How Electricity Dereg Causes Blackouts

by Marsha Freeman

During the Winter of 2000-01, citizens in California watched while rolling blackouts shut the lights off in their homes and workplaces. The previous Summer, the state's utilities watched while an unregulated power mafia drove electricity prices from $30 to $3,000 per megawatt-hour. Deregulation had opened the state to manipulated "shortages" designed to drive up prices—and to power marketers like Enron, which made a financial killing trading on the volatility of the market. Deregulation eventually drove the state's largest utility, and the state itself, into bankruptcy.

In early 2001, Lyndon LaRouche proposed a straightforward—and the only—solution to the crisis: Re-regulate the electric utilities. Go back to the framework set up in the 1930s by President Franklin Delano Roosevelt, which established that the provision of universally available, reliable, affordable electricity is a public good, and a government responsibility.

An increasing number of state legislators agreed with LaRouche that that might be the right thing to do, as the California crisis worsened. But, they protested, "You can't put the toothpaste back in the tube." LaRouche replied, "Oh, yes, you can." And there is no other choice.

Now, a study released on Aug. 24, conducted by a group of engineers with years of high-level experience in the electric power industry, documents in detail what had been the case in the earlier California crisis: that the Northeast blackout that affected 50 million people on Aug. 15, 2003, was caused by deregulation.

Power Engineers Supporting Truth (PEST) was formed in 2003 in order to review and evaluate then-forthcoming reports from investigations of the 2003 blackout. As retired executives, they said, they are "no longer constrained from speaking out by employment or financial ties." They report that they were "disheartened by the failure of the leadership" of professional organizations which did not speak out, when incompetent, if not compromised, investigations into the blackout were being carried out.

According to George Loehr, a PEST founder, more professionals do not speak out either because they are afraid, or they have been "bought off" with bonuses and other financial carrots. What had been a "culture of cooperation," he says, after the 1965 blackout in New York City, was destroyed by deregulation. "Commercial entities" infiltrated the industry, with Enron being the most aggressive, to promote policies and water down reliability standards to see "how much power they could push around the system."

The PEST report, "Contributions of the Restructuring of the Electric Power Industry to the Aug. 14, 2003 Blackout," states unequivocally that "deregulation and the concomitant restructuring of the electric power industry in the U.S. have had a devastating effect on the reliability of North American power systems, and constitute the ultimate root cause of the Aug. 14, 2003 blackout."

The Danger of Putting Profits First

Deregulation was based on "an almost fundamentalist reliance on markets to solve even the most scientifically complex poblems," the report states. Optimizing reliability has been replaced by a "total dependence on immediate profits." With deregulation, "the emphasis shifted from technical knowledge and competence to financial and marketing knowledge. Economic theory replaced engineering fact."

What have companies done to be "competitive"? According to the report, between 1990 and 2000, investment in new transmission capacity fell at a rate of about $50 million per year. Between 1990 and 1999, the labor force in the generation industry decreased from 480,000 to 350,000. There was an additional ratchet collapse in manpower from 1999 to 2000, when the number of employees in power-generation fell from 350,000 to 280,000, and in transmission and distribution, from 196,000 to 156,000.

To maximize profits, companies reduced or eliminated the training of professional engineers and systems operators. Senior personnel were encouraged to take early retirement, "effectively ending the transfer of essential expertise from one generation to the next."

The transfer of operation and oversight of transmission assets from professionals in the industry to Federal regulatory agencies, put electricity delivery in the hands of bureaucrats with little or no knowledge of the complexity of the transmission system. The notorious Federal Energy Regulatory Commission (FERC), from its inception has been staffed largely with pro-deregulation neo-conservative ideologues, who lack any knowledge or expertise for their positions, "or are beholden to certain segments of the industry," the report states. (Enron's financing of President Bush's career, its role in formulating Vice President Cheney's energy "policy," and its role in "recommending" who gets chosen for key energy regulatory positions are well known.)

The engineers' report ridicules the conclusion of previous studies of the 2003 blackout, conducted for the Department of Energy, for blaming untrimmed trees, lack of communication, and other specifics, rather than finding the root cause. The problem is "not an error or two in procedures or protocols," but "a belief system." An indication of this, it says, "is the fact that, despite such evidence as the California Meltdown, unprecedented price spikes, the criminal actions of Enron and others, and the most devastating blackout in our history, policy makers still steadfastly deny that deregulation and restructuring had anything at all to do with any of it. Sociologists call this 'cognitive dissonance.' "

The engineers conclude that unless the root causes of the 2003 blackout are reversed, "the likelihood of future blackouts will increase."

