Testimony of

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on

The Adequacy of State and Federal Regulation of Electric Utility Holding Company Structures

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Table of Contents

I. Cross Subsidies in Context: Effective Corporate Structure Regulation Should Encourage Transactions that Serve the Public Interest and Discourage Inefficient Ones that Do Not 2

II. The Repeal of PUHCA 1935 Created Gaps in Corporate Structure Regulation 4

A. PUHCA 1935 created accountability to investors, consumers and the public through four types of regulation. 4

1. Mergers and acquisitions 5
2. Mixing of utility and non-utility businesses 5
3. Issuances of debt or equity 6
4. Interaffiliate transactions 7

B. The repeal of PUHCA 1935 eliminated key accountability measures, increasing the likelihood of corporate complexity and abuse of interaffiliate relations. 7

III. To Ensure Public Accountability in Corporate Structure Transactions, We Must (a) Identify and Promote Sensible Corporate Structures, and (b) Apply Cost-Benefit Standards 9

A. What types of corporate structures promote the public interest? 9

1. Utility acquisitions of more utility businesses 11
2. Mixing of utility and nonutility businesses 12
3. Interaffiliate transactions 13
4. Issuance of debt or equity 14

B. In assessing corporate couplings, how do we ensure that benefits justify the costs? 15

IV. Regulatory Preparedness for New Structural Transactions Requires Multidisciplinary Expertise and a Shared Multijurisdictional Purpose 17

A. Multidisciplinary analysis calls for a new array of regulatory resources and skills 17

B. Multiple regulators of the corporate structure market need a shared purpose 19

V. Conclusion: The Repeal of PUHCA 1935 Does Not Relieve Regulators of Their Duty to Advance the Public Interest Through Corporate Structure Regulation 20

Mr. Chairman and Members of the Committee:

My name is Scott Hempling. I am the Executive Director of the National Regulatory Research Institute (NRRI). NRRI is an independent, Section 501(c)(3) corporation, funded largely by voluntary state commission payments. Its mission is to carry out the research activities that enable utility regulators to make public interest decisions of the highest possible quality. My testimony today reflects my own views, and not those of NRRI, any state commission or any past client of mine or of NRRI.

As an attorney in private practice, I advised public and private sector clients involved in regulated industries, particularly state regulatory commissions and organizations of consumers or consumer representatives. I have represented clients in many cases under the Public Utility Holding Company Act of 1935 (PUHCA), before the Securities and Exchange Commission (SEC) and the U.S. Court of Appeals. I have testified before this and other Congressional committees many times on PUHCA and other electric industry matters.

The stated purpose of this hearing is to "examine the adequacy of state and federal regulatory structures for governing electric utility holding company structures in light of the repeal of the Public Utility Holding Company Act" of 1935, and in particular to discuss the concerns raised by the report of the United States Government Accountability Office (GAO), *Recent Changes in the Law Call for Improved Vigilance by FERC*, GAO 08-289 (February 2008). These "recent changes" are the 2005 repeal of the Public Utility Holding Company Act of 1935, and the new FERC authorities established by the Public Utility Holding Company Act of 2005. The GAO report has produced some useful dialogue between FERC and the GAO on

FERC's regulatory policies. My testimony seeks to extend this dialogue so that we address the gamut of regulatory issues raised by the Committee and by the 2005 amendments.

My testimony has five parts.

Part I places the current debate between FERC and GAO in the larger context of corporate structure regulation. Effective corporate structure regulation should encourage transactions that serve the public interest and discourage ones that do not.

Part II explains that the 2005 repeal of the Public Utility Holding Company Act of 1935 created gaps in corporate structure regulation.

Part III argues that to restore public accountability in corporate structure transactions we must (a) identify and promote sensible corporate structures and (b) apply cost-benefit standards.

Part IV explains that regulatory preparedness for the new structural transactions made possible by the repeal of PUHCA 1935 requires multidisciplinary expertise and a shared multijurisdictional purpose.

Part V, the conclusion, argues for alertness on the part of all regulators.

