told by railway people that they feel confident that they will come out better than the public in this valuation problem."

Wisconsin legislator Edward Bennett [1931, p. 1] was also critical of the *Wisconsin Public Utility Law of 1907* and the discretionary nature of accounting within it because he felt that the bill "empowers the Commission to fix just and reasonable charges for services, [yet] leaves the citizen to search the law in vain for any statement of the policies and principles which are to be followed by the Commission in the determination of the reasonableness of the charges." Citing Section 196 of *Wisconsin*

[9]This view is consistent with Ely's [1931, pp. 3-12] emphasis on the excellence of the civil service in Germany where the government provides generous recognition of those who contribute to social and economic functioning.

Public Utility Law of 1907 as the one area where "the substance of everything which the law has to say about the principles of rate-making and valuation," Bennett [1931, p. 1] gave examples of the law:

> Paragraph 196.03. *Utility charges to be reasonable and just*. Every public utility is required to furnish reasonably adequate service and facilities. The charge made by any public utility . . . shall be reasonable and just, and every unjust or unreasonable charge for such service is prohibited and declared unlawful.
>
> Paragraph 196.05. *Utility property valuation*. The Commission shall value all the property of every public utility actually used and useful for the convenience of the public.

As Bennett [1931, pp. 2-3] argued, "The legislature empowers the Commission to fix just and reasonable rates but is silent, utterly silent as to the principles or the policies which are to be controlling in the determination of reasonableness". Commons [1907b, p. 223] agreed, stating

> Herein the law is elastic enough to offer the opportunity for ingenuity and experiments that may combine the principle of State regulation with that of private initiative, thus circumventing the probable damaging effect of government regulation or enterprise and initiative and on the investment of capital for extensions and improvements.[10]

[10] This same critique of manipulability/subjectivity of accounting is evident in McGraw's [1984, p 31]criticism of earlier efforts by Charles Francis Adams to incorporate a "reasonable return" for the regulation of railroads in Massachusetts in the late nineteenth century:

> The Massachusetts approach (to rate regulation) rested on three premises, each of which could as well apply to twentieth-century utilities as to nineteenth-century railroads. First, any determination of the "reasonableness" or "fairness" of rates must inescapably remain a subjective undertaking. Scientific precision in rate-setting is therefore a practical impossibility. Second, the pricing function is part of corporate management, a function jealously guarded by all business executives, and with good reason. Third, the rate question directly reflects the debate over competition versus monopoly. In the case of nineteenth-century railroads, rates were the means through which an impersonal market signaled its ability or inability to cope with two conflicting forces: with the economic requirements of railroading in particular, and "natural monopoly" in general; and with the non-economic requirements imposed by society.

Thus, despite the appearance of being concrete, the abstract notion of rate of return as represented in the *Wisconsin Public Utility Law of 1907* remained manipulatable by big business. Commons [1934, pp. 125-126] later attributed this result to the underlying nature of the political process employed in piecing together the legislation:

> In the negotiations leading up to the Public Utility Law of 1907, the joint legislative committee did not rely so much upon public hearings required by "due process of Law," where everybody has a lawful right to be heard and the conflicting opinions are [reconciled], as upon private and even confidential conferences with the leaders of the interests to be brought under the law, where concessions could be made and the investigations of experts could be weighed and balanced. . . . It was the general class of negotiations which I afterwards defined as "rationing transactions" distinguished from managerial and bargaining transactions. I could tell [before the enactment of the law] just how the Railroad Commission would administer and interpret the law. This foreknowledge enabled us to greatly condense the bill, leaving a huge field of investigation and discretion to the Commission, instead of inserting into the law a multitude of minute details, so familiar and so often conflicting in American legislation.

Despite the apparent motive to accommodate business interests, one can argue that Commons' motive was more to strike a balance the powers of government and business. On this point, departing from such other pragmatists of the period as Ely's veneration of Germany, Commons [Democracy: The Best Basis for Reconstruction, *Milwaukee Journal,* July 28, 1918] observed that:

> We have learned in all democratic countries of the world one important lesson from the way which Germany's power has been built up and used. The democratic nations have learned to dread Socialism. Prussia is the modern exhibition of state Socialism. And government ownership of railways in Germany is probably the main instrument by which the power of autocracy has been built up in that country. Other nations dread government railroads when controlled by autocracy and military power, for it means that the railroad system can be used to dominate the business people, and to bring submission on the part of labor.

Commons thus saw the role of effective rate setting to be as much about preventing state governments from reducing the rates of utility companies to the point where the state actually runs the utility or defacto confiscates its property, as it is about protecting society from exploitive monopolies [Horwitz, 1992, pp. 145-167].

