

# RETAIL WHEELING: IS THIS REVOLUTION NECESSARY?

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## I. INTRODUCTION

As of a former state regulator and a once enthusiastic practitioner of public utility law, I find it fascinating to see the latest nostrum to burst on the electric utility scene: retail wheeling. Wheeling became a personal interest in the Texas interconnection<sup>1</sup> fight of the late seventies and may have led to the interconnection and wheeling provision of the Public Utilities Regulatory Policies Act (PURPA).<sup>2</sup>

Retail wheeling contemplates that every electric power customer should be given an opportunity to seek out the lowest cost source of power wherever it can be found. As a practical matter, the drums for retail wheeling are presently being beaten by large industrial users, who believe that they have the capability to find low cost sources and to make advantageous commercial arrangements to acquire electricity.<sup>3</sup> Large industrials have long been fighting the utilities for cheaper electricity, frequently using the threat of self-generation and cogeneration.<sup>4</sup>

Today, the argument for retail wheeling is that it would create a free market in electrical generation, provide a maximum opportunity for competition in generation, and thereby apply the most potent stimulus possible for efficiency in the industry. It is the rhetorical cloud on which this wheeling proposal floats that is particularly entrancing. Its advocates state with messianic conviction that retail wheeling will revolutionize (perhaps by overthrowing) the regulatory regime that has heretofore governed the distribution and pricing of electrical power.<sup>5</sup> Bureaucratic decision-making by government will play only a sharply declining role in the brave new world

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1. See *Central Power & Light Co. v. FERC*, 575 F.2d 937 (D.C. Cir.), *cert. denied*, 439 U.S. 981 (1978). The Honorable Richard D. Cudahy was a participant in this litigation.

2. 16 U.S.C. §§ 2601-2645 (1988). Compulsory wheeling authority in the Federal Power Commission was not adopted in the 1935 enactment of part II of the Federal Power Act (FPA). It did not resurface until 1978 in the PURPA (where the perplexing language—partly attributable to the Texas imbroglio—contributed to its subsequent non-use). The 1992 enactment, Energy Policy Act of 1992 (EPAAct), Pub. L. 102-486, 106 Stat. 2776, 2905-21 (1992) (codified at 42 U.S.C.A. §§ 13,201-556 (West Supp. 1993)), therefore, seems the first practicable compulsory wheeling provision—although, of course, restricted to the wholesale sphere.

3. See Frederick H. Lowe, *Manufacturers Try to Turn Off Utility Monopolies*, CHI. SUN-TIMES, May 8, 1994, at 1.

4. See *In re Commonwealth Edison*, 24 Pub. Util. Rep.2d (PUR) 209 (I.C.C. 1958).

5. See Thomas G. Donlan, *California Dreamin': The Sunset State Tries the Free Market On For Size*, BARRON'S, Aug. 29, 1994, at 46.

to come; the guiding regulatory framework will be sketched instead by Adam Smith's invisible hand.<sup>6</sup>

The most vocal opponents of retail wheeling, on the other hand, have been the environmentalists, who see external environmental costs ignored in a chaos of unregulated market transactions, leaving no "excess" revenues available to subsidize conservation, demand-side management programs, and other worthy causes.<sup>7</sup> The environmentalists have been joined by many of the beleaguered electric utilities who obviously fear the loss of their best customers to unregulated generators.<sup>8</sup> The utilities also tremble at the stranding of huge investments which they have made to serve customers who may unceremoniously "dump" them for more distant, but ostensibly cheaper, sources. Additional opponents of retail wheeling can be found among the representatives of the captive classes (like the residential) whose rates arguably have been subsidized over the years. The captives are also aghast at the prospect of having to fill the revenue gap left by the departing industrial opportunists. David Owens of the Edison Electric Institute has laid it flatly on the line: "The only result of retail wheeling is lower costs for larger customers and higher costs for smaller ones."<sup>9</sup>

## II. THE COMPETITIVE VISION

Quite apart from the usual confrontation between the presumed winners and the anticipated losers under a retail wheeling scheme, the underlying theme of the debate over this "revolutionary" approach is between those who seem to believe that low cost on a relatively short-term basis is the be-all and end-all of the business, and that competition, however achieved, is always the best, if not the only, means of getting at economic efficiency and low cost.