I. Cross Subsidies in Context: Effective Corporate Structure Regulation Should Encourage Transactions that Serve the Public Interest and Discourage Inefficient Ones that Do Not

Over a century, our citizens have paid trillions of dollars to support the infrastructure of our nation's electric and gas industries. Corporate structure regulation seeks to make the recipients of those trillions—owners, financiers and operators of that infrastructure—accountable to the public. To that end, legislators and regulators have asked five questions:

1. Who can acquire and own electric and gas utilities?
2. What business activities may exist within the utility's corporate family?
3. What corporate structures may these corporate families have?
4. What financial structures may these corporate families have?
5. What interactions may occur among the members of the corporate family?

These five questions share a common purpose: to encourage transactions in the public interest, and discourage transactions that are not.

The detailed dialogue between the General Accounting Office and the Federal Energy Regulatory Commission on cross subsidies addresses one subset of these questions: Do FERC's practices and policies prevent infrastructure owners from forcing ratepayers to bear, through excessive electricity and gas rates, the cost of business activities unrelated to the provision of essential electric and gas service?

The five major questions make clear that cross subsidy regulation is only one part of a corporate structure accountability mechanism. The GAO-FERC debate is part of a larger conversation: What is our vision for corporate structure? Does anyone have one? If so, is that vision consistent across states, and between states and FERC? If there is such a vision, do the regulators work consistently toward that goal? If there is no such vision, is there a process for creating one?

When Congress in 2005 repealed the Public Utility Holding Company Act of 1935, it left these questions unanswered. The result is multiple gaps in corporate structure regulation, in our ability to screen inefficient from efficient transactions, and in the accountability of infrastructure owners to consumers, investors and the public. Ensuring accountability requires that regulators identify and promote sensible corporate structures that satisfy rigorous cost-benefit standards. To prepare for this task—to put standards in place before receiving proposals for the many structural transactions made possible by the 2005 repeal—requires new multidisciplinary expertise and a common purpose shared by the multiple regulatory jurisdictions.

II. The Repeal of PUHCA 1935 Created Gaps in Corporate Structure Regulation

A. PUHCA 1935 created accountability to investors, consumers and the public through four types of regulation.

For 70 years, the federal Public Utility Holding Company Act of 1935 ("PUHCA 1935") defined and limited the structural options for electric utilities.[1] PUHCA 1935's central policy goal was utility accountability -- to customers, investors, regulators and legislators. Its central technique was corporate simplification -- the alignment of corporate form with public service obligation.

The alignment mechanism was the "integrated public-utility system": each utility holding company had to limit its assets and activities to those necessary to provide electric or gas service to the public. PUHCA 1935 applied this principle by running corporate structure proposals through a series of tests, restrictions and reviews in four major areas: mergers and acquisitions, mixing of utility and non-utility businesses, issuances of debt or equity, and

[1] I use the term "PUHCA 1935" to distinguish that statute from the Public Utility Holding Company Act of 2005, which includes the language repealing the PUHCA 1935, plus some provisions relating to regulators' access to books and records, and procedures for allocating certain costs among holding company affiliates. PUHCA 1935 was codified at 15 U.S.C. sec. 79 et seq. Practitioners customarily referred to PUHCA 1935 provisions by section number rather than by U.S. Code cite; therefore Section 1 of PUHCA is 15 U.S.C. sec. 79a, Section 2 is 15 U.S.C. sec. 79b, etc.

interaffiliate transactions. An understanding of these tests assists the analysis of how deeply the regulatory infrastructure has changed.

1. Mergers and acquisitions

Under Section 10 of PUHCA 1935, the acquisition of a public utility, through the holding company form, had to satisfy six tests. Specifically, the acquisition:

1. Must not "tend towards interlocking relations or the concentration of control of public-utility companies, of a kind or to an extent detrimental to the public interest or the interest of investors, or consumers," Section 10(b)(1);
2. Must bear a "fair relation to the sums invested in or the earning capacity of" the property acquired, Section 10(b)(2);
3. Must not "unduly complicate the capital structure of the holding company system," Section 10(b)(3);
4. Must not be "detrimental to the public interest or the interest of investors or consumers or the proper functioning of" the holding company system, Section 10(b)(3);
5. Must not be "detrimental to the carrying out of the provisions of" Section 11 (relating to simplification of holding company systems, Section 10(c)(1); and
6. Must "serve the public interest by tending towards the economical and efficient development of an integrated public-utility system," Section 10(c)(2).

