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The Government Structure Over the U.S. Electric Industry: Federal–State Tensions

James E. Hickey, Jr.

There are about 3,500 separate electric systems in the United States that are owned by various government entities, by consumers (nonprofit cooperatives), and by shareholders (private companies). Most of the electricity in the U.S.A. is provided by private companies. The private electric companies are about 250 in number and they supply about 80% of the electricity in the United States. The private companies are tax-paying corporations that are financed by the sale of stocks and bonds and by the sale of electricity for profit. Most electric systems in the U.S.A. are connected to one another and there are connections with Canada and Mexico. Overall, the U.S. electric system provides a fairly reliable electric supply at a relatively reasonable price.

The government structure over the U.S. electric industry presently is divided between the federal government and the governments of the states. The tension created by this divided government structure has resulted in failures in the U.S. electric industry. Those failures include wasteful and expensive litigation over who has jurisdiction, the cancellation of needed power plants, unnecessarily high electric prices to consumers, a reduction of energy supply options, and harm to international relations. This paper briefly analyzes some of those failures in the U.S. system of dual government authority over electric markets. The paper suggests that other countries like the sovereign states of the former U.S.S.R. may provide, in certain respects, a viable alternative model for future government regulation of the electric industry than the U.S. structure.

GOVERNMENT REGULATION OF PRIVATE ELECTRIC COMPANIES

The present dual system of federal and state regulation of electricity in the

U.S.A. is somewhat an accident of history.

The electric industry in the U.S. began on September 4, 1882, when Thomas Edison, the inventor of the lightbulb, started the first private electric company for making electricity in New York City. At this time there was no government regulation. As electric use grew, electricity became an essential public service that was needed to operate factories and businesses and to provide light and heat for homes and offices. Because electricity became an essential public service, it began to be regulated by the states in order to assure reliable supply at a reasonable price.

State regulation of private electric companies was not based on competition. Rather, states granted companies exclusive rights to make and sell electricity in assigned geographic areas within the states. The states also set the price at which electricity could be sold at retail to consumers. For the most part, private electric companies welcomed state regulation because it prevented competition, wasteful duplication of facilities, and city governments from taking over profitable electric operations. The federal government began to regulate electricity transmitted across state borders and sales of electricity at wholesale in the 1930s. Thus, state authority over electric prices at present is confined to retail electric sales within a state (intrastate) and federal authority over electric prices is confined to interstate wholesale sales and interstate transmissions of electricity.

FAILURES IN THE FEDERAL-STATE REGULATORY STRUCTURE IN THE U.S.A.

The End of the U.S. Nuclear Power Industry

The end of the U.S. nuclear power industry is due, in large part, to conflicts between state and federal authorities over the construction and operation of nuclear power plants.

Commercial nuclear electric power development in the U.S.A. began in the 1950's. That development came within exclusive federal authority under laws passed by the Congress and signed by the president. The premises for exclusive federal government regulation were concerns about national security and health and safety. At that time, electricity made with nuclear power was thought by everyone to be the answer to unlimited electric supply to be sold at a very low price.

In the 1970s and 1980s, citizens in the states became very concerned about the safety of nuclear power plants and about the serious problem of where to dispose of nuclear power waste.

State and local governments, in response to those concerns expressed by

their citizens, began to strongly oppose the building of nuclear power plants in their communities. The federal government, however, continued to encourage construction of new nuclear power plants as it was required to do by federal law. Each government entity attempted to assert jurisdiction. The result was tension and conflict between state and federal government entities that caused long and costly delays in issuing construction permits to build nuclear power plants and licenses to operate them. Resolution of the federalism tensions involved many lawsuits and administrative proceedings which, over time, made electricity generated by new nuclear power plants very expensive when compared to electricity made from power plants using coal, natural gas, and oil.

As a result, the commercial nuclear power industry is dead in the U.S.A. The nuclear electric plants that were built in the 1950s and 1960s are reaching the end of their productive lives. All nuclear power plants that were ordered since 1974 have been canceled (sometimes at the loss of billions of dollars of investment). No new nuclear power plants have been ordered since 1978 and there are no new orders coming in the future. This is an extraordinary situation for the U.S.A. because it comes at a time of great concern about global warming and acid rain caused by power plants fueled by oil and coal. It also comes at a time when the U.S.A. depends heavily on foreign petroleum, much of which is used in oil-fired and natural gas-fired electric power plants. This harms the U.S. trade balance, increases its national debt, and weakens its economy.

