

THE FRONT PAGE

News & Views You Can Use

Welcome to High-Cost Energy

by Timothy Capps

The Maryland Public Service Commission (PSC) was instituted in 1910 with the mission of regulating the electric utilities of the day as well as certain types of transportation systems. It has continued to function in that role for nearly a century, although its focus is now on state utility operations, transportation regulation having shifted over the years to other agencies at the state and federal levels.

During the nine-plus decades since the PSC was created, much has changed in the utility and energy world. Population growth has expanded the demand for electrical and gas services exponentially, and the shape of the industry that supplies power to residential and business consumers has changed dramatically. That industry is now dominated by very large companies that, until recently, enjoyed virtual monopoly status in return for operating in a regulated environment that effectively controlled their pricing policies while making certain that they faced minimal – if any – competition.

Bye-bye, 'Bad Hair Days'

Here in Maryland, as elsewhere in America, it was a neat *quid pro quo* that assured consumers of a ready supply of something essential to everyday living and the conduct of business: energy to keep the lights on, the air conditioning running, the heat pumping, the

water running. For better or worse, our society has become extremely energy dependent, with the basic necessities of life built around having a reliable flow of electricity in one's home, office, or other place of business or recreation. Sure, our great-great grandparents lived without electricity, or gas operated vehicles for that matter, but every day was a bad hair day for them and their neighbors.

The public utilities industry grew as the nation grew, building generating plants and the connective capacity to deliver electricity and/or natural gas into homes and businesses. This was typically done under the umbrella of a regulatory agency that oversaw rates, approved permits for new generating or distribution capacity, and determined rates of return for these monopolistic businesses so that they could earn a profit for their shareholders without unduly charging their customers for what was an increasingly necessary product.

Things of course got more complicated as America sprawled. There were increasing demands for utility services from remote rural areas to megalopolises and the country became more pollution conscious, which influenced the building of generating capacity and the types of fuels used to run those plants. We went through a nuclear phase in the 1950s and '60s, when the clean-burning aspects of nuclear power were paramount in deciding how to supply generation needs. Then came Three Mile Island, and suddenly, there was no more

appetite for permitting new nuclear facilities. In fact, two major East Coast utilities ended up in bankruptcy because of their inability to get approval to operate completed nuclear power plants (whose construction costs still had to be paid).

Then, with nuclear energy placed on a remote back burner and rising concerns over the pollution coming from coal-fired generating plants, came the enormous rise in oil-based petroleum products as major oil-producing nations in the Middle East and elsewhere starting controlling the output and pricing of crude oil. The era of cheap energy was over, noted by consumers in both the price of gasoline and their monthly utility bills. At the same time, demand for power has continued to rise

in both the United States and worldwide – especially in countries like India and China, whose

vast populations and economic evolutions into high volume industrial production has made them increasingly energy-intensive and dependent upon foreign produced oil.

All these factors meant that the day when economies could be built and sustained by seemingly limitless supplies of cheap, fossil-based fuels was a pleasant memory.

Enter 'De-Reg'

Deregulation of public service industries in the United States was arguably energized by the conclusion of the anti-trust

case that led to the break-up of American Telephone and Telegraph Corporation (AT&T). In that case, there was a shake-out period in which consumers got very confused by the competing claims of people who wanted

their long distance business and maybe their local business, then started offering cellular service, and now

internet connections and voice internet and interactive video, etc., etc.

It isn't clear whether we're paying more or less for phone service these days, but we certainly have far more communications options available than ever before and there has been a faster evolution in communications technology since the AT&T break-up than in all of human history.

Next came the deregulation of the cable television industry, with results that, thus far, have been almost the opposite of what occurred in the telecommunications business. The much-anticipated competition in the cable market has not really materialized, since the logical competitors for cable service – such as the telephone companies and internet service providers – have been slow to venture into that world. The cost of entry into that business is still steep and the technology is still evolving, so we are just now beginning to see major telecomm operators like Verizon and Cingular edging into cable competition against the Comcasts and Cox Communications of

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The era of cheap energy was over.