2. Mixing of utility and non-utility businesses

For "registered" holding companies (usually the multi-state systems), the Act limited operations to "a single integrated public-utility system." The only exception was for "such other businesses [i.e., other than the business of a public-utility company] as are reasonably incidental, or economically necessary or appropriate to the operations of such integrated public-utility system...." Section 11(b)(1). Example: If a utility owned coal burning plants, its holding company could own a coal mine to service those plants; but it could not own hotels and restaurants to house and feed coal miners.

For all "exempt" holding companies (usually the intrastate systems), the Act allowed ownership of nonutility businesses, but only to the extent not "detrimental to the public interest, or the interest of investors or consumers." Section 3(a).

3. Issuances of debt or equity

For the registered holding companies, Section 7(d)(1) prohibited an issuance of securities if the issuance triggered one or more of six negative findings:

1. "The security is not reasonably adapted to the security structure of the declarant and other companies in the same holding-company system";
2. "The security is not reasonably adapted to the earning power of the declarant";
3. "Financing by the issue and sale of the particular security is not necessary or appropriate to the economical and efficient operation of a business in which the applicant lawfully is engaged or has an interest";
4. "The fees, commissions, or other remuneration, to whomsoever paid, directly or indirectly, in connection with the issue, sale, or distribution of the security are not reasonable";
5. "In the case of a security that is a guaranty of, or assumption of liability on, a security of another company, the circumstances are such as to constitute the

making of such guaranty or the assumption of such liability an improper risk for the declarant"; or

6. "The terms and conditions of the issue or sale of the security are detrimental to the public interest or the interest of investors or consumers."

4. Interaffiliate transactions

Sections 12 and 13 of PUHCA 1935 applied to registered holding companies a set of prohibitions and conditions relating to interaffiliate transactions in two major categories: financial transactions (e.g., loans, guarantees of indebtedness, extension of collateral), and sales of goods and services (other than electricity or gas).

Prohibited transactions included any loaning of money, or guaranteeing of indebtedness, by a utility subsidiary in favor of its holding company or any affiliate. See Section 12(a). Other interaffiliate transactions had to heed SEC rules, which generally required interaffiliate pricing to be "at cost," to prevent utility subsidiaries from being forced to subsidize nonutility businesses. See, e.g., Section 13(d).

B. The repeal of PUHCA 1935 eliminated key accountability measures, increasing the likelihood of corporate complexity and abuse of interaffiliate relations.

By eliminating the 1935 Act's restrictions and reviews, the 2005 statute increased the likelihood of structural complexity, including self-dealing between regulated and unregulated holding company affiliates. Gone are the geographic and type-of-business limits on utility mergers and acquisitions, along with reviews of and limits on leveraged financing and interaffiliate transactions.

These changes make utility regulation more challenging. Because PUHCA 1935 induced conservatism in corporate restructuring, states and FERC had less need to create their own policies. Of the dozens of mergers between 1985 and 2005, most involved the joining of adjacent utilities. In these cases, the main challenges were to test the claims of cost savings from the combination (claims based on the assumption that the combination would produce greater economies of scale and scope); then allocate the risks, costs and benefits associated with those claims among customer groups and investors. Additional challenges included identifying and protecting against horizontal and vertical market power; and ensuring that the larger, post-merger entity devoted sufficient attention to local quality of service. These mergers, for the most part, did not involve the joining of remote electric facilities, or the mixing of utility and nonutility businesses, or leveraged private equity financing that increased debt while decreasing public information.

By removing limits on geographical, type-of business or financial arrangements, the repeal of PUHCA 1935 changed the market for corporate restructuring. Regulators at state commissions and at FERC thus face questions they had not had to address, systematically at least, for 70 years: Should they impose limits on the types of companies and corporate structures that provide retail monopoly service to electricity and gas customers? Or should they welcome new structural options without limit? With respect to these questions, there is no expert consensus, no political consensus, and no systematic process for arriving at one.

III. To Ensure Public Accountability in Corporate Structure Transactions, We Must (a) Identify and Promote Sensible Corporate Structures and (b) Apply Cost-Benefit Standards

A. What types of corporate structures promote the public interest?

In repealing PUHCA 1935, the 2005 Congress expressed no particular vision for corporate structures. There are no federal statutory limits on geographic remoteness, the mixing of utility and nonutility business, leveraging, private buyouts, interaffiliate transactions. Anyone can try anything.