Federal-State Tensions Over Electric Prices

A long-standing tension exists between the exclusive power of states to regulate retail electric prices (the prices paid by consumers like factories and homeowners) and the exclusive power of the federal government to regulate interstate wholesale prices of electricity (like power sales between two utilities that sell electricity at retail). The tension comes when the federal government sets a wholesale price that the state authorities refuse to pass through to customers at retail. The federal government complains that the state by its refusal is preventing the wholesale price from having any effect and that the state is, in effect, requiring electric companies to swallow internally wholesale price increases granted by the federal government. The state government complains that if the state is required to pass along wholesale prices set by the federal government without question, then the federal government is wrongly interfering with the state's exclusive authority to set retail electric prices. This split in pricing authority is subject to constant, expensive litigation, which increases the price of electricity paid by everyone.

The Absence of a National Energy Supply Policy

In the U.S.A., the government does not directly regulate the private companies that supply the traditional fuels of oil, natural gas, and coal to electric companies. This means that those companies compete with one another for utility customers. As a result, coal companies oppose government policies favorable to the oil and natural gas industries and vice versa. And all three industries oppose government policies favorable to alternative, nontraditional sources of energy like solar power, geothermal power, or the making of fuel from corn (gasohol). This means that the U.S.A. has no coordinated national energy supply policy. The marketplace, with its wild swings in price, is primarily left to control supply and demand. At times, just as now, the U.S.A. is heavily dependent on foreign oil supply while, at the same time, it has enough domestic coal and natural gas reserves to meet all its electric fuel supply needs for the next 200 years (putting aside environmental concerns).

The Harm to International Relations

Federalism experts like Daniel Elazar have spoken about a "new species" of federalism. Perhaps one such "new species" of federalism may emerge in the form of central international authorities to address unique international electric production, supply, and sales problems among similarly situated states.

The reason that the United States and its neighbors (Mexico and Canada) may require such a "new federal" or "supernational" authority can be shown by the recent tension between the Province of Quebec and the State of New York. The tension is about using Quebec hydroelectricity to meet the energy needs of the population of Long Island, New York (6 million people). Long Islanders are at the limits of local electric supply because the Long Island communities and the State of New York successfully opposed federal government approval of a large nuclear power plant (800 megawatts) that was constructed on Long Island but has never opened (the Shoreham nuclear power plant). Long Island taxpayers have agreed to pay \$5.5 billion in increased electric prices to tear down the plant as soon as possible or to convert it to burn natural gas.

Long Island has turned to Quebec (among other places and sources) to replace part of the electric power of that closed nuclear power plant. The Province of Quebec is building a huge hydroelectric project (the James Bay Project) that, if completed, will produce excess electricity that it wants to sell to Long Island. The problem is that New York State suddenly has decided not to contract with Quebec for that power. The reason for this decision is in part because the predictions about how much electricity New York will need in the future has changed and because New York objects to the environmental consequences in Canada that will be caused by the large-scale flooding that will

take place to build the hydroelectric dams necessary to supply Long Island with power. New York State also objects, on human rights grounds, to the displacement of the Canadian Indian population (the Cree) when their land in Quebec is flooded by these hydroelectric dams.

As a result of New York's decision, the economy of Quebec is in serious danger. The Quebec government borrowed large sums of money from financial institutions, using as collateral the expectation of future electric sales by the province to Long Island. Quebec understandably objects that New York is controlling Canadian energy policy and the internal economy of Quebec on grounds that are totally a matter of Canadian sovereign authority. That is, Quebec says New York has no right to question the means of production of electricity inside Canada. New York may insist that it cannot contract for electricity made in Canada in a way that would violate New York law and international human rights law if that electricity were made in the same way in New York. This controversy has contributed to the tensions in international relations with Canada and may have profound implications for future relations of the U.S.A. with Mexico as well.

It is in this last example especially that the U.S.A. may have much to learn from government structures already in place to deal with electricity in the sovereign states of the former U.S.S.R. One solution that the U.S.A. appears likely to pursue to resolve these federalism tensions is to deregulate utilities at the federal level and to introduce competition among utilities at the state level. These trends, if pursued, do not resolve problems raised by integrating electric markets in Canada, Mexico, and the U.S.A. In the former U.S.S.R., all electricity assets presently are owned by the government and there are no immediate plans to privatize electric operations. In addition, electric coordination and supply among the new states continues to be handled, for the most part, in the same way it was handled in the U.S.S.R. This post-U.S.S.R. government structure, for the present, avoids the wasteful litigation, construction delays due to conflict, and the incoherent energy policy that exists in the U.S.A. In this area, it may well be the case that the West should learn from the sovereign states of the U.S.S.R. and that the states of the former U.S.S.R. should not rush to adopt federalism trends being pursued in the U.S.A. At a time when Mexico, the U.S.A., and Canada are searching for the appropriate structures to address the energy aspects of free trade and integration of markets, the states of the former U.S.S.R. already have such a structure to address the energy aspects of future economic relations. Such structures may prove useful in assuming economic and political sovereign equality in energy and electricity matters in the decades ahead.