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the world. From the consumers' standpoint, deregulation of cable rates has only meant steadily increasing bills with no signs of improved service or more entertainment options to offset those higher charges.

In this atmosphere – with deregulation the “next new thing” – a number of utility operators began to think about the possibilities of a deregulated marketplace for suppliers of power services. Buffeted by what they regarded as an antiquated regulatory environment, not to mention environmental demands, unpredictable fuel supplies, and volatile demand cycles, many concluded that they would be better off crafting some form of deregulation that would allow them to compete in markets beyond their traditional service areas.

To accomplish this, they would need to convince regulators and, more importantly, elected officials, that deregulation would lead to greater com-

petition and therefore more options for customers and, theoretically, price flexibility. In various states, “de-reg” became the latest and greatest effort to shift a historically regulated industry into a market-driven mode. The utility providers were tired of being perceived as stodgy, conservatively run companies dependent upon the political whims of their jurisdictions for their sustenance. They wanted the opportunity to spread their wings and fly, to become growth stocks instead of “carriage trade” investments.

Seven-Year Sleep

“De-reg” came to Maryland in 1999, when, after a couple of years of considering how to craft a business and regulatory model that would work for both the utilities and consumers, the legislature passed a bill to deregulate the state’s utility services.

The legislation was certainly not universally popular, and it was widely recognized that Maryland was about to tread

uncharted waters. As a failsafe of sorts, the legislation, which was supported and heavily influenced by Baltimore Gas & Electric (BG & E), Potomac Electric Power Company (PEPCO), Allegheny Power, and other power

suppliers in the state, included a provision that kept rates capped until

July 1, 2006, at which time they would be allowed to “float” to market prices.

BG & E made the decision to split into a holding company, Constellation Energy, and an operating company or retailer, BG & E. Constellation would be the owner of the real estate assets of the company – specifically the generating plants and distribution network – while BG & E would maintain the sales and service structure. From the consumer standpoint, nothing seemed to have changed, and no one was talking about the looming deadline in the summer of ‘06. Meanwhile, across the country, one of the effects of deregulation was the steady increase in mergers (often complicated by the schizophrenic nature of the deregulatory process) of utility companies. For the first time since the Great Depression, utilities were casting their nets across state lines, much like banks have done since the ‘80s. In 2005, following the industry trend, Constellation Energy announced a merger with FPL, the holding company that owns Florida Power & Light.

That announcement caused some uneasiness among consumer advocates and eventually opened up the conversation about the looming rate increases, which suddenly seemed to emerge from nowhere in January of 2006. It was as if somebody had awakened from a seven-year sleep and said, “Gee, we better tell everybody what’s coming, then get out of Dodge ‘til the shooting stops.”

It was, in a sense, a perfect storm about to happen. PEPCO’s rate caps had been eliminated in

2004 and the consequent rate increases were not monumental. BG & E, however, would be a different story, in part because the price of their raw materials, oil in particular, had increased so significantly over the past year – especially after the hurricanes that hammered the Gulf Coast at the end of last summer and the ever-present crisis in the Middle East.

At that point, it became clearer to both PSC members and staff (as well as the utility companies) that rates would have to go up significantly in 2006 – 72% in the case of the typical BG & E customer. Then, BG & E announced the FPL merger and acknowledged that those extreme rate hikes were beyond the point of speculation; they were really going to happen. The merger wasn’t really tied to the new, market-based rate structure, but it was impossible to disassociate the two in the minds of shocked and angry consumers. It looked like capitalism run amok, even if logic said otherwise.

Rhetoric and Posturing

The legislature then jumped into the fray with all its collective feet, saying all the right things for consumer consumption and offering a potpourri of bills that ranged from efforts

to extend rate caps to halting the merger to eviscerating the PSC to finding a means to

dampen the rate increases.