Regulators thus face corporate structure transactions not permitted, or not permitted without review, for 70 years. This circumstance requires us to revisit regulatory policy on corporate structures. The purpose of such revisiting is not to replicate every aspect of the prior federal regime, but to inquire systematically into the nature of the new transactions and to determine the appropriate regulatory response, if any.

The table on the following page, "Corporate Restructuring by Public Utilities: How Should Regulators Prepare and Respond?," displays the necessary analysis. Listed on the left are corporate structure events which attempt to describe all major types of transactions: 7 categories and 21 subcategories. Listed across the top are the 3 categories of regulatory options—prohibition; permission without review; and permission subject to reviews, limits and conditions. By completing this table, the regulator determines, systematically, the types of companies and corporate structures permitted to provide utility service. For each of these 63 cells, PUHCA 1935 gave an answer. With PUHCA 1935's detail eliminated, the answers now must come from state law, and state and federal regulatory discretion.

This Part III of my testimony introduces the type of analysis applicable to four of these subjects: expansion of utility business, mixing of utility and nonutility businesses, interaffiliate transactions and issuance of debt or equity. First, the regulator must define the types of transactions that trigger regulatory concern. Then the regulator must determine the response: prohibition, permission without review, or permission subject to standards and review. The concepts below are examples for consideration. Some overlap. There is no intent that all should

Corporate Restructuring by Public Utilities: How Should Regulators Prepare and Respond?

	Regulatory Action		
Corporate Event	Prohibition?	Reviews, Limits and Conditions?	Permission w/o Review?
1. Utility merger with another utility			
a. operationally integrated			
b. not operationally integrated			
2. Utility acquisition of nonutility			
a. for utility purpose			
b. not for utility purpose			
3. Nonutility acquisition of utility			
a. acquirer has operational relationship to utility			
b. acquirer has no operational relationship to utility			
4. Interaffiliate transactions			
a. goods and services: sale to utility			
b. goods and services: sale by utility to nonutility			
c. financing: loan or guarantee to utility			
d. financing: loan or guarantee from utility to nonutility			
e. sale or lease of utility assets			
5. Issuance of debt or equity			
a. at the holding company level, for utility purposes			
b. at the holding company level, for nonutility purposes			
c. at the utility level, for utility purposes			
d. at the utility level, for nonutility purposes			
e. at the nonutility level, for utility purposes			
f. at the nonutility level, for nonutility purposes			
6. Divestiture or spin-off			
a. of utility assets serving your state			
b. of utility assets serving other states			
c. of nonutility assets or businesses			
7. Use of utility assets for non-utility business			
a. utility assets in your state			
b. utility assets in other states			

be promulgated. Rather, regulators and legislators should consider the full array and select those that suit their preferences.

Caution: Advocates of regulatory forbearance may misinterpret this table as a recommendation for regulatory conditions in every cell. The table does not prescribe a result; rather, it ensures alertness—to those corporate structure actions that warrant regulatory attention, and to the types of regulatory intervention (including no intervention). The purpose is to alert regulators to a statutory fact: the 1935 Act addressed every cell, in some way; the 2005 Act addresses only some.

1. Utility acquisitions of more utility businesses

The regulatory concern here relates to diseconomies of scale, management distraction and business risk: Will a utility become part of a system so large that quality and efficiency of local service will suffer, or local concerns be ignored, in setting terms and conditions of service? These transactions warrant attention whether structured as an acquisition, pooling of interests, transfer of assets or other form of restructuring; or whether the certificate to serve is transferred or remains in the original hands.

As with all the subject areas discussed here, the options for regulatory action on utility requests for permission to acquire other utility businesses include prohibitions, permission without review, and permissions subject to conditions and reviews. In cases where the statute or regulator does not prohibit the acquisition, regulators should submit it to ***economic tests***, such as requirements of new efficiencies, non-recovery of any acquisition premium except to the extent the premium is matched by demonstrated cost reductions, and limits on the utility debt used for the acquisition. There also are ***structural conditions,*** such as placing the in-state utility business in a corporation separate from nonutility business, requiring that the utility maintain its own bond ratings, and requiring that the in-state utility obtain, file, maintain and update annually a third party's nonconsolidation opinion, i.e., an opinion that regulatory provisions are sufficient to prevent utility from being forced into bankruptcy should the holding company or other affiliate fail. ***Operational conditions*** include requirements that the merged entities be operationally integrated, commit to specified operational cost reductions (otherwise, there would not be cost justification for the merger), use best practices in all areas, satisfy quality of service standards, and bring no new cost or risk unless exceeded by measurable benefits.