The Legacy of Reasonable Value: Constraint or Flexibility?

While a precise rate percentage could in fact be set by the State under the rate of return approach, the income and asset base to which it applies could still be manipulated by utilities. For example, in their seminal economics work in the area, Averch and Johnson [1962, pp. 1052-1055] developed a model which suggests that because of the asset base used for determining prices, rate of return regulation actually encourages utilities to bias their input mix toward capital, i.e., by artificially increasing the asset base, more money could be made at the established rate, with the increased cost passed on to consumers. Because of rate of return regulation, utility resources would be inefficiently allocated, thereby decreasing consumer welfare. Utility managers would also not be motivated to reduce expenses, thereby once more decreasing consumer welfare. Employing the agency theory perspective, this reasoning was supported by Abdel-khalik, [1988, pp. 144-145] for example, who observed fully four score years after Commons' work that:

> Incentive problems arise in the electric utilities industry as a consequence of the institutional and legal arrangements of the cost-plus pricing regime under which natural and statutory monopolies operate. In the United States, such monopolies operate under a cost recovery system that gives the firm a mechanism by which it can shift all or part of the cost of "moral hazard" risk to consumers, who then become the residual claimants. In this setting, expense accruals have a more direct link to the firm's cash flows than is the case in unregulated industries. In particular, pricing a monopolist's output at cost-plus means that accruing expenses generates sales revenues for utilities. Consequently, agency cost can be included in the allowable cost passed on to consumers. The result is that the residual loss is shared between the consumers and shareholders with two competing consequences: (1) it would be in the best interest of shareholders to provide managers with incentives to shift all costs to the consumers; and, by the

same token, (2) it would be in the consumers' interest to persuade regulators to challenge the cost assumptions underlying the firms' requests for revenue requirements [see also Sappington, 1980, pp. 363-370; and Baron and Myerson, 1982, pp. 911-915; who modified the general agency theory model to better reflect regulated contexts].

Seeking to understand whether managers serve shareholders or consumers, as influenced in their compensation systems, Abdel-khalik conducted an empirical examination of the U.S. utility industry. Consistent with Averch and Johnson's [1962, pp. 1059-1065] theorizing, he found that after controlling for the effects of size, the "padding" of operating costs and over capitalization are, indeed, associated with higher manager compensation. Thus, utility managers are actually rewarded for passing on cost inefficiencies to consumers. But, would the paradox have been a revelation to Commons?

According to McGraw [1984, pp. 59-60], it was generally recognized in the Progressive era that there arose interpretive problems and internal instabilities in actually applying the concept of reasonable rate. A cost-plus formula relies on assets (before or after depreciation), on operating costs (included or not included), and asset valuation procedures (market, book, etc.). All of these possibilities lead to various incentive problems, as McGraw [1984, p. 60] concludes:

> In practice, these problems promoted the rise of ingenious accounting methods by corporations, all calculated to maximize revenues in the face of regulatory limits of percentage rates of return. At worst, they made the process of rate regulation a ritualistic charade, played out in the form of full-scale "rate-cases" as part of the routine operations of commissions. Such cases conducted under elaborate procedural laws, often turned into extremely laborious hearings dominated by lawyers and engineers, incomprehensible to the ordinary citizen.

Maxwell concurred with McGraw's [1956, p. 202] observation, stating:

> In spite of the Progressives' campaigns against monopoly, the administration unwittingly fostered monopoly in the process of regulating many public service corporations. Because the Railroad Commission lacked a yardstick for measuring unit costs, it tended to guar-

> antee a fair return and profit regardless of the efficiency or inefficiency of the operations of a power plant, water works, or street railway. The physical evaluation of properties was only a partial check against inefficiency and the trend was toward higher rates to compensate for rising costs.

In contrast with other pragmatists of his era, Commons, overtly recognized the political nature of government administration that socially constituted such regulations as the *Wisconsin Public Utility Law of 1907*. Unlike others of his era who thought that the, "act of organization was intrinsically an ethical act vital to human nature and to society," [Hamilton and Sutton, 1989, p. 15], Commons [1965, p. 109, emphasis added] had no illusion of the purity of the Wisconsin's bureaucratic structure nor of the neutrality of forms of accounting it deployed:

> Social organization is *psychic*, and consists of those *coercive sanctions* which subordinate individuals to a single will, notwithstanding their inclinations to satisfy their desires at cross purposes in their own private ways. Organization is not originally the free persuasive grouping of men for mutual satisfaction, but is an alternative forced upon them by increasing population and increasing struggle for existence. Upon the utilitarian explanation, organization would be immoral, for it tends to suppress the individual to the passions of a few. As it is, *organization is neither moral nor immoral — simply necessary*.