These proposals for retail wheeling of electricity are perhaps the most sensational development yet in the on-rushing movement toward deregulation and competition which has dominated almost all "respectable" economic thinking in recent years. The momentum achieved by the "competition first, last and at any price" school of thought has derived from several sources. One obvious source was the successful effort to end

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6. For a description of retail wheeling as working a revolution in the electricity industry, see Bernard S. Black & Richard J. Pierce, Jr., *The Choice Between Markets and Central Planning in Regulating the U.S. Electricity Industry*, 93 COLUM. L. REV. 1339 (1993).

7. The energy program director of the Natural Resources Defense Council, for example, recently advanced these arguments in a New York Times opinion/editorial. See Ralph Cavanagh, *Electricity Shopping Can Be a Bad Deal*, N.Y. TIMES, June 12, 1994, § 3, at 11.

8. See Michael Parrish, *Deregulation Plan Attacked From All Sides*, L.A. TIMES, June 8, 1994, at D1 (reporting that Southern California Edison Co. is siding with the National Resources Defense Council on the state's retail wheeling debate).

9. Mark T. Hoske, *Winners Will Be Small Utilities, IPPs In New World of Transmission Access*, ELEC. LIGHT & POWER, Apr. 1994, at 9.

the telephone equipment monopoly,<sup>10</sup> and more importantly, the long-distance monopoly<sup>11</sup> of the American Telephone & Telegraph Company.

With that monstrous dragon slain, everything seemed achievable to the votaries of competition. Now, rarely a day goes by that some new release from regulatory captivity is not announced.<sup>12</sup> A major development, of course, was the deregulation of the airlines and the complete commitment to competition as the only governing economic force in this infrastructure industry.<sup>13</sup> Another influential development contributing to the apparent triumph of the laissez-faire and deregulatory model has been the collapse of the Soviet Union. We have hopefully watched its attempts and the attempts of its former components and satellites to create market economies by total immersion in the cold waters of competition, bereft of subsidies and other governmental balm.<sup>14</sup>

It always has been recognized in the formerly "regulated" industries that competition was a strong force for efficiency and a value to be cherished by the consumer. Over the years, the courts have chided the regulatory agencies continuously to take into account competitive considerations in their weighing of the "public interest."<sup>15</sup> But only recently has competition been raised to the level of a uniquely crucial value to which all lesser values must yield. Obviously in complete harmony with this attitude is the view that practically any governmental intrusion into private economic affairs is an evil and a burden, which cannot help but decrease competitiveness and hence injure the consumer. The consumer who once saw pure-hearted bureaucrats as the main line of defense against corporate greed has now learned on the knee of the neo-classical economists that bureaucracy is pure burden and it is competition that will magically disperse all poten-

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10. *Carterfone v. American Tel. & Tel. Co.*, 13 F.C.C.2d 420, *recon. denied*, 14 F.C.C.2d 571 (1968).

11. *In re Microwave Communications, Inc.*, 18 F.C.C.2d 953 (1969), *recon. denied*, 21 F.C.C.2d 190 (1970) (approving by a 4-3 vote MCI's application for a point-to-point private line microwave service); *In re MCI Telecommunications Corp.*, 60 F.C.C.2d 25 (1975), *rev'd*, MCI Telecommunications Corp. v. FCC, 561 F.2d 365 (D.C. Cir. 1977) (reversing FCC's refusal to permit MCI to offer switched-access long-distance service), *cert. denied*, 434 U.S. 1040 (1978) (*Execunet I*).

12. MICHAEL K. KELLOGG ET AL., *FEDERAL TELECOMMUNICATIONS LAW* (1992) (containing a detailed description of the deregulatory movement in the telecommunications industry, along with an overview of the related legal issues raised).

13. For a description of airline deregulation offered by a leading participant, whose achievements have taken him to the U.S. Supreme Court, see STEPHEN G. BREYER, *REGULATION AND ITS REFORM* chs. 11, 16 (1982). Certainly, deregulatory efforts for natural gas should be studied.

14. One of the most fascinating aspects of the retail wheeling discussion has been the proud boast or humble concession (depending on the commentator) that retail wheeling is historically inevitable. In this connection, a sort of Marxist determinism in reverse has taken over. The participants in the wheeling debate, who really do not seem to agree whether retail wheeling is part of a great vision or of a great nightmare, persist in asserting that whatever its merits, it is clearly a passenger on the locomotive of history and isn't likely to be dragged off at the next station. Even the environmentalists, who typically see themselves as the vanguard of change, are made to seem a bit reactionary in clinging to the ancient electric order.