A risk associated with any of these conditions is that they may not provide a level of protections comparable to what existed before the transaction.

2. Mixing of utility and nonutility businesses

The mixing of utility and nonutility business, including the control of a utility business by a nonutility owner, was long prohibited or discouraged by PUHCA 1935. The concerns here are management distractions, use of utility ratepayers to finance or guarantee debt associated with the nonutility business, and unearned competitive advantages for utilities entering nonutility markets.

Regulatory options, along with prohibition, and permission without review, include: (a) limits on the percentage of total holding company assets, revenues or net income that can be attributable to nonutility businesses; (b) limits on holding company or utility financing of any acquisition of nonutility businesses; (c) limits on the utility's ability to file for bankruptcy based on affiliate difficulties; and (d) forms of separation between utility and nonutility businesses, such as separate affiliates, accounting, financing and financial statements.

3. Interaffiliate transactions

Affiliate transactions fall into four major categories: sales of utility services, sales of nonutility goods and services, sales of utility assets, and financial transactions (e.g., loans and guarantees of indebtedness). Affiliate transactions move in both directions: to and from the utility, from and to the holding company or other affiliates. There are multiple risks. "Cross subsidy" is a term frequently used in this context but infrequently defined. Where the corporate family has both utility and nonutility businesses, a cross subsidy occurs when a utility ratepayer bears costs caused by nonutility activities; i.e., when the ratepayer pays a price for utility service higher than she would have paid in the absence of the nonutility activities. When a utility holding company buys a hotel and shifts acquisition costs to the ratepayers, a cross subsidy occurs. When a utility enters a risky nonutility business, and the utility covers the higher cost of capital through utility rates, a cross subsidy occurs.

Cross subsidies are only part of the adverse effects of inappropriate interaffiliate relations. When utility customers have historically borne the economic cost of an asset, they should receive the full market value associated with that asset's use by others. But a common practice is for the nonutility affiliate to obtain rights to the asset at cost rather than at market value. The result is not a cross subsidy, technically, because the ratepayers' rates do not rise as a result of nonutility affiliate's use. But there is a mismatch of risk and reward. The utility ratepayers bear all the costs but receive only part of the benefits.

The regulatory options for addressing these challenges again range from prohibition to conditional permissions to unconditional permissions. Examples: (a) prohibition on a public utility providing to an affiliate any financial loan, guarantee or other benefit other than the normal payment of dividends; (b) requirement that any goods or services sold by a utility to an affiliate be priced at the higher of book or market; (c) requirement that any goods or services sold to a utility by an affiliate be priced at the lower of book or market; (d) advance review of dividend payments to protect financial integrity of the holding company system and the working capital of in-state utility affiliate; and (e) advance approval for interaffiliate cost allocation practices and contracts above a minimum dollar level.

4. Issuance of debt or equity

With the electric and gas industries now free of any federal prohibitions on the types of corporate acquisition, utilities, their holding companies or their affiliates may attempt securities transactions that could trigger regulatory concern over leveraging, and over acquisition prices in excess of underlying value (with the expectation that captive ratepayers will fund the excess). The types of transactions warranting attention include issuance of debt or equity, and guarantees or assumptions of liabilities, (a) at the holding company level, for utility or nonutility purposes; (b) at the utility level, for utility purposes or nonutility purposes; and (c) at the nonutility level, for utility purposes or nonutility purposes.

The regulatory options include, besides prohibiting, or permitting without review, these transactions, the following: (a) the terms and conditions of the security issuance must be consistent with the sound and economical financing of the public utility businesses, i.e., that there is neither excess nor insufficient debt, and that the debt be reasonably adapted to the security structure of the utility and all companies in the holding company system; (b) the fees associated with the securities issuance must be reasonable and there may be no conflicts of interest among the transacting parties and their advisers, and (c) debt incurred by or guaranteed by a public utility must be used for public utility purposes only.