Thus, Commons saw monopolies as not "natural," but "artificial" in character, and their regulation by state governance structures that employed accounting as necessary, however flawed. Yet, the use of accounting did ostensibly exhibit the values of rationality, neutrality, objectivity, economy and control, but these values were inherently interpenetrated with conflict between opposing interest groups seeking to control the bureaucratic structure of government. Specifically, Commons saw even accounting concepts he himself advocated as inherently flawed. For example, he saw market value and reproduction cost as circular as applied by the courts in trying to ascertain what was "reasonable." According to Horwitz [1992, p.162]:

> [Commons'] penetrating — though often obscure — *Legal Foundations of Capitalism* [1924] traced the late nineteenth century judicial shift to a market value standard. The Rate Cases, in particular, allowed Commons

to appreciate that it was the guarantee of a future income stream that determined present value of property. 'All value is expectancy' Commons proclaimed. In rate making cases, market value is the present value of expected rates. If the rates are unreasonable, so is the market value. Judges who believed that reasonable rates could be deduced from fair market value were "reasoning in a circle," Commons declared.

Theoretical Interpretation

March and Olsen [1983, pp. 265-295] offered a framework useful in understanding this apparent paradox of power and politics embedded within institutional economics, such as evidenced in the regulatory reform efforts undertaken by Commons under La Follette's direction. They reasoned that such reform efforts were symbolic events which represented a history and embodiment of two forms of political rhetoric. The first, or "orthodox administration" form, represents the official language of laws and regulations which promote reorganization, and speaks in terms of managerial leadership, administrative structures and procedures for facilitating efficiency and effectiveness within bureaucratic structures. It invokes the overall guidelines and values of rationality, neutrality, objectivity, economy and control.

But here, a paradox of bureaucratic action arises: If the impersonal, bureaucratic machinery of rationality is allowed to proceed unchecked, this very rationality would become unresponsive to shifting human values and hence potentially abusive in the exercise of bureaucratic power. Thus, the second form of rhetoric, "realpolitik," arises, which holds that bureaucratic structures and claims to neutrality, objectivity and rationality represent dangerous illusions and threats to the governed unless they are linked somehow with the values, beliefs and goals of the populace and its various constituent groups. Thus, realpolitik recognizes the value of conflict between opposing interest groups which seek expression though and control of the bureaucratic structure of government. Politics becomes stylized or encoded within the litany of bureaucratic structure, as in Commons' case — in the form of accounting rhetoric. More specifically, March and Olsen [1983, p. 283] observed that

> The rhetoric of realpolitik is an empirical and prescriptive counterpoint to an orthodox administrative perspective. To the emphasis on managerial control, it jux-

> taposes an emphasis on political control. It argues that a single individual has neither the cognitive capacity, nor the time and energy, nor the moral and representational standing assumed by the [orthodox administration] perspective.

March and Olsen went on to observe that most political actors, and in the case of Commons, academic/administrative actors, recognize and even can recite either form of rhetoric when necessary, and taken together, these two forms establish a fairly exhaustive frame of reference for understanding bureaucratic structure and action in American government. March and Olsen [1983, pp. 291-92] concluded that while they are fairly exhaustive, the two forms of rhetoric are not mutually exclusive, but rather are interpenetrated:

> Such a perspective may provide an interpretation of the cultural ritual of reorganization and of the rhetorical duality of that ritual. The rhetoric of administration and the rhetoric of realpolitik are mutually supporting and are embedded in a culture in which each is important. The ritual of reorganization is a reminder of both sets of beliefs and testimony to their efficacy. On the one hand, a commitment to administrative purity is made tolerable by an appreciation of realpolitik, much as a commitment to personal purity is made tolerable by an appreciation of human weakness. At the same time, a commitment to realpolitik rhetoric is made consistent with human hopes by a faith in the imaginability of improvement through human intelligence. It should not be surprising to find that both rhetorics survive and thrive, and that both find expression in the symbols of reorganization. The orthodoxy of administration is the voice of the prologue to comprehensive administrative reform; the orthodoxy of realpolitik is the voice of the epilogue; the myths of the first shade into the myths of the second over the course of a major effort at reorganization; and both sets of myths are needed for a normatively proper interpretation of the reorganization saga. . . . [These] rhetorics exhibit and reaffirm fundamental social values, particularly those associated with personal efficacy, with intention, interest, power and rational choice.