15. See, e.g., *Schurz Communications, Inc. v. FCC*, 982 F.2d 1043 (7th Cir. 1992).

tial exploiters.<sup>16</sup> However, in retail wheeling, the ultimate may have been reached. Now, an infrastructure industry, which until recently was viewed as the very paradigm of a natural monopoly, is a turbulent melee of profit maximizers.

### III. AN INFRASTRUCTURE INDUSTRY

There are certain things of a fundamental nature that the classic market model may overlook in coming to grips either with retail wheeling *per se*, or with its implications for the regulatory big picture. First of all, electric power is an infrastructure industry. This means that it is a major element in the "underlying foundation or basic framework"<sup>17</sup> of the economy and our very culture. The difference between an electrified economy and a non-electrified economy is profound—think of a gas or candle-lighting operating room versus a non-airconditioned Houston.

The foundational nature of the electric power industry is important because the more a technology like electricity goes to the roots of the economy, the more it spawns "externalities"—social benefits and social costs which do not figure in conventional economic analyses of the system employing the technology.<sup>18</sup>

Negative environmental externalities, though highly important and best known, are not the only externalities associated with electricity. There are also external benefits<sup>19</sup> which are all too easily forgotten by those who enjoy them, and are often interwoven with negative externalities in surprising and unpredictable ways. These benefits have been proclaimed by authorities as disparate as Vladimir Lenin and Samuel Insull. Lenin in a famous dictum once said, "Communism is the Soviet power plus electrification of the whole country, for without electrification progress in industry is

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16. Elsewhere I have opined on the pendulum-like oscillation in history between regulation and competition as the favored devices for controlling the economic process. See Richard D. Cudahy, *Regulation/Competition: The Swing of the Pendulum*, FORT., Apr. 1, 1991, at 21.

17. WEBSTER'S THIRD NEW INTERNATIONAL DICTIONARY OF THE ENGLISH LANGUAGE (UNABRIDGED) 1171 (1976).

18. The leading article in the legal literature on this now-familiar concept is Ronald Coase, *The Problem of Social Cost*, 3 J. L. & ECON. 1 (1960). Note that benefits as well as burdens are among the unaccounted for impacts of the electrical system. We are all currently acquainted with the environmental burdens imposed by electric power. Because of the environmental impacts, ones that the existing regulatory regime often endeavors to "internalize," environmental groups generally oppose the disintegrating effects of retail wheeling. Environmental control of the system through the existing electric monopolies and their government regulators will be lost.

19. Electrical power is, of course, not unique in the sense that there are external benefits to its consumption. When a homeowner paints her house, for instance, the aesthetic appeal enjoyed by her neighbors is an "external benefit." The greater an activity's external benefits, the stronger the argument for government involvement. A good example is high school education. If families were forced to pay the actual cost of putting a child through high school, it is likely that many families would choose not to conduct the transaction. However, because the social benefits of an educated population are so great, a centralized state bureaucracy metes out schooling to all takers (in fact, typically compels its "purchase").

impossible.”<sup>20</sup> In Germany, supporters of the newly-formed and fragile Weimar Republic believed that formation and nationalization of an all-German electrical network, or grid, could contribute greatly to saving the republic.<sup>21</sup>

Lewis Mumford, a philosopher of technologies, characterized the ages of history in accordance with the prevailing energy and material technology of the times.<sup>22</sup> Mumford thought that electric power, the principal generator of change in what he called the “neo-technic” period, would make possible the elimination of many of the evils of the coal and steam-driven “paleotechnic” era. He noted that hydroelectric power could transform isolated mountain areas suited only for forestry into industrial areas carefully planned to avoid the congestion and ugliness of “paleotechnic” industrial centers.<sup>23</sup>

The general point that emerges is that when we are talking about electricity we are referring to a truly infrastructure system—almost as basic as the water supply and far removed from the ubiquitous convenience enterprises of the modern world—here today and gone tomorrow. We have in mind a service which is fundamental almost to the culture itself and carries within it great potential for significant change as well as, like the air we breathe, an essential role in simply maintaining the status quo. These social impacts—good and bad alike—are externalities. They are external to the market as conventionally conceived and to the conventional transactions which characterize the day-to-day distribution of electricity.

