policy and making regulatory decisions.

THERE IS MORE WHERE THAT CAME FROM

EPA IS NOT THE ONLY REGULATORY AGENCY TO FAIL IN ITS basic mission. Following the dust bowl of the 1930s, the U.S. government created the Soil Conservation Service, now the Natural Resources Conservation Service (NRCS), to monitor soil erosion and encourage efforts to reduce soil erosion from farmers' fields. The agency was quick to create an army of "conservationists" to advise farmers, but it failed miserably at the basic task of measuring and monitoring soil erosion.

It turns out that soil erosion has been nearly eliminated as a major problem according to an exhaustive, 30-year research effort by Stanley Trimble at the University of California, Los Angeles. Trimble's research, which includes data from the 1930s he found in the National Archives, indicates that soil erosion rates in the Coon Creek Basin of Wisconsin are only about five percent of what they were during the dust bowl. Recent U.S. government erosion estimates for the basin, originally chosen for study because of tremendous erosion problems, are about three times higher. If the erosion rates are that low in a highly erodible basin, as Trimble puts it, "the burden of proof is on those who have been making pronouncements about big erosion numbers."

The continued widespread perception that soil erosion remains a major agricultural and environmental problem is a direct result of the government's lack of effective monitoring.

The crux of the problem is that there are no incentives for a government bureaucracy to track the problems it is tasked with solving. Discovering the truth could put the agency out of business. Until Congress demands that EPA and NRCS—and who knows how many other bureaucracies—actually find problems before we fix them, expect more Dilbert doublespeak. ■

Is There Light at the End of the Regulatory Tunnel? Not in Pennsylvania

By Randolph J. May

THE PROMISE OF UNFETTERED COMPETITION AND meaningful deregulation, so widely heralded when President Clinton signed the Telecommunications Act of 1996, has turned into what some have called a "regulatory Vietnam," a quagmire in which every step toward deregulation is matched by a step backwards.

The Federal Communications Commission (FCC) acknowledged in its draft strategic plan, "A New FCC for the 21st Century," that within five years it expects "vigorous competition that will greatly reduce the need for direct regulation." FCC nevertheless continues to pursue policies more suited to a bygone monopolistic era. Consider the following examples:

FCC continues to issue lengthy and intricate orders setting forth in minute detail the requirements that the incumbent local exchange carriers (ILECs) must follow in unbundling their networks and sharing their facilities. Most recently, the agency went so far as to require ILECs to unbundle the bandwidth capacity of individual loops and sell it to all comers at government regulated prices.

FCC engages in time-consuming reviews of telecommunications company mergers under the indeterminate "public interest" standard, duplicating the competitive analysis performed by the Department of Justice. In order to gain approval to merge, the parties typically propose "voluntary" conditions that go far beyond regulatory requirements. For example, approval of the SBC-Ameritech merger was conditioned on compliance with thirty (not counting the subparts!) extremely detailed new requirements.

Even after the fourth anniversary of the 1996 Act, the agency has approved only one request to allow a Bell operating company to provide long distance service, despite the fact that several state regulatory bodies have recommended approval of such requests.

These examples are at the federal level. Unfortunately, there are examples of actions at the state level that are even more regulatory and inconsistent with the development of competition. A recent action of the Pennsylvania Public Utility Commission (PUC) is a case in point.

WHAT PENNSYLVANIA HAS DONE

ON SEPTEMBER 30, 1999, THE PENNSYLVANIA PUC ISSUED an order that sets a new standard for regulatory intervention in today's competitive telecommunications markets. Simply put, the order goes beyond regulation to demand the breakup of the local telephone company, Bell Atlantic-Pennsylvania, Inc., into two companies for purposes of

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offering local exchange services. One entity would offer only “wholesale” services, the other only “retail” services. The retail company would compete in a more or less unregulated market against other local phone companies—the “competitive local exchange carriers” (CLECs). But the wholesale company would be subject to traditional regulation, apparently into the indefinite future.

This proposal is misguided because it appears to assume—contrary even to what FCC is now saying—that the incumbent telephone company’s local exchange network will never face effective competition and, therefore, that the incumbent’s local exchange services must be subject indefinitely to heavy regulatory oversight. Such a regime reduces ILECs’ incentives to invest in network modernization efforts and undermines the development of competition.

STRUCTURAL SEPARATION ASSUMES PERMANENT MONOPOLIES

THE FUNDAMENTAL PURPOSE OF REQUIRING SEPARATION between various parts of ILECs is to keep them from using their dominant market power to favor their own affiliates over their competitors and from cross-subsidizing their competitive services with revenues from their non-competitive services.

Structural separation involves the creation of wholly separate subsidiaries, with separate corporate structures, separate staff, facilities, offices, and so forth. Nonstructural safeguards typically imply (1) accounting conventions to ensure the appropriate allocation of costs between the regulated and unregulated portions of the business and (2) equal-access requirements to ensure nondiscrimination.

Before the implementation of policies at the federal and state level designed to foster competition at the local level—and before the resulting emergence of competition—the imposition of some form of structural separation may have made sense. Structural separation generally imposes greater costs than does reliance on nonstructural safeguards, because structural separation leads to duplication of facilities, personnel, and systems. But if the prospects for the development of competition are sufficiently bleak, such greater costs arguably might be justified.

Assuming that competition is the ultimate goal, however, the Pennsylvania’s PUC’s decision to require structural separation at this late date can only be counter-productive. Specifically, the interconnection, unbundling, and resale requirements applicable to ILECs—the array of nonstructural safeguards guaranteeing that an ILEC’s competitors will have cost-based access to the ILEC’s network infrastructure—ensure the opening of the local exchange marketplace to competition.

