

## 70<sup>TH</sup> ANNIVERSARY CELEBRATION OF THE FEDERAL POWER ACT

*Remarks by the Hon. Richard D. Cudahy\**

I really appreciate the invitation to be with you today to help celebrate the birthday of a legislative landmark not properly appreciated even by those who have learned to cherish it section by section. The Federal Power Act is 70 years old today, and I have been asked to make these comments today because I am even older than the Act and, of course, recall its birth vividly. I was then nine years of age, and, like most other nine-year-olds of the time, was deeply troubled by the continuing blot of the Attleboro Gap on the legal landscape. For those of you who may be so benighted as not to recognize it, the Attleboro Gap is not a New Hampshire ski resort. It is a constitutional free fire zone for electric power generated in one state and sold in another. Filling it was an urgent priority for me as I celebrated my ninth birthday.

Of course, there were a few other problems at the time. Twenty-five per cent of the population had been put out of work, oil was for sale at ten cents a barrel, most of the railroads were in bankruptcy, the only place any spare cash, if you had any, was safe, was in a mattress, but the big problem on President Roosevelt's mind was the continuing disgrace of the Attleboro Gap.

I didn't realize then what a huge problem it was for a struggling national economy that an electric company that sold its output across a state line to another electric company couldn't be required to raise its rates. This was the sort of thing John Maynard Keynes so deeply deplored in his classic work, "General Theory of Employment, Interest and Money." Keynes and his many disciples thought the way to jump-start the faltering U.S. economy was somehow to bring closure to the Attleboro Gap. And that's why filling in that Gap was tried as a desperation measure immediately after the Supreme Court outlawed the Blue Eagle of the NRA.

Well, that's one way of looking at it, but in a slightly more serious vein, beside closing the Attleboro Gap and providing federal regulation of interstate sale of electricity at wholesale, the Federal Power Act (let's call it the FPA) started out as part of a package. It was introduced in Congress as part of what was named the Public Utility Act. The other part of that Act was the Public Utility Holding Company Act, which, of course, administered the death sentence to the life work of Samuel Insull, Harrison Williams and others. As most of you know, the Insull Empire crashed in 1932, and its counterparts, the holding companies, collapsed in varying degrees about the same time. A good part of all the New Deal regulatory legislation—the Securities Act of 1933, the Securities Exchange Act of 1934, our birthday boy, the Federal Power Act, of course, the Public Utility Holding Company Act (we'll call it PUHCA for short), the Rural Electrification Act, and the TVA Act and related public power legislation—all owed their origins in some measure to the holding company collapse and the related problems of the electric power industry.

Even before the downfall of the holding companies, in the Great Depression, the electric power industry had acquired several black eyes that in

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the end made it a prime target for more regulation and gave impetus to the growth of its public sector. In the election of 1926, Samuel Insull had backed the candidacy of Frank Smith in the Republican primary for Senator from Illinois and contributed a six-figure sum to that end. The incidental fact that Smith was the Chairman of the Illinois Commerce Commission, regulating Insull's home town utility, was, despite disclaimers and other plausible explanations, the source of a not surprising uproar. The whole episode and subsequent investigation of corrupt campaign practices led to the refusal of the Senate to seat Smith after he won the general election.

A little later the controversy over the future of the federal development at Mussell Shoals on the Tennessee River led to a strident debate between conservatives in the Senate and the public power wing led by George Norris of Nebraska. The Federal Trade Commission was instructed to investigate the gas and electric industries and the need for new legislation. Franklin D. Roosevelt, who, as Governor of New York, had espoused public power, campaigned for President in 1932 with denunciations of Insull and the "power trust."

One of the aspects of holding company operations, lending new anguish to the Attleboro Gap, was the inability of anyone to regulate interstate holding companies. State regulators tried and failed and, of course, there was no federal regulation until the Federal Power Act. So it made perfectly good sense for the FPA to be paired with PUHCA as parts of the Public Utility Act. Both these pieces of legislation had emerged from studies by the Federal Trade Commission, later by the Federal Power Commission, and finally by President Roosevelt's own National Power Policy Committee. PUHCA, of course, was focused on the holding company problem specifically, and led pretty much to the demise of companies holding electric utilities in more than one state unless the operating utilities could be integrated—that is, operated as a single unit. I don't want to try to elaborate on the repercussions of this approach except to say that it is more or less the opposite of what would be approved in today's competitive climate. Now, without considerations of PUHCA, there is no objection to ownership of multiple operating companies unless the result is too much concentration in a single market. The Holding Company Act, on the other hand, seeks and rewards concentration and, specifically, integration.

In that regard, I notice that we are not having a celebration of the birthday of the Holding Company Act. PUHCA has, for better or for worse, become the black sheep of New Deal regulatory legislation. I don't think it deserves all the hostility that's been visited on it. After all, it succeeded in reorganizing the electric utility industry in this country into handy-sized state-bounded companies with local managements that were always willing to help with the community fund drive—and isn't that what electric companies are for? Beside that, PUHCA is a survivor. They've been trying to drive a stake through its heart for the last fifteen years and it's still alive and kicking. So, maybe we ought to save at least a candle on the birthday cake for PUHCA.