Perhaps this is too obvious to need reciting. But, what would have happened with respect to the electrification of the American countryside if the whole matter had been entirely left to classical market economics? It was government subsidies that brought power to the farms of America and brought electric service to many areas where it might not even now be found had the whole matter been left to the market.<sup>24</sup> Would this have happened if someone possessing the authority of government had not made the decision to extend the network at a loss in the belief that the

20. THOMAS P. HUGHES, *AMERICAN GENESIS: A CENTURY OF INVENTION AND TECHNOLOGICAL ENTHUSIASM* 299 (1989).

21. *Id.* at 284-94.

22. *See id.* at 300, 355-60.

23. It apparently did not occur to Mumford, however, that in addition to the external benefits associated with electrification of mountain areas like the Pacific Northwest would come another externality—a severe threat to the salmon fishery in that part of the country.

The often unconscious interrelation of favorable and unfavorable externalities is also manifest in the proposal of the once Governor of Pennsylvania, Gifford Pinchot, a patron saint of environmentalism. In 1925, he proposed for his state the “Giant Power” plan that specified huge, 300,000 kilowatt minemouth power plants in the coal regions of western Pennsylvania, and transmission lines of 100,000 volts or more to carry the power as far as the heavily populated industrialized area of eastern Pennsylvania, which were two hundred miles distant. *See HUGHES, supra* note 20, at 303. While Pinchot likely hoped to take advantage of some of the “external benefits” that accompanied electrification, the negative externalities of so colossal a project are to the modern ear patent even without the now-required Environmental Impact Statement.

24. Though now, presumably, the loads that have developed in the rural areas once connected to an electrical supply provide a profitable basis for commercial relations on a conventional basis.

surrounding benefits (as yet unbooked) would more than offset the costs immediately reflected in the books of account?

A similar process unfolded in the Pacific Northwest where the great hydroelectric dams captured the energy for which there were probably few customers at the time. But the supply perhaps created the demand—once the rivers were harnessed there was power both for irrigated agriculture and for electric-intensive industries, like aluminum ingot production, that moved in to broaden the industrial base. At the same time, we now know that the size and multiplicity of these dams on the Columbia River has severely impacted the salmon population to the detriment of the ecology, as well as the commercial salmon fishing industry.

Such environmental costs have not been discussed in detail because they are so well known and so often emphasized today. For example, it is well known that production of electricity spews out waste heat, frequently generates sulfur dioxide (and thus acid rain), forms carbon dioxide and fosters the "greenhouse effect," is sometimes a source of undisposable radioactive waste, and is otherwise a major despoiler of the environment.

All of these are only some of the benefits and costs of electricity that do not enter into the conventional computation of least cost and greatest benefit. These are benefits and costs that are generally not recognized in the books of account or in the marketplace, which as a systemic matter, seems to focus on the short-term at the expense of the long-term. The existence and fundamental importance of all these externalities suggests that everything ought not be left to the invisible hand.<sup>25</sup>

Quite to the contrary, it is the potential for good as well as for evil of such a basic infrastructure enterprise as that of electric power which makes it a fit subject of planning and of affirmative regulation to give practical effect to farsighted planning. According to the conventional wisdom, governmental planning and oversight have proven to be worthless in telecommunications, in the airlines, and certainly, in the economic wasteland of the former Soviet Union. But planning under government oversight has characterized many of the infrastructure enterprises of our country during a good part of their modern history, and that is not an inglorious history. Can planners be wrong? Of course. Can regulators be ignorant, timid, political, or even venal? Unfortunately, yes. Can markets, reflecting the mass behavior of rapacious humanity, be imperfect and manipulated, blind to crucial long-term considerations, moved by pervasive delusions or powered by crowd hysteria? History would suggest all of the above.<sup>26</sup> Thus,

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25. The service of these long-term interests, what James Madison referred to as the "permanent and aggregate interests of the community," was thought—at least at the time of the framing of the Constitution—to be the "principal task of modern legislation." See *THE FEDERALIST* No. 10, at 78-79 (James Madison) (Clinton Rossiter ed., 1961).

26. Efficient Capital Market Hypothesis and other classical economists have a difficult time explaining phenomena like "tulipmania," Amsterdam's 17th century frenzy of trading in tulip bulbs. See CHARLES MACKAY, *EXTRAORDINARY POPULAR DELUSIONS AND THE MADNESS OF CROWDS* 1-97 (1980). Also, the 18th century's Mississippi and South Sea Bubbles present similar puzzles. *But see* ROBERT FLOOD & PETER GARBER, *SPECULATIVE BUBBLES, SPECULATIVE ATTACKS AND POLICY SWITCHING* (1994) (endeavoring to "rationalize" these seemingly irrational market behaviors).

there is no panacea in total reliance on an inherently imperfect market to the exclusion of imperfect, but essential, regulatory institutions.