In fact, right across the border, the New York Public Service Commission already has determined that the local exchange marketplace is open to competition. There are differences between New York and Pennsylvania, of course, but it is difficult to imagine that the conditions in the two states are so different that Bell Atlantic-Pennsylvania would be that far behind Bell Atlantic-NY in complying with market-opening requirements.

Indeed, Bell Atlantic’s progress in Pennsylvania is confirmed by the fact that the Pennsylvania PUC says it anticipates that Bell Atlantic can obtain “Section 271 approval” from FCC to offer long-distance services within approximately one year. As the commission points out, in order to recommend such approval to FCC, the Department of Justice must conclude that the local market is “irreversibly open to competition” and FCC must find that Bell Atlantic has satisfied a 14-point competitive checklist.

> Public policy has not caught up with the reality of telecommunications competition. Proposals such as Pennsylvania’s represent a throwback to an earlier era, when monopoly was the rule and regulation the natural response.

The Pennsylvania PUC’s action is even more difficult to understand when one considers the timing. The commission specifically states that it does not anticipate it can complete a follow-on proceeding necessary to develop a structural separation plan before FCC is ready to grant Bell Atlantic’s request for Section 271 approval. Thus, the Pennsylvania PUC proposes to implement a plan appropriate only for a monopoly at the very time that—by its own reckoning—procompetitive measures will have succeeded in “irreversibly” opening local exchanges to competition.

Whatever merits a structural separation approach may have had in the past, it is counterproductive for regulators to impose such a costly remedy at this late date, when compliance with nonstructural safeguards will foster competition.

CONCLUSION

THE TELECOMMUNICATIONS ACT WAS DESIGNED TO MOVE the telecommunications industry away from its historical monopoly structure to one characterized by competition. While neither the Act nor its implementation by FCC (or state public utility commissions) has been close to perfect, the fact is that the telecommunications industry today is vastly more competitive than it was in February 1996, when the Telecommunications Act became law. Indeed, there is now widespread agreement that the industry is moving in the direction of becoming fully competitive, and that there will be no continuing need for significant continuing economic regulation.

Obviously, however, public policy has not caught up with the reality of telecommunications competition. Proposals such as Pennsylvania's represent a throwback to an earlier era, when monopoly was the rule and regulation the natural response. Rather than facilitate the transition to competition, such overzealous regulatory intervention can only slow it down, driving the light at the end of the regulatory tunnel further into the indefinite future. ■

The "Backdoor Btu Tax"

By Glenn Schleede

Many people in the "traditional" energy industries relish the recollection of the stinging defeat in 1993 of the hated Clinton-Gore "Btu Tax." Political ideas never die, however, they just come back in different forms. Few have recognized it, but the national Renewable Portfolio Standards (RPS) and renewable credit trading scheme in the Clinton administration's proposed "Comprehensive Electricity Competition Act" would tax electricity produced from coal, oil, natural gas, nuclear energy, and hydropower, much like the proposed 1993 tax.

The "Broad Based Energy Tax," or Btu tax, proposed in 1993 would have imposed a tax ranging from $0.257 to $0.599 per million Btu on coal, oil, natural gas, nuclear energy, and electricity from hydropower. The tax would *not* have been imposed on non-hydro renewable energy sources. The purpose of the tax was to increase the price of the "undesirable" forms of energy targeted by the tax.

The proposed national RPS would require certain percentages of all electricity offered for sale to come from non-hydro renewable energy sources, including geothermal, biomass (including biomass used in coal-fired plants), solar thermal, solar photovoltaic, wind, and the biomass portion of municipal solid wastes. Because the use of these energy sources generally results in higher cots, the Clinton administration produced a scheme that would *force* electricity sellers to include electricity from non-hydro renewable sources in their product mix:

- First, organizations producing electricity from non-hydro renewable energy sources would be given "tradable credits" for each kilowatt-hour (kWh) of electricity produced.

- Second, electricity sellers would be required to include a specified percentage of electricity from non-hydro renewable energy sources in the mix of electricity they sell: a minimum of 2.4 percent from 2000 to 2004, increasing to a minimum of 7.5 percent by 2010.

Electricity suppliers could meet the minimums in any of the following four ways:

- Produce some electricity from non-hydro renewable energy sources.

- Buy electricity produced by other organizations from non-hydro renewable energy sources.

- Buy "tradable credits" from organizations that produce electricity from non-hydro renewable energy sources.

- Buy the credits from the U.S. Department of Energy at a cost of $0.015 per kWh. (The availability of credits from DOE at $0.015 per kWh is intended to put a cap on the "market" price for the credits.)

In one of these ways, electricity sellers would be forced to incur higher costs because of RPS. Suppliers would, to the best of their ability, pass those higher costs to their customers by spreading the higher costs of "green" electricity across all kWh sold. In effect, the higher costs would become a "tax" on electricity produced from "undesirable" energy sources: natural gas, oil, coal, nuclear energy, and hydropower. Suppliers would have no practical alternative, except in states where customers can volunteer to pay a premium price for more expensive "green" electricity.

The added cost of meeting the Renewable Portfolio Standards may seem quite small. For example, it would be about $0.0012 per kWh for a producer buying only enough credits from DOE to meet the 7.5 percent minimum in 2010. And $0.0012 per kWh is roughly $0.12 per million Btu—a little less than half the $0.257 per million Btu tax proposed in 1993 for coal, natural gas, nuclear energy, hydropower, and some oil products. Advocates of RPS probably assume that such a small "tax" would not be noticed in monthly electricity bills—and the "backdoor Btu tax" would have its foot in the backdoor. ■

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