The governor, while expressing concern about the degree of the rate increases and their impact on lower-income families, essentially supported the “de-reg” concept and said that there should never have been rate caps and that if the market had been allowed to work its magic, rates would have risen but in a much more palatable way. Legislators who had voted against “de-reg” in 1999 were saying, “I told you so,” and most Republican legislators were lying low because the ones who had been around in ‘99 had generally supported the idea.

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There was no practical way to put the ‘de-reg’ genie back in the bottle.

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The bottom line: There was plenty of rhetoric and finger pointing and posturing about consumer protection, but most legislators realized, as did the governor, that there was no practical way to put the “de-reg” genie back in the bottle.

However, it is an election year, and everybody needed a “de-reg” story to take back home. So legislation was passed to phase in the new rates and fire the PSC, with a new PSC to be appointed by the legislative leadership. The governor vetoed those bills and “de-reg” was left in limbo for a few weeks. A suit challenging the PSC’s rate decisions was filed in Baltimore City Circuit Court, and a judge ruled that the PSC needed to re-open its deliberations, a notion grudgingly accepted by the PSC with the sense that whatever revised rate plan it devised would not look much different from its old one.

This was followed by a special session of the legislature called by the president of the Senate and the speaker of the House. This resulted in the passage of an emergency bill that was almost identical to the bills passed in the regular session, combined in one 50-page legislative tome. If you really want to, you can go the Maryland General Assembly’s website and pull up Senate Bill 1, then read the entire thing, which gets pretty complicated very quickly unless you are familiar with existing utility industry statutory and regulatory law. In a nutshell, it did two things: It put into place a requirement to allow consumers options that would phase in the rate increases over 18 months (so-called rate stabilization); and it fired the PSC, replacing it with a legislatively appointed group.

The rate story is still confusing, but you shouldn’t be seeing those high double-digit increases at this point, unless you opt to pay them now instead of dribbling them out. Either way, you’ll pay for the full rate in-

crease within an 18-month period, and it is unlikely you will see those rates go down as long as our society is heavily dependent upon fossil fuel-based energy.

Political Power Grab

The PSC? Well, that’s another story.

Anticipating that the firing of the PSC would not be well received either by the PSC members or the Ehrlich administration, the legislature wrote into the new statute a provision that required any suit over the changes in the PSC appointments process to be filed in Baltimore City Circuit Court, presumably because that court would likely be more favorably disposed toward the legislative majority’s views of recent PSC behavior.

The expected suit was duly filed by PSC Chairman Ken Schisler, who was joined by most of his fellow commissioners, and is now in the hands of the circuit court, whose ruling could come at any time (although it might not occur until mid- or late fall). The basic argument is over whether or not the legislature exceeded its constitutional authority in firing gubernatorial appointees and setting up a procedure to wrest away from the governor all future appointments to the PSC.

Stripping away all the intellectual arguments, was this a power grab? Absolutely. Was it warranted? Depends on whose ox is being gored. Is it legal? It will probably be awhile before the courts reach a final conclusion on that (meaning when all appeals have been exhausted).

What does all this mean to you, the consumer?

Well, on the utility front, it means you need to get used to the idea of living in a quasi-de-regulated world.

Whatever the experience with utility deregulation in various states, the need to change the *status quo* in the world of power production was evident by the early ‘90s, so there was an inevitability to the process, if not the execution. Could things

have been done differently? Undoubtedly, especially in the area of public education and information.

What is clear at this point is that BG & E, PEPCO, Allegany Power and other Maryland utilities will be buying their power from a number of sources in the future, and will be much more subject to the whims of the marketplace than ever before. That means they will have to be more nimble than in the past, and one has to hope that the market for both energy raw materials and production and distribution capacity reaches a rational equilibrium level, an uncertain proposition in a global economy.

Meanwhile, there are efforts underway in Maryland – includ-

ing a handful in the agricultural community – to develop alternative sources of power generation utilizing agricultural and forestry byproducts to generate electricity that can be used by the producers and sold to the distribution companies. Though none of this is meaningful at the moment, it will become more so as the price of energy continues to climb. This is certainly an area where government could lend a boost by providing tax incentives or facilitating loans to assist fledgling start-ups and technology development.