#### IV. SOME QUESTIONS: SERVICE OBLIGATION, NATURAL MONOPOLY, AND SUBSIDIZATION

Before exploring alternative perspectives from which to approach electric power regulation, there are a number of important questions for the retail wheeling proponents. One of these relates to the obligation to serve and to the related question of territorial responsibility. One of the merits of territorial electrical franchises has been their function of defining who is responsible in a particular place for the adequacy, reliability and quality of the electric supply. In other words, what number do you call when the lights go out?

But what about the much more general problem of the obligation to serve? This has been analyzed rather ably and comprehensively elsewhere.<sup>27</sup> But there are those who are commenting blithely that, of course, the local electric utility will have to be the provider of last resort and retain an obligation to serve not only the captive customers, but also the "Prodigal Industrials" when they return home. However, the basic problem may be that there is a clash of cultures. In mature public utilities, publicly or privately-owned, there is a culture of commitment to service—almost military (as opposed to commercial) in nature—which transcends considerations of short-term or even long-term profit. If such a commitment is missing, there is certainly no place for the utility. Its franchise is in urgent need of revocation. But, despite current prejudices to the contrary, there is or has been a tradition of persons engaged in public service to keep the lights on, come what may.

Nevertheless, it is uncertain whether this kind of attitude can be maintained in the case of a utility whose best customers have been "cherry-picked" by upstarts, leaving the less desirable customers for the utility. The game seems to be that if the customer is hopelessly captive or there is not something better out there reachable on the transmission network, then, and only then, does the local utility suddenly acquire an obligation to serve. Somehow, we may have a contradiction in cultures here—the culture of the fast-moving and entrepreneurial unregulated source, and the culture of the regulated, but financially strapped, local provider.

There has been an effort to bridge the gap between the entrepreneurial ethic and the public utility ethic simply by asserting that if there is a workably competitive market in electricity, there need be no obligation to serve. The market in its infinite wisdom will supply power where power is needed and at a price reflecting cost. Who can ask for more? But this "solution" may be contradicted from experience in a whole variety of businesses where there has always been obvious reluctance to do business in high-cost, low-revenue areas. This phenomenon may be perfectly

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27. See Joe D. Pace, *Wheeling and the Obligation to Serve*, 8 ENERGY L.J. 265 (1987) (wholesale and limited retail wheeling).

acceptable when the infrastructure is not at stake. But in infrastructure industries, there must generally be universal service—as the telephone business has always recognized.<sup>28</sup>

Where do these considerations leave us with respect to the prospects for retail wheeling or, alternatively, for public regulation of the electric supply? They seem to leave the debate where it started: between those who are willing, even anxious, to take considerable risks in their quest for market solutions and those who see no reason to take risks merely to serve a theory. The first group is persuaded that competition can best guide any economic process and that the hand of government is at the throat of progress. This group will opt for retail wheeling without second thoughts, despite the numerous practical difficulties which lie in the way of its implementation. But to be of this view, one must be a certain kind of economic determinist. One must believe that the market makes all decisions and determines all outcomes. No puny efforts can divert it, and “practical difficulties” will not stand long in its way. However, there are indeed difficulties.

For example, some authorities maintain that the electric power industry retains enough natural monopoly characteristics to make it uneconomic to disaggregate the industry in the interest of competition.<sup>29</sup> These authorities rely primarily on economies of scope and the coordination afforded by vertical integration.

There is no way to know if they are correct, but simply as an economic matter, disintegration is bound to introduce costs as well as provide benefits. Who is to maintain reserves for the low-cost power obtained at distant points, and what is the cost of maintenance of reserves and how should it be compensated? Vertically integrated utilities have had a great deal of experience in planning for a variety of system contingencies. This may mean drawing on spinning reserves, starting up idle plants, buying power from a neighbor or wheeling it from a distant source, or shedding load when necessary, all to be accomplished in the most reliable and economic way. Is it really possible to provide the same reliability and economy in circumstances where customers are moving about at their own whim in search of the low-cost supplier? The answer no doubt, will be that universal banality—we can do it with computers.<sup>30</sup>

Moving from difficulties in operations to problems with prices, one is likely to encounter talk of cross-subsidies. However, traditional tendencies toward modest interclass subsidization, theoretically doomed by retail wheeling, have not been wholly misguided because we start from the premise that regulated electric rates have been far more cost-based than those in telecommunications, railroads, or other comparable industries. For exam-

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28. See generally KELLOGG ET AL., *supra* note 12.

