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Now More Than Ever, Consumers Need Protection—not More Energy Deregulation

It is unfortunate that Republicans and Democrats alike propose repealing a key federal consumer protection, the Public Utility Holding Company Act (PUHCA) just when courts are finally using the law to rescue consumers. At a time when the Enron disaster and the failure of electricity deregulation across the country (a dozen states have repealed or delayed their deregulation laws) illustrate how vulnerable consumers and investors are to impenetrable corporate structures and unaccountable markets, PUHCA's protections are needed now more than ever.

Enron's collapse exposed consumers and investors to the dangers of inadequate government oversight inherent in electricity deregulation. The combination of deregulated state wholesale electricity markets, federal deregulation of commodity exchanges and the gutting of PUHCA removed accountability and transparency from the energy sector. California's recent energy crisis and Enron's bankruptcy would have been impossible under a regulated system.

PUHCA is the most important protection the federal government provides for electricity consumers. But the law's potency has been eroded over the last decade, with Enron responsible for undermining the act's effectiveness by spearheading many of the loopholes. Incredibly, rather than proposing to close these Enron-exemptions to prevent other energy companies from abusing consumers and investors, the response by the Bush Administration and Congress (including the Senate Democrat energy bill) is to *repeal the entire law, and replace it with no consumer protections*. Repealing PUHCA will lead to a rash of mergers, threatening consumers.

Although proponents of repealing PUHCA claim that the law's ownership restrictions hinder adequate investment, the industry is only interested in purging PUHCA to satisfy their craving for Enron-style accounting freedom and *convergence*. If PUHCA were repealed, a flurry of mergers would bury our electricity markets, rendering states incapable of regulating sprawling multi-state holding companies, and besiege an already overwhelmed Federal Energy Regulatory Commission (FERC). Both Democrats and Republicans propose replacing PUHCA with access to the companies' books. But these huge holding companies will have incentive to cover their tracks with Enron-esque accounting, and no state or federal agency will be able to verify the accuracy of the bookkeeping.

PUHCA currently prevents regulated holding companies from *convergence*—the desire of energy corporations to extend their control beyond electricity into telecommunications, water and other essential consumer services. PUHCA's repeal will result in giant holding companies, threatening consumers by consolidating unaccountable corporate control over crucial commodities.

How PUHCA Protects Consumers and Shareholders

PUHCA was enacted in 1935 in response to America's first Enron-style energy crisis in the 1920s. A handful of energy companies, employing business strategies strikingly similar to Enron's, held consumers hostage with complex, multi-state pyramiding schemes. These holding companies jacked up prices by purchasing financial, fuel and construction services through a complex web of subsidiaries. Not only were consumers overcharged by these impossible-to-regulate ploys, but investors were robbed because the holding company's assets were inflated. These pyramiding holding companies finally collapsed, ringing in the stock market crash of 1929 and the Great Depression.

The Securities and Exchange Commission (SEC) enforces PUHCA, which protects consumers by ensuring that multi-state utility companies re-invest ratepayer money into providing affordable and reliable electricity. A corporation must register as a "holding company" if it owns at least 10% of the stock of an electric or natural gas utility. Consumers benefit from PUHCA's requirements that holding companies only invest in "integrated systems"—utilities that are "physically interconnected"— thereby maximizing economies of scale by operating a single, coordinated system. PUHCA has historically prohibited holding companies from investing ratepayers' money in areas that will not directly contribute to low bills and reliable service (out-of-region power plants or non-electricity industries such as water and telecommunications).

PUHCA's Consumer Protections Have Been Eroded

PUHCA has lost much of its teeth over the decades as a result of deregulation, Enron's lobbying, and decisions by the SEC to simply ignore the law. First, Congress undermined PUHCA by passing the 1992 Energy Policy Act, permitting holding companies to invest ratepayer money in foreign power projects and divert resources away from American consumers. Second, Enron pushed a gaping hole in SEC jurisdiction when the SEC, in response to a petition by the company, exempted power marketers like Enron from PUHCA on Jan. 5, 1994. As a result, power marketers—creatures of deregulation that don't own power plants but rather trade electricity contracts—can trade free from government oversight in deregulated markets across the country. Finally, the SEC has refused to enforce PUHCA, instead rubber-stamping mergers that are in direct violation of PUHCA's consumer protections—including the foreign acquisition of several U.S. utilities.

These loopholes have already resulted in a significant increase in utility consolidation. In 1992 (prior to the passage of the loophole-creating Energy Policy Act) the largest 10 utilities owned one-third of the national generating capacity. By 2000, the top 10 owned half of all capacity, while the top 20 owned 75%. These numbers will become more concentrated if PUHCA is repealed.

Mend PUHCA, Don't End It

Had PUHCA's loopholes been closed and the law properly enforced, Enron's fraud against shareholders and consumers never could have occurred, because PUHCA's ownership limits would have prevented the company from hiding revenues and debts in off-shore tax havens and failed foreign projects, like Enron's Dabhol power plant in India. So the solution is to close the loopholes and strengthen PUHCA. First, Congress must mandate the SEC to strictly enforce the act, and beef up funding and staff for the SEC so they can do the job right. Second, the harmful loopholes pushed through by Enron and other energy companies must be closed. Holding companies must no longer be allowed to invest in foreign countries, and power marketers must be subject to PUHCA. Third, Congress can improve PUHCA by using it to address issues of market power. For example, Congress should grant federal and state regulators the authority to order holding companies to divest assets, expand anti-trust investigations and enforcement, and create non-profit, consumer owned regional transmission councils to ensure non-discriminatory access to the grid.

It is important to note that the tide is already beginning to turn. In January 2002, the U.S. Court of Appeals for the District of Columbia ordered the SEC to revisit their decision to approve a merger between American Electric Power (AEP) and Central & South West (CSW). Public Citizen had maintained that the SEC's earlier decision to approve this merger between Ohio-based AEP and Texas-based CSW violated PUHCA's requirements that holding companies have interconnected systems. The SEC had sloppily ruled that because the two utilities are connected by a lone, 250-mile transmission line *owned by an unrelated company* that the merger satisfied PUHCA. The judge's decision illustrates that the court has finally noticed that the SEC has refused to enforce the law, and will force the review of other recently approved mergers that clearly violate PUHCA (Progress Energy, a union between Florida Progress and Carolina Power & Light; Exelon, a product of PECO Energy and Unicom; Xcel, a merger between Northern States Power and Public Service Co., and the foreign acquisition of Oregon-based Pacificorp by Scottish Power).