If you ever had any doubts about the need to be alert and active on the political front, those should be put aside forever.

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Editor’s Note: Timothy Capps is the former executive vice president of the Maryland Jockey Club and, before that, the Maryland Horse Breeders Association. He is currently working as a consultant in the industry.

Coping with the Crisis

When *Equiery* readers were queried about how higher energy prices were affecting them, the responses were both swift and interesting.

As might be expected, the greatest immediate concern is with the surge in gasoline and diesel fuel prices, and virtually every respondent mentioned that as an inhibiting factor in their equine activities.

Overwhelmingly, people are curtailing anything that requires significant transportation expenditures, which means cutting back on showing or attendance at clinics or lessons. Several riding operations mentioned that their business was off significantly because of higher gas prices, with customers spacing out their lessons or simply dropping out altogether for the time being. Some of those who have competed actively in the past said they had essentially stopped doing so for now, choosing to spend their money on farm operations instead and citing rising veterinary, farrier, mowing and other costs as a result of the higher gas prices.

Virtually all of the boarding operations said that they had raised prices somewhat to help offset the higher energy costs, with a couple of respondents noting that their electric bills had almost doubled already. In addition, many reported taking conservation measures like the following:

- Using solar powered fence charges and/or looking into use of solar roof panels
- Using timers on lights and fans
- Keeping all outside lights off except in emergencies
- Changing barn hours to avoid non-day-light activities
- Cutting off fans and lights when horses are outside, also eliminating any non-essential appliances
- Keeping horse operations at the same level, but closing up the house, keeping lights off and turning up the thermostat
- Eliminating HBO and cutting back on take-out food in order to maintain horse activities
- Starting to use bio-diesel as a cheaper, cleaner burning alternative to gas or regular diesel fuel
- Buying a small car for regular transportation while keeping the pick-up parked unless absolutely necessary

The thrust of the responses is that horse people are looking for different ways to change their energy-burning habits. Those who offer products or services are also having to adjust their prices upward to reflect

the higher energy costs, and are nervous about doing so because higher gas prices have already driven customers away. At the same time, many said they have made sacrifices in personal consumption in order to maintain their horse care standards, and have found that their reductions in travel to shows or other events has given them a new appreciation of their horses and having them in their backyard.

Taken together, these responses indicate an economy that is slowing down – perhaps heading into a recession – due primarily to higher gas and utility costs. Unfortunately, there is little that elected officials and regulators can do to fix things or even ease the pain.

It is a time of uncertainty, much like the mid- and late '70s, when a sluggish economy and persistently higher prices (triggered by oil price shocks resulting from Middle East armed conflicts) led to double-digit inflation and double-digit interest rates.

It wasn't pleasant then, and it isn't likely to be now. The good news is that we got through that period, learned some lessons, and emerged better and stronger.

The better news is that your horses don't even know it's happening.

–*Timothy Capps*

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MHIB Awards Grants

The Maryland Horse Industry Board announced on July 19 that 13 groups will receive more than \$20,000 in MHIB grants this year, among them therapeutic riding programs, youth clubs, public riding facilities, educational programs and research programs.

These grants help build awareness of and involvement in the horse industry through research, education, and promotional activities.

"The equine industry is important to the state's economy and to the lives of many Marylanders," said state Agriculture Secretary Lewis R. Riley. "The scope and worth of the projects the board evaluated illustrates the demand for these grants. The 'feed fund' continues to make it possible to support many of those requests."

The latter fund, established during the 2002 legislative session, provides an ongoing source of money to promote the horse industry. The refundable \$2 per ton assessment on equine feed costs about \$1 per horse per year to the horse owner and supports this grant program as well as other promotional, research, and outreach activities undertaken by the Maryland Horse Industry Board.

This year, the board received 27 grant applications totaling more than \$100,000, with individual requests ranging from \$750-\$10,000. Projects were evaluated for value to the industry, degree of industry promotion, size and scope of the activity, financial need, and quality of the written presentation. To date, the MHIB has awarded 136 grants totaling more than \$150,000.

