

NGI's Power Market Today

Breaking News : posted Jul 10, 11:11 AM

Consultant Challenges Economists Over State of Competition

Outspoken energy economic consultant, Robert McCullough strongly challenged a group of well-known economists' open letter late last month to policymakers to stay-the-course on electric industry competition. McCullough argued that real-world experience resulting in generally higher retail power utility rates flies in the face of his colleagues' recommendation. He strongly objected to the economists telling policymakers that competition currently is working in the industry and fired off a rebuttal letter to the economists, who include Alfred Kahn and Paul Joskow.

McCullough told Power Market Today late Friday that he doubted he "would set a fire that will inflame the Western world" from his rebuttal, but policymakers should not keep "ignoring the problems showing up" with what he called centralized industry restructuring. He would much prefer adoption of the natural gas industry restructuring model with an open, wholesale market where anyone can enter and leave.

That gas model was replicated in the 1980s in the Northwest by the old Western Systems Power Pool (WSPP), McCullough said. "People who want to play, can play, and those who don't want to, don't have to. That allows the market to evolve, but what we have ended up with instead are some pretty artificial alternatives." In contrast to the WSPP approach, he said, when the Maryland auction model, or the one proposed in Illinois, is analyzed, "you conclude, this is a long way from competition; in fact, it is sort of a step away from it."

Contending he shared his fellow economists' commitment to competition, the Portland, OR-based McCullough said that secretiveness and high-cost bureaucratic operations of the nation's regional transmission organizations (RTOs) -- a regular focus of the former Pacific Northwest utility executive's criticism -- prevent the current industry from functioning competitively in a transparent manner. He said in his letter he is not surprised that "price controls are very common" as a result.

A catalyst for the public economic debate is the Electric Energy Market Competition Task Force report at the Federal Energy Regulatory Commission (FERC) that has drawn industry stakeholder comments on a draft document released June 5. This prompted the eight economists led by Joskow to publish their June 26 open letter recommending that policymakers "stay the course and continue to support restructuring and evolution of competitive wholesale and retail markets for power" (see Power Market Today, June 29).

In addition to Kahn and Joskow, affiliated with Cornell University and MIT, respectively, other signatories were William Hogan (Harvard), Peter Cramton (University of Maryland), Howard Axelrod (Energy Strategies Inc.), Vernon Smith (International Foundation for Research in Experimental Economics), David DeRamus (Bates White, LLC), and Gary Hunt (Global Energy Decisions).

Never shy about going against prevailing views, McCullough said in a prepared statement that the United States now needs "the best possible

advice on how to reform electricity deregulation, and telling policymakers that competition is working if only we give it more time is simply wrong." He called out the state of Maryland as an example, saying projections were calling for a 72% increase in retail power rates until the state legislature stepped in last spring.

McCullough said that economists can "do immense harm when we choose to ignore the political and social realities of our market experiments."

To his eight colleagues, McCullough warned that "disaster awaits" in the upcoming Illinois first-ever state-run electricity auction because the process is being "undertaken in secrecy." He cited the fact that even the sign-in sheet used at a bidders' conference last month was designated as "classified information."

Claiming that at least four western states (California, Montana, Oregon, and Washington) still have not fully recovered from the 2000-2001 wholesale energy market meltdown, McCullough suggested to his economic colleagues that the power industry and competition would be better off if what he called the "ponderous bureaucracies of the RTOs" could be eliminated, and the industry could be returned to what he called the "open outcry market," something he claims the federal Bonneville Power Administration (BPA) pioneered in the early 1980s establishing an open market for 3,000 average-MW of nonfirm hydroelectric power.

"Prices were set by open outcry in the old WSPP without the supervision of special governments formed to manage prices and quantities [presumably RTOs]," McCullough wrote in his letter.

Posing the rhetorical question with the negative answer, McCullough concluded his letter by asking, "Would eBay flourish if the rules were arcane, the bidding secret, the participants unknown, the regulators largely absent, and a massive bureaucracy was required to manage each and every transaction?"

©Copyright NGI Inc. All rights reserved. The preceding news report may not be republished or redistributed, in whole or in part, in any form, without prior written consent of Intelligence Press, Inc.