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PUHCA at Work Protecting Consumers in 2005

The Senate energy bill repeals the Public Utility Holding Company Act of 1935 (PUHCA), the most important electricity consumer protection statute, replacing it with very weak provisions giving the Federal Energy Regulatory Commission increased authority over utility mergers. The many corporate interests seeking repeal of PUHCA—in order to make large profits off of utility consumers—insist that PUHCA is an “outdated, Depression-era” law. If reasonable electricity and natural gas rates are “outdated,” then this claim is correct. Ironically, many opponents of PUHCA point to the Federal Power Act or the antitrust statutes, both laws older than PUHCA, as providing an adequate replacement for its “outdated” consumer protections.

Despite poor enforcement of PUHCA by the Securities and Exchange Commission (SEC), the federal agency entrusted with enforcement of the statute, PUHCA continues to protect utility consumers.¹

◆ **Investment credit ratings of PUHCA-regulated holding companies are better than those of unregulated companies**

Ratings agencies *Standard and Poor's* and *Fitch* both issued reports in 2004 finding that utility holding companies regulated under PUHCA had better credit ratings than those that had been exempted from PUHCA. S&P found that PUHCA's limitations on investment of utility revenues in non-utility businesses should be strengthened. S&P also rejected the claim that PUHCA was preventing investment in utility infrastructure. In fact, it found that the opposite was true, since investors like strong credit ratings. Fitch's report pointed out the indirect bad effects on an operating utility when the holding company's credit is lowered. A classic example was when utility holding company, Xcel, put all of its PUHCA-unregulated businesses into a subsidiary, an un-PUHCA-regulated utility, NRG, which promptly went bankrupt, lowering the credit rating of the three remaining PUHCA-regulated Xcel subsidiaries. Utility holding company, Southern Company, put its unregulated businesses in a spin-off company, Mirant, which went bankrupt and is now suing Southern. Numerous other PUHCA-exempt power plant owners and power marketers have either declared bankruptcy or sold off their power plants, often at “fire sale” prices, resulting in a lowering of credit ratings for the entire sector.

◆ **Zero PUHCA-regulated electric utility holding companies have declared bankruptcy**

Pre-PUHCA, 53 utility holding companies went bankrupt, and 23 more defaulted on bank loans. However, because the SEC has granted Allegheny Energy numerous waivers from PUHCA compliance, the company is getting close to bankruptcy. An investor in Allegheny Energy, Harbert Distressed Industries Master Fund, filed a complaint on February 18, 2005, requesting the SEC to enforce PUHCA, discontinue the waivers, and save the credit of Allegheny.

¹ The PUHCA staff of the SEC appears to represent a classic case of “regulatory capture,” primarily promoting the interests of the utility owners that PUHCA is designed to regulate. As a result, the SEC is currently under investigation by the Government Accountability Office (GAO) to determine whether the SEC is enforcing PUHCA.

- ◆ **Thanks to PUHCA, state regulators are able to continue to protect ratepayers**
Without PUHCA, the Oregon Public Utility Commission would not have been able to protect the Oregon utility, Portland General Electric (PGE), as much as it did from Enron's ownership and bankruptcy. Enron obtained a "single state" PUHCA exemption, where the holding company incorporated in the same state as its operating utility, which gives the state the opportunity to regulate the holding company's activities under state corporate law. If the holding company is incorporated elsewhere, the state has no such opportunity and it is up to the SEC to regulate the holding company. If PUHCA is repealed, no entity will be able to regulate a holding company's finances and investments for the protection of utility customers, even if there is "ring-fencing" to directly protect the utility's revenues from its parent.

- ◆ **PUHCA breaks up or regulates multi-state holding companies**
One of the chief goals of PUHCA was to break up the huge, multi-state utility holding companies that cannot be effectively regulated by any single state, and to prevent their re-creation. After the break-up, only 12 multi-state holding companies existed and these were strictly regulated by the SEC. However, since 1995, the SEC has been engaging in a "flexible" interpretation of the statute and has allowed the creation of a growing number of new, multi-state holding companies that cannot be effectively regulated by any state.

Even with lax SEC regulation, PUHCA itself restrains giant utility holding company mergers. The SEC's order approving the 2000 merger between giant utility holding companies American Electric Power Inc. (AEP) and Central and Southwest Corp (CSW), which cover eleven widespread states, was vacated and remanded by an appellate court as failing to explain how it met the merger standards under PUHCA. A subsequent decision by an SEC law judge found that the merger failed to meet PUHCA's requirement that the merged utility would operate in a "single region" of the country so that it could be effectively regulated. AEP has appealed. If PUHCA is repealed, no state and no federal agency will be able to effectively regulate the growing number of multi-state holding companies; today, 31 top registered companies exist. These are all now regulated under PUHCA, but without it, they will be free to merge with one another and massively consolidate *unregulated* control over utilities.

Apparently in anticipation of PUHCA repeal, several huge and geographically distant utility mergers are already in the works: Exelon (headquartered in Illinois) has proposed to acquire PSEG (New Jersey), resulting in the largest utility in the country; Duke (North Carolina) has announced that it will acquire Cinergy (Ohio), and MidAmerican (Iowa) has proposed to acquire PacificCorp (Oregon and five other states in the Pacific NW). Without PUHCA to restrain either the size or geographic reach of utility holding company mergers, we may once again see the massive consolidation of unregulated utility ownership and the related abuses that originally precipitated enactment of PUHCA.

- ◆ **PUHCA is preventing an oil/natural gas/electric utility cartel**
PUHCA does not allow non-utilities, including oil companies, investment banks, insurance companies, engineering companies, and others, to own public utilities. The ownership ban is accomplished by Section 11, which requires the divestiture of non-utility businesses if a public utility is acquired. If PUHCA is repealed, there will be nothing to prevent the oil companies—which have a lot of extra cash right now—from buying up both electric and natural gas holding companies and other systems. Then we will have a cartel not only setting our gasoline prices, but also our prices for electricity and natural gas.