From Bad to Worse

That the lessons of the California crisis and the Northeast blackout are yet to be learned is shown by the repeal of the Public Utility Holding Company Act (PUHCA), in the recently enacted Energy Bill. PUHCA, promulgated by Franklin Roosevelt, prevented holding companies from extending their service area into noncontiguous territories, limiting them to serve their regions. It barred foreign purchase of U.S. utilities, and allowed very limited non-utility investments by electric companies. PUHCA built a wall between the regulated electricity company, and any unregulated subsidiaries it might hold, to prevent customers from being milked to bail out failed, high-risk investments. It required holding companies to register with, and meet the standards set by, the Securities and Exchange Commission (SEC). As FDR intended, the law drove Wall Street and speculators out of the utility industry, and broke up the holding company conglomerates which had had a stranglehold on the industry.

Congress and Federal (de)regulators had been nibbling away at the restrictions and protections under PUHCA since the push for deregulation started in earnest in 1992. At that time, Congress legislated that American utilities would be allowed to purchase foreign utilities, and vice versa. The Securities and Exchange Commission moved into a more "flexible" interpretation of PUCHA, as utilities merged and the number and assets of holding companies mushroomed.

A day after President Bush signed the Energy Policy Act of 2005, which repealed PUHCA, Aug. 8, the General Accountability Office of the Congress released a report suggesting that the SEC should more *strongly* enforce PUHCA's restrictions! Over a decade, the GAO reports, the number of holding companies registered with the SEC went from 15 to 31 in 2004. An additional 81 claimed, and were granted, exemptions from SEC standards.

There are already shadows of what lies on the horizon with PUHCA repeal. Southern Company, which produces power and delivers it to millions of consumers in the Southeast, spun off an unregulated subsidiary, Mirant Corp., to get in on the speculative frenzy of Enron-inspired power marketing. Mirant is now bankrupt, and is suing Southern. Will electricity customers end up bailing out the power pirates, the very thing that PUHCA had prevented?

But even the SEC itself finally thought FERC's granting of approval for far-flung mergers, and its own rubber stamp, had gone a bit too far. On May 3, SEC Administrative Law Judge Robert G. Mahony ruled that the acquisition by Ohio-based American Electric Power Co. of Central & South West Corp. of Texas in June 2000 violated a key provision of PUHCA.

PUHCA, as even the *Wall Street Journal* noted, had been made nearly "moot," as the SEC joined FERC in making deregulation *de facto* Federal law, in many cases, without Congressional approval or oversight. So what convinced a bipartisan majority in the Congress to repeal a law that for 70 years had protected the American people from abuses?

The Congress has fallen, once again, for the siren song of deregulation promises. "I'll invest $10-15 billion in the capital-starved energy sector, if you just repeal PUHCA," says mega-speculator Warren Buffett, through his Berkshire Hathaway-owned MidAmerican Corp., just as Enron CEO Ken Lay had promised gullible California state legislators in 1996 that the price of electricity would be lowered dramatically, if they passed a deregulation law.

Deregulation, which was sold to the public as a way to increase "competition," has, in fact, led to a consolidation of the industry, where utilities that have merged now own power plants spread across ten or more states, making it impossible for state utility commissions and regional reliability councils to maintain control over their regions of responsibility. Now, with the repeal of PUHCA, "merger mania" is expected, and new "players" will enter the field. (See "Will Warren Buffett Be the New Samuel Insull?" *EIR,* Aug. 26, 2005.)

Not everyone has been hoodwinked. In July 2004, Public Citizen filed a lawsuit which challenges a key tenet of deregulation. The suit charges that FERC is in violation of the Federal Power Act. That Federal law states that wholesale rates will be set that are "just and reasonable," not what the market will bear. FERC's "market rate" regulation scheme, in which companies virtually set their own price for selling electricity, allowed them to manipulate the "market" and overcharge consumers billions of dollars. The suit was filed in the District of Columbia Circuit U.S. Court of Appeals by State Attorneys General of New Mexico and Rhode Island, state agencies in Colorado and Utah, the National Consumer Law Center, and consumer advocacy organizations,

The attorney of record, Lynn Hargis, who worked for FERC for ten years, says there will be a "massive consolidation" of the industry now that PUHCA is repealed. The oil industry, known for monopoly control and price fixing, she says, will now buy up utilities. The prospect that investment banks will also join the merger spree is "frightening." FDR's purpose in PUHCA, she says, was not just to regulate the electricity industry for the benefit of the consumer, but to "control the investment banks."

No patchwork of proposals to mitigate the disaster caused by deregulation will restore this critical infrastructure. The only solution is to "put the toothpaste back into the tube."