March and Olsen [1983, p. 291] urged that the two rhetorics not be interpreted as deceits for subverting public attention and diverting public resources, but rather as symbols of the possibility, the hope for effective government reform.

It appears that among the pragmatists at least Commons was well aware of the covertly political attributes of specific, accounting-based techniques he himself advocated. Consistent with other institutional economists [e.g., Dewey, 1910, 1922; Veblen, 1904, 1919], Commons did criticize the "pecuniary calculus of accounting" [see Merino, 1993, pp. 164-165]. But in addition, Commons also redirected accounting and deployed it in support of government intervention vis-a-vis regulation. Here, accounting performed two roles. First accounting was deployed in the hope of making the private public by rendering the inner workings of such monopolies as utilities transparent to regulators. And second, accounting rendered conflicts of interest as discursive affairs as compared to physical conflict in the form of boycotts, picket lines and armed Pinkerton agents typical of the era. This use of accounting aided in bringing confrontations from street and rail-level violence to the negotiating table [McGraw, 1984, pp. 77-93]. More specifically, exhibiting marked reflexivity, Commons [1965, pp. 99-100; emphasis added] asserted that:

> The State is primarily coercive, but where technical work has been absorbed by it, just as its officials must be equipped in knowledge and skill, they must also learn tact. Penology, pedagogy, "scientific" charity, are highly successful only *when the iron hand of coercion is gloved by the arts of persuasion*. The state extracts coercion from private hands in order that the latter may be compelled to rely on persuasion, and the criterion for the success of state coercion itself is the extent to which the officials have learned to make it unnecessary. The state is, indeed, becoming more persuasive and less coercive in proportion as the officials recognize their position as public servants, and the people become upright and patriotic in character.

Thus, accounting is not only an instrument for representing an economic reality as proposed by proprietary theorists, but also a rhetorical device for setting forth the concept of reasonable value which makes rage, coercion, physical force, unreasonable.

CONCLUDING COMMENTS

The analysis provided in this paper suggests that the contributions of John R. Commons in the development of accounting in the governance structure of the state and the regulation of monopolies is underrepresented within extant academic accounting literature. More specifically, Commons' work in Wisconsin, which spread to other states and the federal government, appears to be important to understanding and making possible state governance, and this governance in turn, makes accounting and accountants possible. Harter [1962, pp. 210-212] concluded that while Commons is comparatively obscure in American history, his leadership in the drafting and adoption of social legislation entitles him to more attention than he has so far received. Harter [1962, p. 128] further states that "No single man was responsible in bringing it (social legislation) about, but if anyone could be called its father, he would be John R. Commons." Similarly, Horwitz [1992, p. 162] observes that "The first thinker to see the relationship between the de-physicalization of property and its abstraction into market value [key concepts within accounting theory] was the great Wisconsin institutional economist John R. Commons." Commons' legacy is still very apparent as seen in recent efforts to deregulate the utilities industry:

> "We're cutting through 100 years of sedimentary layers in trying to make the market for power work better," said Gary J. Lavine, senior vice president at the Niagara Mohawk Power Corporation in Syracuse. . . . The central quandry is that much of the existing investment in electrical power . . . is more expensive than the cost of starting over with a clean sheet of paper. As a result, utilities contend, the only way to provide big electricity savings quickly would be to deny investors a fair return on hundreds of billions of dollars of financial commitments that with hindsight should never have been made. That, they say, would be unconscionable. . . . "Regulators made promises to investors, and government has a moral obligation to honor them," said Alfred E. Kahn, an economist at Cornell University [*New York Times*, 2/3/95, p. C1].

The work of John Commons has an interrelated theme with that of DR Scott [1931, p. 133], who suggested that the development of accounting ". . . must be provided for within the process of cultural change . . ." thereby emphasizing the importance of such issues as: the social creation of accounting; how alternative sets of meaning are attributed to accounting; and the presence and influence of competing interest groups within organizations and society who differentially deploy accounting to serve their own vested interests. Scott [1931, p. 264], for example, called attention to accounting being complicit in the creation of organizational managers' reality, both in terms of determining the goals of management as well as the means to achieving those goals; he stated "Accounting and statistical methods are serving as vehicles of the current cultural reorganization because of their limitation of expression to objective terms" [see also Ijiri, 1967, pp. 158-159].

