U.S. has a bad case of crony capitalism
by William O'Keefe

"Entrepreneur" used to refer to someone who assumed the risk of a business venture with the expectation of making a profit. In the political world, however, our overregulated economy has spawned a new type of entrepreneur: the political entrepreneur, who exploits the regulatory and legislative process for profit and whose assumed risk is mitigated or even eliminated by political and government connections. Cooperation with government for financial gain all too often leads to crony capitalism, and we have a bad case of it.

A recent New York Times article - "Ties to Obama Aided in Access for Big Utility" - documented how Exelon Corp., a Chicago-based utility, used its political support of President Obama for access and profit. According to the Times, Exelon was one of six utilities that received the maximum $200 million stimulus grant. It also got a $600 million renewable-energy grant and a $646 million loan guarantee for a solar project in Los Angeles. One of Exelon's subsidiaries received a $200 million grant to install "smart meters" in the Philadelphia area.

There is nothing in the Times article to suggest Exelon did anything wrong in reaping those rewards or in lobbying to influence regulations. Exelon is just one of a growing number of companies that find profiting from the regulatory system easier than beating competitors in the marketplace. As the Times reported, one federal official who met with Exelon representatives said that "while the company's connections did not guide specific decisions, federal officials knew to handle Exelon carefully."

The economic burden from steady growth in regulations coming out of Washington provides a strong incentive for companies to work the system. Some go beyond attempting to reduce the cost of regulation and attempt to game the system so that regulatory burdens fall heavier on competitors.

When the environmental community pushed to ban incandescent light bulbs, leading the charge were General Electric and Phillips Electric, two companies that had invested heavily in the unpopular fluorescent light bulbs. What they were unable to gain in the marketplace, they gained in the halls of Congress. Getting the heavy hand of government to tilt the playing field in favor of some companies is seen as fair play.

These examples are what Clemson University economist Bruce Yandle dubbed the

"Baptist and Bootlegger" theory of regulation. This theory explains how the political world works in a heavily regulated economy: Public-interest arguments are used to serve special interests. The theory derives its name from state attempts to ban the sale of alcohol on Sundays. Baptists strongly supported those efforts on moral grounds, while bootleggers tolerated them, knowing full well that their effect would be to limit competition, not consumption.

The complexity of environmental issues, a regulatory bias toward command-and-control approaches and extreme advocacy of environmentalists - the Baptists in this case - has created fertile ground for bootleggers to profit. When the Environmental Protection Agency (EPA) began tightening clean-air rules in 2010, according to the New York Times, Exelon estimated it would earn $400 million annually because the regulations would force dozens of competing coal-burning plants to close.

Just recently, the EPA issued a controversial Utility MACT (Maximum Achievable Control Technology) regulation, which is the most expensive regulation under the Clean Air Act - $10.9 billion annually. The winners from this regulation are utilities with nuclear or compliant coal-fired plants. Recognizing that the rule would force some utilities to close, these actors formed the Clean Energy Group to support the EPA's initiative. This group of bootleggers based its support of the multibillion-dollar rule with advocacy saying it would promote the public health and the economy. In reality, they profit; the consumer pays.

Bernstein Research's report "U.S. Utilities: Coal Fired Generation Is Squeezed in the Vice of EPA Regulation; Who Wins and Who Loses," examined the regulation's impact and concluded that some utilities would gain upward of $362 million in additional revenue by 2015. The other side of the ledger is a NERA Economic Consulting report concluding that retail electricity prices will rise upward of 24 percent and employment will be reduced by 1.4 million jobs between 2013 and 2020.

The Baptist-Bootlegger coalition didn't begin with the Obama administration, and it won't disappear when the administration ends. It has gotten worse as a result of regulatory zealotry, stimulus spending, Solyndra-style opportunism and an administration that thinks rewarding the politically favored is good public policy. "Crony capitalism," a frequently used term describing firms that seek to invest with taxpayer dollars instead of shareowner dollars, will not reduce unemployment, promote robust economic growth or help the United States compete in the global economy. Reform is needed. Shrinking the public trough, creating a level playing field, providing business confidence and implementing true regulatory reform provide a good start.

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