Banking on Energy: A Reflection on Patterns of Deregulation

Roger D. Feldman, Partner
Chair, Project/Structured Finance
Bingham Dana LLP
(Washington, DC, office)

THIRTY YEARS AGO, BANKS LOOKED LIKE UTILITIES.

They had *fragmented service areas*, reflecting regulatory policy; *fragmented service lines*, again a product of regulation; and *stability*, based on that territorial division.

While regulation stood still, it turned out funds could be raised, transferred and paid for by non-bank competitors. Electronic commerce turbocharged the process. ("Independent liquidity producers," as it were, arrived on the scene.)

Goliath Trust stirred, however, breathed the fire of deregulation, and broke the chains of regulation, both sectorial and regional. The result is the elephant mating dance we now see; the prospect is for a few tyrannosaurs roaming the financial jungle.

Energy superficially took a different route from banking. Deregulation began as a David & Goliath upstart revolution; it proceeded in Congress as a mega consumers revolt. Consolidation thus appeared to be the last gasp of the old order.

But what does California teach us? The stranded cost recovery gambit has proved a powerful delaying barrier to change. The retail customer market has proved dauntingly unfluid, pax Enron. Meanwhile, the asset purchasers have turned out to be mostly the biggest utility "boys-next-door." The divested behemoths have become the acquirers across the continent. Convergence has been fully rationalized.

Meanwhile the use of ISOs in the name of system efficiency has all the earmarks of providing large market territories for those with expanding generation power. Even were anti-trust standards to suddenly be reasserted, they will do so in the light of this larger definition of competition. Just as the securities and banking industries have melded, so too inexorably will the energy industries.

So, despite seemingly divergent paths, after 35 years, banks and utilities may well look alike again. Private power, aggregation and discount brokerage are alike—all slated to be divisions of national pillars. (Indeed, the rationale of separation of energy and finance may be expected to blur as well.)

In neither industry does a reliance on resurgent consumer populism seem like a likely business strategy. In finance, the possibilities for customization under the radar "seems possible." In a sense, private ESCOs represent an analogous phenomenon in energy.

But is this all for the good? It is not entirely clear that the cycle of deregulation/competitive diversification/consolidation is necessarily in the optimal long-term public interest in either industry. Just as enforced fragmented monopoly led to stagnated innovative change, so too can apparently competitive oligopoly. (Remember what happened to the U.S. auto industry when it ruled the market.)

Since we are still in the period of industry transition to change, this concern may seem extraneous or alarmist musing. The political debate is still being framed as one of consumerists versus monopolists defending their fiefdoms.

But perhaps a different public policy needs to be taken—in banking and in energy. Not a backward-looking Luddite cry for community banks and neighborhood "Reddy Kilowatts," but a focus on what it will take to perpetuate the sparks of innovation which deregulation initially produces: new services, new technical products, continual possibilities of market entry.

Not a backward looking restraint on self-generated growth, but a preservation of some areas of growth, for some period of time, before their opening to the general marketplace.

Inevitably the actual areas of opportunity where such a policy may be appropriate often prove to be different than those which appear most plausible at any time. But just as there seems to be a logic to preserving the internet as a vehicle for competitive finance, so the area of dispersed energy development might benefit from protective "infant industry" status.

While deregulated capitalism can produce both astonishing creativity and undreamed of new forms of business organizations, in energy as in banking, there is merit in recognizing that it will seek financially satisfying (and potentially stultifying) oligopolistic stasis, unless our approach to deregulation seeks to learn from the past.

We may bank our energies, if we allow energy to go the way of the banks.

ABOUT THE AUTHOR

Roger D. Feldman, Chair of the 35-member Energy Finance Group of the 325-attorney national firm of Bingham Dana LLP, has been involved in all types of project finance and development for over 30 years. He has also been deputy administrator of the Federal Energy Administration, chair of the American Bar Association's Energy Law Committee and a regular columnist in *The Cogeneration and Power Marketing Letter* and *The Construction Business Review*. He is a member of the editorial board of *Cogeneration and Competitive Power Journal*. Mr. Feldman is a graduate of Brown University, Yale Law School and Harvard Business School.

Bingham Dana, 1200 19th Street, N.W., Suite 400, Washington, DC 20036-2400; 202-778-3181; feldman@bingham.com