Similarly, as March [1987, pp. 38-40; emphasis added] observed in a plenary speech before the American Accounting Association:

> These components of decisions and decision processes are not unfortunate manifestations of an irrational culture. They are important aspects of *the way organizations develop the common culture and vision* that become primary mechanisms for effective action, control and innovation. As a result, information strategies are as much strategies for managing, interpreting and creating visions as they are strategies for clarifying decisions. And if this sometimes seems perverse, it may be well to remind ourselves that human life is, in many ways, less a collection of choices than a mosaic of interpretations. *It involves both discovering reality and constructing it.*

Thus, there appears to be a core appreciation among the loosely defined group of institutional economists that political rationalization vis-a-vis economic rationalization became *the* means of attaining both order in the economic sphere and security in the political arena [Scott, 1931, pp. 34-61]. On this point, Hopwood [1990a, pp. 83-88; 1990b, pp. 10-16] has argued that accounting is centrally implicated in the institutional frameworks, language and patterns of power and influence that characterize contemporary organizations. It follows that accounting practices evolved in a manner which involves more than merely formulating and legitimizing economic actions, but also in preserving the status quo vis-a-vis power of specific business and political actors. The power of accounting derives from its ability to move beyond merely facilitating the operation of pre-given and relatively unproblematic forms of economic management, such that accounting categories take on a visible, rule-like status in social thought and action, thus transcending even social and political considerations. Consequently, research interest in accounting should not be conceived as purely a technical one of improving its ability to passively represent an objective economic reality, but also stands for much broader issues by which patterns of power and influence are developed and maintained as they concern the nexus linking the organization with society. As Scott argued, such rationalized administrative policies and practices as accounting did not emerge as a *consequence* of widespread concern for operational efficiency, but as an *artifact* of the power nexus linking economic and political spheres of influence.

Commons' use of accounting as an orthodox administration form of rhetoric, and his role in developing it as influenced by the rhetoric of realpolitik [March and Olsen, 1983, pp. 285-295], was essentially reflexive in nature. That is, as an external critic of monopolies, he challenged such general concepts as accounting profits as aligned with socially dysfunctional behavior. He was also cognizant of the flaws in specific techniques he himself developed as being subject to influence by vested business interests, that his rate of return remained "elastic" and "manipulable" by the very monopolies to which it was applied. However, he saw such calculative practices of governmental regulations as a necessary aspect of a modern, organization-based society. As March and Olsen [1983, p. 292] suggest:

> [Our] observation is that governance is an interpretation of life and an affirmation of legitimate values and institutions. In a society that emphasizes rationality, self interest, and efficacy, politics honors administrative and realpolitik rhetoric, it provides symbolic and ritual confirmation of the possibility of meaningful individual and collective action. The argument is not that symbols [such as the rationality and objectivity achieved through accounting] are important to politics, although they certainly are. Rather, the argument is the reverse — that politics is important to symbols, that a primary contribution of politics to life is in the development of meaning. It is not necessary to decide here whether decision making and the allocation of resources are symbols and the construction of meaning are more fundamental. They are heavily intertwined, and discussion of primacy may obscure that fact. But itseems unlikely that a theory of governance can represent or improve the phenomena of governing without including the ways political institutions, rhetoric, and the rituals of decisions facilitate the maintenance and change of social values and the interpretation of human existence.

Thus, accounting as a symbol of rationality, efficiency and science within state governance came to be politically constituted as opposed to being solely the product of rational actions and events within the private sector. That Commons' "reasonable value" and rate of return regulation impacted accounting and economic thought is attested to by its use in regulating utilities for most of this century and by research in economics and accounting probing its efficacy for over eighty years [illustrative are Averch and Johnson, 1962, pp. 1052-1055; Sappington, 1983, pp. 363-370; Baron and Myerson, 1982, pp. 911-915; Abdel-khalik, 1988, pp. 44-62; Lanen and Larcker, 1992, pp. 71-81].

To be sure, Commons recognized imperfections in the state apparatus in general and the techniques of regulators in particular, that there exists no universal truths as represented by economic "laws" and accounting "facts." A "coping schizophrenic" [Campbell, 1970, pp. 1-23], he nevertheless continued to struggle with the paradoxes of his era. According to Hoksbergen [1994, p. 708]:

> On the one hand, there are what might be called extreme relativists, who upon the discovery that there is no objectively certain foundation for the true, the good, or the beautiful, jump to the conclusion that nothing matters. On the other hand, there are those who accept the demise of foundationalism and acknowledge the existence of many different traditions of understanding but still have a deep sense that it does matter, that there is meaning to our lives, and that we can continue the struggle to improve our understanding and our lives. I am persuaded by the latter position, and because the participants in the debate [such as John R. Commons] have cared enough to write down their thoughts on the issue, I presume they are persuaded, at least in practice, by that position too.

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