

Report on the Spring Meeting: '21st Century Regulation, Paradigms under Pressure'

By *Bethany L. Appleby*

This year's spring meeting of the Section of Public Utility, Communications and Transportation Law, held at Pepco Holdings' Washington conference center on April 10, was well attended and aptly named.

The meeting's general theme, "21st Century Regulation, Paradigms under Pressure," is clearly a topic that has been weighing on the minds of the speakers and attendees for quite a while. Nearly every speaker commented on the effects of technology, particularly the Internet, on the industries that the Section serves, and the pressing need for effective industry and regulatory leadership in the future.



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Speakers were distinguished and varied, including state public utility commissioners, the chief of the Wireline Competition Bureau at the Federal Communications Commission, general counsel, outside counsel, energy industry consultants, and a judge on the Seventh Circuit Court of Appeals. As could be anticipated given the variety of their backgrounds, the participants did not always agree on the effects of regulatory changes at the state and federal level, or what would happen in the regulatory environment in the future.

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Gerald A. Connell, Section chair, kicked off the program in his welcoming remarks. Linda L. Randell, program chair, introduced the keynote speaker, Diane Munns, the president of the National Association of Regulatory Utility Commissioners (NARUC) and a board member of the Iowa Utilities Board. Munns, who is a lawyer as well as a regulator, described the changes in the Iowa utilities landscape over the past few years, including the recent organization of MISO, the Midwest ISO.

She advocated a regional approach to planning and regulation, to the extent appropriate and possible, and identified three questions that Congress should answer:

- What, if anything, does government need to do?
- How should government act, that is, with upfront regulation or in response to market failures?
- What level of government (state vs. federal) is appropriate for establishing any necessary regulation?

Munns also urged that any federal regulatory framework ensure that states have the flexibility to act where appropriate, particularly with respect to consumer protection concerns.

She acknowledged that these are trying times for the electric industry, and warned that higher electricity prices are on the horizon no matter what regulatory — or deregulatory — systems are in place in a particular state or region. Like some of the other speakers, she commented on the recent announcement that Baltimore electricity ratepayers were about to be faced with a 79-percent rate increase in June of this year, and noted that customers in other areas have seen or will see similarly dramatic increases.

A segment entitled “Airlines — the Original Changing Paradigm” explored the longer-term effects of deregulation by examining developments in the airline industry since the 1977 deregulation of cargo by air and the 1978 deregulation of passenger air travel. Speakers for this segment were Dr. Howard Axelrod, president of Energy Strategies Inc. in Albany, N.Y.; Dr. Brian Campbell of the Campbell-Hill Aviation Group Inc. in Alexandria, Va.; and Frank J. Costello, a partner at Zuckert, Scoutt & Rasenberger in Washington.

Roughly 30 years after deregulation, the airline industry faces many risks and has seen many players fail, yet there is active competition, and the ability to price fares without agency approval has led to greater choice and greater flexibility.

Costello noted that the industry is still among the most heavily regulated. There is extensive federal aviation administrative oversight and controls, even if airlines now have the ability to decide themselves what to charge customers, rather than having to obtain regulatory approval for pricing. Axelrod criticized airline management as being unimaginative and holding to an irrational pricing structure.

Campbell appeared the most enthusiastic concerning the benefits of airline deregulation, citing, among other things, service innovations and lower prices. He also pro-

vided an interesting and instructive historical background to airline deregulation, saying that the moving force behind the industry’s deregulation was the lobbying efforts of Fred Smith of Federal Express, whose efforts to expand had been stymied by almost insurmountable barriers to new players in the industry.

The next segment was “The Case For/Against Complete Deregulation of Communications, Video and Internet.” The speakers for this segment were Daniel R. Conway, a partner at Porter Wright Morris & Arthur LLP in Columbus, Ohio; Maureen Helmer, former chair of the New York Public Service Commission and presently in private practice in Albany; Thomas Navin, chief of the Wireline Competition Bureau of the Federal Communications Commission; T. Michael Payne, senior vice president and general counsel of AT&T Communications Corp.; and David R. Poe, a partner at LeBoeuf, Lamb, Green & MacRae in Washington.

These speakers addressed the types of new technological innovations and communications media, how they should be regulated and the appropriate role, if any, of state regulation. Helmer, asked to present the issues of interest to regulators based on her former work as a state regulator, noted that certain areas, such as public welfare, were probably appropriate for regulation, such as establishing a 911 obligation for voice-over-Internet providers.

Poe similarly acknowledged that there were legitimate areas for regulation, such as the use of public rights of way and the federal government’s allocation of spectrum. However, he also pointed out that regulation does not do certain things well, including choosing among competing technologies and predicting the course of competition.