In any event, the FPA did a few other things than close the Attleboro Gap. For example, it gave the Federal Power Commission authority to order interconnection between jurisdictional utilities and to decide whether wholesale power rates met the magical standard of being just and reasonable. The Commission had jurisdiction over mergers and security issues and authority to establish the legitimate cost of utility property and to investigate the electric industry and to establish joint boards with state commissions. Not included in

the bill, as enacted into law, was Commission power to order wheeling (or transmission service) although this was a continuing issue for many years thereafter. The legislation also carefully preserved state jurisdiction over retail electric rates and facilities.

Interconnection is a subject particularly dear to my heart, since my last struggle prior to reaching the federal bench was to try to establish interconnection between the companies in Louisiana and Oklahoma owned by Central and South West Corporation (known as CSW), and the companies in that magically non-jurisdictional enclave in Texas, called ERCOT. CSW got into this controversy because its state of integration under PUHCA had been challenged. We at CSW fired the first shot of what became the Texas Range War by sending power in the wee hours of the morning from a substation located in ERCOT to light the lights in Altus, Oklahoma. This interconnection presumably involved all of Texas in interstate electric transmission and, under the controlling decisions of the Supreme Court, under the FPA, brought all of ERCOT under federal jurisdiction. The big Texas utilities, when informed of what had happened, didn't argue the point, but instead broke all the connections between themselves and the power systems that had been infected by interstate electricity. Meanwhile, we—claiming the infection had rendered all of ERCOT jurisdictional—filed a petition in the FPC asking the Commission to investigate and order more extensive interconnection between Texas and the outside world. Based on an obscure order involving some Colorado company, the Commission turned us down, with some particularly unkind words in a concurrence by Commissioner James Watt. We, of course, soldiered on and successfully sought amendments in 1978 to the FPA, which would have authorized mandatory interconnections even to ERCOT. The key amendment became sections 110 and 112 of the Act, which were subject to the famous and unfathomable condition that an ordered interconnection could not result in a “reasonably ascertainable uncompensated economic loss for any electric utility.” This amazing condition, and others like it, are the sort of thing that results from the horse-trading process that produces new legislation. As far as CSW was concerned, we welcomed the new legislation granting the expanded Commission jurisdiction regardless of the adjective attaching to it. And the broadened jurisdiction was enough to win a settlement of the interconnection dispute long after I had departed the world of holding companies for the federal bench. For some reason, either of charity or inadvertence, nobody from Texas appeared to object to my confirmation.

Another feature of the FPA that merits comment is the famous provision that electric rates be “just and reasonable.” This language, enthusiastically adopted by the courts, has been construed to mean that there is a range of reasonableness, not merely a single point to satisfy the requirement. Also, market-based rates, resulting from the process of free competition where there is no exercise of market power, are, by reason of the process, just and reasonable. This proposition equates what is efficient—the outcome of free competition—with what is equitable, just and reasonable. Under ordinary circumstances this equation does not seem outrageous, or even questionable. But it is likely always to come under severe stress in circumstances of scarcity where rates go through the roof. Electricity cannot be stored and its therefore price-sensitive to small changes in supply and demand. It is very doubtful that the typical user of electricity is going to agree what widely fluctuating rates are just and reasonable when they are moving against him or her. For that reason, of course, upper

limits, or caps, are placed on rates so that the theoretically appropriate results of market processes do not put theory to the ultimate test of consumer acceptance.

This problem also raises the very pertinent question whether any revision of the FPA now or in the future should retain the just and reasonable standard for application to market-based rates. In that respect, Texas once again joins the analysis. For Texas has adopted a new utility restructuring law for application to the wholesale and retail market presided over by the Texas Commission—and this is the only state commission that has wholesale jurisdiction. So far as I can tell, the new law does not contain the words, “just and reasonable” but instead defines the process under which a competitive process will discipline rates. I would question a similar approach at the national level. As I have indicated, competition leads to efficiency but “just and reasonable” measures equity. If the courts see fit to find an equation between them, so be it, but I don’t think that equation is appropriate for legislative determination, and equity ought to be the ultimate standard. Out of mercy for my listeners today, I won’t delve into the Roman and the medieval standards of justice to justify that conclusion.

The importance of the FPA has been enhanced by the development of competitive markets in electricity and the perceived need for regional transmission organizations, standard market designs, and the like. In the American scheme of things, regional organization can only be regulated at the federal level. Although the states will continue to play a part, the role of federal regulation is necessarily advanced by a system of regional markets—and I say that as one who once played a part in state regulation.

Besides that, the FPA awards power over transmission to the federal commission without any limitation. As the availability and adequacy of transmission become increasingly important in a market scheme of things, the responsibility of federal regulators and federal law are correspondingly enhanced. So I guess my enthusiasm at age nine for the Federal Power Act will be replicated and enhanced at this point as the FPA and I approach the age of eighty. I’m nine years closer than the FPA.

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