29. See Douglas Gegax & Kenneth Nowotny, *Competition and the Electric Utility Industry: An Evaluation*, 10 YALE J. ON REG. 63 (1993).

30. Many of the claims now made for computers were first made for electricity in its early days. See HUGHES, *supra* note 20, at 443-72.

ple, at least until recently, cross-subsidization in telecommunications was the royal road to universal service—a preeminent national goal.

In the same spirit, whatever tilt in rates to favor residential consumers existed in electricity has been a gentle bow toward social harmony with no significant burden on efficiency. Whatever the facts, the captive home or apartment dweller never believed he or she was favored over industry and, as an inelastic user, he or she very well might not have been. In addition, residential ratepayers have nowhere else to send the bill, while industry can look to its own customers—at least if it is not the victim of a discrimination far more egregious than is likely to be the case. The whole issue of cross-subsidies in electricity is overblown, especially when raised under the improbable banner of meeting international competition.<sup>31</sup>

Not mentioned is the question of costing and pricing of transmission service as a problem in retail wheeling. Of course, this is a matter which is crucial to identifying the lowest cost source. These costing and pricing questions are matters that have been with us for a long time and they are to some degree indeterminate. The contract path approach, as opposed to that of loop flows ordained by Kirchoff's Law and other physical principles, is a perennial dilemma.

#### V. "AFFECTED WITH THE PUBLIC INTEREST"

In the gentlest way, I suggest that lawyers who are acquainted with some of the seminal decisions of the Supreme Court on the regulation of industry ought to be reasserting themselves at this time. They should not leave matters entirely in the hands of neo-classical economists. *Munn v. Illinois (Munn)*,<sup>32</sup> which involved price regulation of grain warehouses, brought into our jurisprudence the concept of the business "affected with a public interest."<sup>33</sup> *Munn* recognized categories of industries corresponding roughly to today's infrastructure industries, that were so basic to the functioning of the economy and of such fundamental importance that public regulation was admissible and in some respects essential.

*Munn* was an antecedent to the famously discredited case of *Lochner v. New York (Lochner)*.<sup>34</sup> Cases like *Allgeyer v. Louisiana*<sup>35</sup> and *Lochner* established the constitutional primacy of private property, rendering suspect governmental regulatory efforts that "interfered" with private ordering. The gist of these cases, decided under the rubric of the Fourteenth Amendment's "substantive due process" provision, was a deep skepticism

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31. It does seem that in this, as in many other areas like wages, international competition is proffered as a reason for redistributing income upward so that those with the most resources are the biggest beneficiaries. Although arguments to this effect are being made with increasing stridency, the social fabric may not remain intact if they are pushed too far.

32. 94 U.S. 113 (1877).

33. This is derived from Sir Mathew Hale's *DE PORTIBUS MARIS*. See FRANCIS HARGRAVE, *LAW TRACTS* (1787).

34. 198 U.S. 45 (1905). For a description of *Lochner's* vice, see Cass R. Sunstein, *Lochner's Legacy*, 87 *COLUM. L. REV.* 873 (1987).

35. 165 U.S. 578 (1897).

of governmentally established regulatory mechanisms that interfered with the then-predominant laissez-faire model. During the *Lochner* era (from around the turn of the century until the New Deal), such regulations were typically struck down as violations of "fundamental" property rights. The Supreme Court thus invalidated state attempts to regulate railroad rates,<sup>36</sup> the insurance industry,<sup>37</sup> minimum wages and maximum hours in bakeries,<sup>38</sup> and entry into particular lines of business.<sup>39</sup>

But *Munn* carved out an exception for the business "affected with a public interest." Under that concept, private property may assume a quasi-public aspect, justifying the interference with private property that regulation brings.<sup>40</sup> While the New Deal spelled the end of *Lochner* and its judicially-enforced aversion to government efforts in the regulation of economic affairs, the classical model that now plays so preeminent a role in economic thinking might be thought of as representing—from the vantage point of government regulation—a modern-day *Lochner*, a deep suspicion of regulatory efforts. The triumph of neo-classical economic thought has brought us—as a practical matter—a return of *Lochner*. Government regulation and centralized planning face similar disfavor, though now more as a matter of political exigency than judicial fiat.<sup>41</sup> But against this background we might consider whether the "modern" rule of unfettered competition should be subject to *Munn*'s "public interest" exception.