B. In assessing corporate couplings, how do we ensure that benefits justify the costs?

After dozens of utility mergers, the fundamental economic analysis of whether a merger is, from the consumers' perspective "worth it," remains unsettled. This "merger equation" involves four main questions:

1. What should be the relationship of costs to benefits?
2. How should we measure costs?
3. How should we measure benefits?
4. If actual costs and benefits deviate from projections, who is accountable?

There is no commonly held answer to these questions. In many mergers, the questions never arise, let alone receive answers.

What should be the relationship of costs to benefits? **T**he most frequent answer is either (a) "benefits must not be less than costs" (sometimes called the "no harm" test), or (b) benefits must exceed cost, but not necessarily by much (sometimes called the "positive benefits" test). Another test, applied uniformly in prudence review, and in standard financial analysis, but rarely in merger review, is "Does the cost produce benefits at least equal to alternative, feasible uses of the money?" The roots of this third test are in the common sense view of economic efficiency, that the "public interest" is harmed when a merger consumes resources that would allow a lower-cost means of achieving benefits. In the regulatory community there has been no systematic examination of these alternative equations, or of the implications of allowing dozens of mergers to proceed without such examination.

How should we measure costs and benefits? Savings asserted by merger applicants have included: administrative/general savings, labor savings, fuel savings, O&M savings, savings from coordination efficiencies, savings from construction deferral and savings from bulk purchases and other economies of scale.

As with the benefit-cost relationship, there is no common regulatory treatment of costs. Some states require merger applicants to quantify savings with the degree of specificity required in a rate proceeding, or to accept rate reductions based on their assertions of savings. Sometimes, however, applicants' assertions of savings are so general that there is insufficient information on which to base a credible cost-benefit judgment. Regulators also differ over the period of time over which they must quantify savings. Nancy Brockway, NRRI's Director of Multi-Utility Research and Policy, points out that there is no industry standard for estimating likely merger synergies, and typically no track record of proven synergies from other mergers by which to assess forecast results from the proposal under review.

If actual costs and benefits deviate from projections, who is accountable? A continuing difficulty is determining whether an asserted merger benefit would have occurred without the merger. Otherwise merger cost recovery from ratepayers would negate cost reductions that would have occurred without the merger.

After-the-fact rate review is not enough. Some argue that protection against cross subsidies and other risks lies in ratemaking. The implication is that structural complexity poses no risk because ratemaking will catch problems. This view is not fact-based. Ratemaking depends on auditing. Auditing is not like a trip to the dentist, who checks every tooth. Auditing is sampling. It cannot promise 100% coverage -- especially with limited regulatory resources.

Allowing structures that invite cross subsidies or complicate auditing increases the probability of problems.

Reliance on after-the-fact disallowance also invites too-big-to-fail situations. In the competitive world, poor decisionmakers fail. But not always. We all are familiar with situations in which a company's size or national importance pressures regulators to prop them up. State commissions whose residents depend on the incumbent will tend to save the company rather than exact the ultimate penalty -- especially since bankruptcy law addresses creditor rights, not consumer protection. Given the inherent uncertainty of "back-end" accountability in the form of rate review, "front-end" accountability in the form of advance review of financial risks becomes even more critical.

IV. Regulatory Preparedness for New Structural Transactions Requires Multidisciplinary Expertise and a Shared Multijurisdictional Purpose

A. Multidisciplinary analysis calls for a new array of regulatory resources and skills

The GAO study cited state commission concerns about availability of resources to deal with cross subsidies. That concern applies as well to the larger set of questions throughout this testimony. Analysis of corporate structure events requires expertise and resources in the area of economics, engineering, finance and accounting, and business management. In this subpart I give examples of the types of question demanding new skills and resources.

1. Economics: What are the economies and diseconomies of scale for the various components of utility service -- production, transmission, distribution, customer relations? What are the economies and diseconomies of scope among various utility and nonutility activities potentially coexisting within the same corporate family? How can regulators gather this information in the context of reviewing merger and acquisition proposals?

2. Engineering: For each of the major physical functions involved in utility service, what are the geographic and size limits beyond which reliability, quality and responsiveness of service are affected?

3. Finance and accounting: What are appropriate financial structures for the various businesses within a utility holding company structure? Do some structures pose the risk of corporate managers channeling utility cash flow to nonutility businesses, in amounts detrimental to the utility's optimal functioning? For example, can there be "safe harbors" for various types of nonutility investments by utility holding companies, such that should business failures occur, no damage to the utility will result? Are there true benefits to utility shareholders to having a utility holding company diversified into other business, as compared to the shareholders diversifying their portfolios individually?