Payne advocated minimum governmental regulation, citing lessons learned from the development of competition in the cellular industries. He also warned that companies will not invest in infrastructure and technological innovations if they believe that current or future regulation may force them to make their investments available to their competitors.

The luncheon speaker was William F. Hederman, the founding director of the Federal Energy Regulatory Commission’s Office of Market Oversight and Investigations and currently the executive director of Morgan Lewis Energy Resources Group in Washington. He described FERC’s expanded jurisdiction with respect to enforcement and penalties and the establishment of mandatory reliability standards. He also discussed FERC’s new Office of Enforcement and increased staffing levels to implement FERC’s new powers and responsibilities.

The speakers in the next segment were Dr. John A. Anderson, president and CEO of the Electric Consumers Resource Council (ELCON); James S. King, a partner at Couch White, LLP in Albany, N.Y.; Donald L. Mason, chairman of the NARUC Gas Committee and commissioner of the Public Utilities Commission of Ohio; Douglas L. Miller, senior counsel at Alston & Bird LP in Atlanta and former senior vice

president and general counsel at Mirant; and Christopher Warner, chief counsel, corporate and regulatory at Pacific Gas and Electric Co. (PG&E) in San Francisco.

This segment was “Electric and Gas: Successful Deregulation, or, Is There a Case for Re-Regulation?” King discussed the disconnect between the goals of electric restructuring and the apparent results. Anderson asserted that today’s “organized markets” are not competitive and that the current market conditions are worse than traditional regulation. He also noted that what is referred to as “restructuring” simply established a *new* form of regulation.

Anderson discussed his six “essential preconditions” for competitive electricity markets:

- efficient and effective Regional Transmission Organizations (RTOs) with nondiscriminatory stakeholder processes;
- markets, not regulators, must set prices;
- price-responsive loads and generation must be treated symmetrically;
- market power must be mitigated;
- there must be adequate transmission infrastructure; and
- federal and state regulators must cooperate rather than compete.

Mason discussed Ohio’s efforts to create a level playing field for gas and electricity industry participants in Ohio. An important feature is to alleviate companies’ bad-debt risk. Miller’s view was that while electricity prices are up everywhere, prices in unregulated states have increased *less* than those in regulated states. He also noted that providing adequate compensation to capacity is critical to revenue adequacy, which is critical to resource adequacy.

Warner spoke about developments in California since the difficulties there, including PG&E’s innovations and efforts to thrive in the current environment.

He discussed the company’s recent agreement to return to the construction, ownership and operation of generation through a turn-key construction contract for the generation. This is a significant change in California, which was a leader in utility divestiture of regulated generation.

Walton F. Hill, vice president of regulatory business at United Water and Kathy L. Pape, vice president, treasurer and rate counsel of Aqua America Inc., and William D. Patterson, senior vice president and CFO of Pennichuck Corp., discussed the changes and challenges affecting the water industry today. Anthony M. Macleod, a partner at Whitman Breed Abbott & Morgan LLC in Greenwich, Conn., was the moderator.

Hill presented the history of non-U.S. ownership of water companies. He discussed United Water, which dates back to 1868 and now encompasses 25 utilities in eight states and more than 550,000 customers. A significant portion of United Water’s revenue also comes from contract operations, pri-

marily wastewater. Its focus has changed from large municipalities to small/medium contracts. Suez has four business lines — Energy Europe, Energy and Industrial Services, Energy International and Environment (water and waste services) — and almost \$50 billion in revenues, most of which comes from North America and Europe.

He also discussed the increasing privatization of water and wastewater in Europe and the consolidation of publicly traded water industry companies in the United States.

Pape noted that the U.S. water industry is currently highly fragmented and inefficient, although consolidation is increasing and European companies and private equity are becoming involved. Water demand has increased dramatically, raising infrastructure and reliability concerns. Water is provided through regulated monopolies and is the lowest cost utility to consumers.

There are also high barriers to entry by new players, including the significant capital required compared with other industries. While electric utilities have ventured into the provision of water services, many have chosen to leave the business. She also discussed the difficulty of maintaining Standard & Poor’s credit ratings in the current regulatory environment.

Patterson discussed the history of water service, water mains and eminent domain. In the year 1800, 93.7 percent of water was privately supplied. In less than 100 years, by 1896, only 46.8 percent of water was privately supplied. He explained that, more recently, investor-owned utilities’ market share has continued to decrease and industry consolidation/regionalization has continued. Foreign ownership and electric-company purchases have not changed the trend of municipal ownership (and may have spurred consolidation), and municipal outsourcing has accelerated. He also noted that wastewater opportunities may now exceed drinking water opportunities.

The day closed with Judge Richard D. Cudahy, well known for his decisions on regulatory matters that have reached the appellate court and a former regulator himself, providing perspective on the sometimes conflicting, sometimes agreeing industry commentaries.