Over the years, the idea of businesses affected with a public interest became linked with the concept of monopoly.<sup>42</sup> To the extent this linkage assumed importance under economic theory, direct regulation began to be thought necessary only to discipline monopolies.<sup>43</sup> If, by some restructuring, monopoly status could be changed and market power reduced (its total

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36. *Chicago, Minneapolis & St. Paul Ry. v. Minnesota*, 134 U.S. 418 (1890) (also called the Minnesota Rate Case).

37. *Allgeyer*, 165 U.S. 578.

38. *Lochner*, 198 U.S. 45.

39. See *New State Ice Co. v. Liebmann*, 285 U.S. 262 (1932) (ice manufacturing); *Louis K. Liggett Co. v. Baldridge*, 278 U.S. 105 (1928) (pharmacies).

40. See also *German Alliance Ins. Co. v. Lewis*, 233 U.S. 389 (1914) (allowing regulation of fire insurance prices under *Munn*'s "affected with the public interest" rationale); *Block v. Hirsh*, 256 U.S. 135 (1921) (same for rental housing). Cf. *Williams v. Standard Oil Co.*, 279 U.S. 235 (1929) (rejecting the application of *Munn* to gasoline prices); *Ribnik v. McBride*, 277 U.S. 350 (1928) (employment agencies); *Tyson & Brother v. Banton*, 273 U.S. 418 (1927) (theater tickets). For a more general discussion of *Munn* and the "affected with a public interest" rationale, see Walton H. Hamilton, *Affectionation With Public Interest*, 39 YALE L.J. 1089 (1930); Breck P. McAllister, *Lord Hale and Business Affected With a Public Interest*, 43 HARV. L. REV. 759 (1930).

41. It is therefore perhaps not surprising that the few voices calling for a return to *Lochner*-style judicial enforcement of private property rights tend to come from the neo-classical, Chicago-school libertarian camp. See BERNARD SIEGAN, *ECONOMIC LIBERTIES AND THE CONSTITUTION* (1980); RICHARD EPSTEIN, *TAKINGS: PRIVATE PROPERTY AND THE POWER OF EMINENT DOMAIN* (1985).

42. See McAllister, *supra* note 40, at 768-69.

43. This, at least, is the justification for the regulation of public utilities in two leading economics textbooks. See PAUL A. SAMUELSON & WILLIAM D. NORDHAUS, *ECONOMICS* 523-27 (12th ed. 1985); RICHARD G. LIPSEY ET AL., *ECONOMICS* 295-99 (8th ed. 1987). See also BREYER, *supra* note 13, at 15 (stating "The most traditional and persistent rationale for government regulation of a firm's prices and profits is the existence of a 'natural monopoly'").

elimination is a chimera pursued by antitrust enthusiasts), then public regulation might be jettisoned and the disciplinary task left exclusively to competition. However, *Munn* and its progeny essentially justify regulation on the basis of the nature of the activity and not exclusively upon its monopoly characteristics. This view is insufficiently considered today.<sup>44</sup> There can be regulation of the electric power industry not simply because it is a natural monopoly (although there are some authorities who continue to believe that it is just that),<sup>45</sup> but essentially because it is a foundational industry, furnishing the nerves and sinew of the body politic.

On this basis, there are some fundamental questions about current trends in deregulation such as the apparent lack of concern about price discrimination. The traditional focus of regulatory attention has been the need for price uniformity.<sup>46</sup> In the case of electric power, a level-playing field has meant in most cases class rates based on cost.

The concerns about price discrimination and class rates arose in the early efforts to regulate the railroads. The fledgling Interstate Commerce Commission was faced with a railroad practice of giving lower rates or rebates to certain large shippers having strong economic leverage. A famous example was the ostensibly favorable rate treatment given the Rockefeller oil interests, enabling them to defeat and subsequently acquire small competitors in an attempt to gain a monopoly.<sup>47</sup>

The avoidance of discrimination through enforcement of filed class rates has been a foundation stone of conventional regulation. There have always been economic arguments to justify special rates for large customers based on scale economies, but distinguishing between economic leverage and scale economies is difficult, and regulators and courts have been rigid. They have favored the establishment of filed class rates and insisted upon their application to all members of the class.<sup>48</sup> Perhaps, this rigidity would meet with the disapproval of many economists. But it stood for a kind of level-playing field principle with a tendency to look with suspicion on what were proffered as special situations.