In corporate acquisitions occurring within noncompetitive markets, there is a risk of financial circularity: the acquiring company pays a premium for a utility knowing that the premium can be recovered from monopoly ratepayers. (Competitive markets, in contrast, cap premium payments because the acquired entity cannot raise product prices above market prices.) Given the circularity risk, what methods exist for determining the appropriate size of acquisition premia? What regulatory policies best line up the acquirer's desire to pay a premium, the acquiree's insistence on a premium, and the ratepayer's legal right to protection from rate increases associated with the premium? (Such policies should encourage efficient mergers—meaning mergers that lower costs—and discourage inefficient mergers.)

4. Business management: What are implications for efficient and effective management when utility operations are geographically dispersed, i.e., not operationally integrated? How do managers, and regulators, determine these limits? What are the incentives, for various management positions, which result from a mix of utility and nonutility businesses in the same corporate family? Are these incentives aligned with the public interest? What are the skill sets necessary to manage, simultaneously and successfully, monopoly and competitive businesses within the same corporate family? After several dozen mergers and acquisitions in the electric and gas industries since 1985, what data are available to study these questions?

B. Multiple regulators of the corporate structure market need a shared purpose

While eliminating federal statutory restrictions, Congress left pre-existing state and FERC roles undiminished. The responsibility for making those judgments necessary to prevent adverse effects on consumers, markets (for power, gas and finance) and the general public thus shifts to the regulators, federal and state, who must try to use their existing jurisdictional tools to address the new challenges. This situation creates opportunities for regulatory experimentation and creativity, but it raises a fair question: Will the separate actions, or inactions, of multiple jurisdictions produce a rational regulatory policy on corporate restructuring in multistate markets?

I suggest that the current conversation on cross subsidies grow into a discussion of this larger question: Do we need consistent regulatory policies across jurisdictional lines to encourage utility corporate structures that serve the public interest, and discourage ones that do not? Can we achieve that consistency while still leaving flexibility for individual jurisdictions?

This question need not trigger a federal-state dispute over a jurisdictional zero-sum equation. There is opportunity for a jurisdictional policy that allows for federal and state roles, and for variation among the states on a number of issues. A rational policy would distinguish between (a) the need for an efficient multistate market for utility asset acquisitions, and (b) the need for responsible state-level regulation to ensure efficient and reliable local service. Without a concerted effort on the part of federal and state policy makers to address the whole set of issues raised by utility mergers and acquisitions, from cross-subsidies to federal/state jurisdiction, however, we will dilute out ability to address the gaps left by the repeal of PUHCA 1935. I hope this Commission, and the participants in today's testimonial panels, can address this question.

V. Conclusion: The Repeal of PUHCA 1935 Does Not Relieve Regulators of Their Duty to Advance the Public Interest Through Corporate Structure Regulation

This testimony has focused on alertness, in the form of four types of anticipatory actions: (a) identifying the types of utility corporate structure transactions that trigger regulatory concern; (b) establishing principles to guide market participants who fashion such transactions; (c) recognizing the multidisciplinary ingredients to effective regulatory review; and (d) revisiting the federal-state relationship to ensure consistency in vision and implementation. The present focus on cross subsidies is too narrow to accommodate these larger, more far reaching questions.

Some have argued that to articulate and encourage a vision for accountable corporate structures is to "reconstruct" PUHCA 1935, in violation of Congress's 2005 intent. This argument is deficient in logic, law and thoughtfulness. Section 203 of the Federal Power Act requires the Commission to judge mergers by a "public interest standards. The 2005 Congress did not dilute this language, but rather subjected more transactions to it. State merger statutes create similar duties.

It remains regulators' continuous obligation to align corporate structures with the public interest. With the repeal of PUHCA 1935, that obligation becomes more difficult to fulfill. The acquisition of remote utility properties, the mixing of utility and nonutility businesses, and the use of unconventional ownership structures and financing structures, all call for new resources and new expertise. The dialogue created here by GAO and FERC is a worthy beginning, but it is only a beginning.

Thank you for the opportunity to present this testimony. I look forward to any questions from the Committee.