The Maryland Horse Industry Board was established in 1998 to promote and develop the horse industry. For further information, contact MHIB Executive Director Rob Burk at 410-841-5861.

2006 Grant Winners

- LEAD Maryland, Susan R. Harrison, 410-827-8056 ext. 136, Class V Fellows Seminars 2007, \$3,300 (Queen Anne's County)

- Maryland Horse Council-Trails and Greenways, Peggy Bree, 410-224-8804, Southeast Equestrian Trails Conference attendance, \$435 (Howard County)

- Maryland Combined Training Association, Janene Gerling-Dunsmore, 410-429-4964, MCTA Horse Trials at Shawan Downs, \$1,000 (Baltimore County)

- University of Maryland, Erin Petersen, 301-405-4690, 2007 Equine Science Society Conference, \$3,596 (Prince George's County)

- Fair Hill International, Charles T. Colgan, 410-398-2111, facility upgrades, \$2,500.00 (Cecil County)

- University of Maryland, Dr. Amy Burk, 301-405-8337, research equipment, \$2,500 (Prince George's County)

- VA-MD College of Veterinary Medicine, Equine Medical Center, Dr. L. Jill McCutcheon, 703-771-6800, equipment for collaborative research lab, \$2,000 (Prince George's County)

- Calvert Therapeutic Riding Center, Leah Rayburn, 410-610-5455, therapeutic riding ramp, \$800 (Calvert County)

- Great Strides Therapeutic Riding Inc., Terry A. Lewis, 301-253-1166, therapeutic vaulting equipment, \$1,565 (Montgomery County)

- Therapeutic & Recreational Riding Center, Dr. Helen Tuel, 410-489-5100, therapeutic riding saddle, \$1,120 (Howard County)

- Garrett Hoofprints 4-H Club, Sheryl Jordan, 301-746-6320, State Horse Bowl competition costs, \$500 (Garrett County)

- Meade Pony Club, Debra Lambert, 410-242-6946, rally attendance costs, \$600 (Anne Arundel County)

- Southern Maryland Horse Council, Susan Cusic, 301-769-3552, Horse Science School, \$500 (Saint Mary's County)

Total Awarded Funds \$20,416.00

Meadowbrook Revisited

In the August issue of *The Equiery*, we reported on neighbors who found housing for 40 horses when flood conditions prompted the June 27 evacua-

tion of Meadowbrook Stables in Chevy Chase.

It is also worth mentioning that several other people helped devise back-up plans in the event that the displaced horses' original housing arrangements fell through. For instance, through Liz Sponseller, Sen. David Brinkley was alerted, as was *The Equiery*, and through our office, Shamrock Farm manager and Maryland Horse Industry Board chairman Jim Steele became aware of the dilemma. The latter contacted Glade Valley Farm near Frederick, whose owners thought they could help. In addition, Willow Hill Farm in New Market had just hung out its shingle and agreed to accommodate all of Meadowbrook's horses, if necessary.

Forum Addresses NAIS, Unwanted Horses

American Horse Council leaders will discuss current issues such as the National Animal Identification System and its impact on the horse industry at the American Horse Council

Issues Forum Sept. 25 in Austin, Texas.

On a related note, the Equine Species Working Group (ESWG) has developed an informational booklet entitled *NAIS and Horses: the Facts Surrounding the National Animal Identification System as it Applies to the Horse Industry in the U.S.* It is currently available through the American Horse Council.

Another issue scheduled for discussion at the AHC forum is the Unwanted Horse Coalition, which was recently folded into the AHC. The mission of the coalition, which grew out of a workshop at the AHC's 2005 National Issues Forum, is to explore ways to reduce the number of horses that are unwanted each year and to improve their welfare through education and organizations committed to the health, safety and responsible care of the horse. Owner education will be a focal point, whereas advocacy in the legislative arena will not.

For more information, visit www.equiery.com ■