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44. Cf. JAMES C. BONBRIGHT, *PRINCIPLES OF PUBLIC UTILITY RATES* 31 (1961). In his book, Mr. Bonbright states:

In the current publications on rate theory by academic economists, the most frequent use made of this self-imposed restriction to 'economic' principles is to absolve the economist from any professional concern for considerations of *fairness* or *equity* as between investors and consumers, or as among different classes of consumers. Instead, the merits of alternative rules of rate making are to be judged solely by reference to their functional efficiency in getting the work of the world accomplished—in attracting capital to public utility enterprises, in supplying incentives to high-grade management, in controlling the demand for the service, etc.

*Id.* (emphasis in original).

45. See Gegax & Nowotny, *supra* note 29.

46. See *New York v. United States*, 331 U.S. 284, 296 (1947) (stating "The principal evil at which the Interstate Commerce Act was aimed was discrimination in its various manifestations"); BONBRIGHT, *supra* note 44, at 369-85.

47. See HERBERT HOVENKAMP, *ENTERPRISE AND AMERICAN LAW, 1836-1937*, 150-51 (1991).

48. As an example of a crude anti-discrimination regime subject to much professional economic criticism, see the Robinson-Patman Price Discrimination Act, 15 U.S.C. §§ 13-13c, 21a (1988).

On the other hand, a system such as that represented by retail wheeling gains its very existence and its economic justification from the practice of discrimination. No longer will electric customers be drawing as a class from a common pool of electricity. They will now, in accounting theory if not in engineering fact, be drawing according to their own choice from widely disparate sources and establishing rates by agreement. Whether these rates reflect purely economic characteristics or result from some sort of economic leverage will be difficult to determine. For better or for worse, the simple level-playing field of the past will be lost in the welter of price deals which are central to the proposed system.

## VI. CONCLUSION

Assuming that the stumbling blocks can be removed, are we going on to the promised brave new world, where the invisible hand will make a distant memory of service territories and the obligation to serve? The competition of one electric generator against another for the custom of a particularly desirable customer ought to make everyone uncomfortable enough to become more efficient. But will this efficiency be gained at the expense of economies of scale that may have been lost, or at the cost of a firmly identified and reliable obligation to serve? The overwhelming majority view seems to be that competition and more competition—whether good or bad—is at any rate inescapable and possibly wonderful as well.

The only recourse of doubters at times like this may be legal precedents. And there, against the dominance of unregulated competition, is the historic commitment to regulation of businesses affected with a public interest—whether the businesses are monopolies or not. This historic approach obviously rests on a belief that there really is a “public interest.” Those with an extreme deregulatory mind-set tend to condemn the idea of a public interest to some sort of bureaucratic underworld. They tend to regard what is urged to be the public interest as merely the private interest of the electric monopolies thinly veiled by a bureaucratic cover.

Some economists may be presently leading us down the path of competition without limit and at all costs with an ever-diminishing respect for public regulation. However, a bit of skepticism is in order. There is a great deal of wisdom in *Munn* and the great Supreme Court cases that both preceded and followed it. In *Munn* the Court said, among other things, “Common carriers exercise a sort of public office, and have duties to perform in which the public is interested. Their business is therefore ‘affected with a public interest’ within the meaning of the doctrine which Lord Hale has so forcibly stated.”<sup>49</sup> This dictum may be applied to electric providers, as they are now or may become in the future, as easily to common carriers.

A provider of complex and deep-rooted infrastructure cannot help becoming a quasi-public institution. It must in large part be guided by public objectives and act in the public interest, or, in the language of our forefathers, provide for “the public convenience and necessity.” So long as

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49. *Munn v. Illinois*, 94 U.S. 113, 130 (1877) (citation omitted).

these fundamentals remain in place, we can usefully consider retail wheeling or any other technical scheme. It is important that we re-examine the rules and the structure of public regulation from time to time to keep them current with new developments and changing technology, but this does not mean that we can do without them. Thus, contrary to much of the commentary, retail wheeling does not seem to be a “revolution” or even a “vision.” It should not try to overthrow public regulation and substitute the invisible hand of a certain-to-be-imperfect competition. Electricity has been a considerable contribution to the public good. Its history should be understood, consulted, and respected in addressing current problems.

