

# Don King Energy Economics

BY DOUGLAS B. REYNOLDS

In politics as in economics there are two focal points to a majority of arguments: The Carl Marx side and the Adam Smith side. The Marxian side has everything to do with socialism, government ownership or command and control aspects of an economy, which is either considered socially egalitarian or inefficient. The Smithian side is everything to do with free market capitalism and dog eat dog competition which is either considered efficient or income inequality maximizing. Some of the greatest heroes for the Smithian side are entrepreneurs like Mark Zuckerberg who made all his money by “borrowing” the initial idea and creating a natural monopoly that has built in barriers to entry, economies of scale and merchandisable data. Other tech oligopolies are similar. A Marxian-type hero is U.S. President Franklin D. Roosevelt who initiated social security in America even though it relies on a dwindling cohort of young workers paying ever more money to keep the system afloat.

But maybe there is another economic system out there that could work better, at least in some instances: Don King Economics. Don King was an agent for heavy weight and other weight boxers. As one boxer said about him, before Don King came along, boxers were only receiving tens of thousands of dollars per fight but after Don King they were receiving tens of millions of dollars per fight. So if Don King makes so many millions of dollars as an agent, it is worth it to the fighter because Don King makes sure each fighter gets millions of dollars in pay. Indeed, boxers like Muhammad Ali (formerly Cassius Clay) did only receive so many thousands of dollars per fight, then after Don King, boxers like Floyd Mayweather received tens of millions of dollars per fight. So having a star negotiator can enhance the value to the economic agents involved, and possibly even to the paying public.

## 1. CEO Bonuses

This kind of Don King economics is alive and well within most corporations where star CEOs receive huge stock option bonuses for their work. And even though some of the stock option specifics could be questionable, nevertheless, most large and even smaller corporations have some form of stock option bonuses now. As The Economist’s (2007) Special Report on Executive Pay said, “Where as executives in publicly traded companies earned about \$3 per each extra \$1,000 in profits, managers in the buyout firms earned about \$64. According to Steven Kaplan of university of Chicago” p. 8 and “the lions share of executive bonanza was deserved in the sense that shareholders got value for the money they handed over.” P. 4. So Don King economics is alive and well. But if it works for corporations, why not try it in other contexts too such as with monopoly electric power utilities.

For some reason there is this belief in energy economics that having a free market electric generator system is the end all be all of electric power utilities and grids even though there is no easy entry or easy exit of such generators on to the market making such generators oligopolies or even making the utility grid a semi socialist system to make up for gaps in supply. But rather than putting the Smithian square peg into a natural monopoly round hole, a Don King system could work better. However, instead of a Don King system incentivizing the use of the natural monopoly characteristics of the utility to ratchet up the electric power price (or tariff) the system can rather be used to incentivize lower prices and if necessary lower carbon emissions.

Think of the beauty of Don King economics. The Don King electric utility monopoly CEO (or King or Tzar) would be given a bonus not for raising prices, but for lowering them. To incentivize long term investments and maintenance the CEO would also receive a bonus for keeping prices, or carbon emissions, low 5, 10 and 15 years after his or her term. And as Don King received millions but was worth it to the boxers, so the utility CEO might receive millions in bonuses but would be worth it to all the electric utility customers and businesses. Such a CEO will be able to use better coordination of generators, power lines and demand side incentives to reduce electric power prices and carbon emissions. The CEO can himself incentivize local utility customers to use energy efficient systems through various public relations steps or even with coordinated neighborhood power storage.

## 2. Consumer Sovereignty

Consider for a moment the whole idea of consumer sovereignty. The idea is, if you have real time power prices, then consumers will react and start to invest in more efficient appliances or better allocate their hourly use of electricity, or even invest in renewables. But having talked to a consumer once who had real time pricing, they said that after a few weeks of checking prices, they soon gave up and didn’t bother with it anymore. This has to do with the costs and benefits of any given consumer action.

When consumers consider their one vacation a year, they may check several websites to save hundreds of dollars on different packages, but also in the process ruminate positively on the coming vacation. If time is worth say \$30 per hour and in one or two hours they can save \$300 on their vacation plan, and gain the imagination benefit of the vacation, then the cost to benefit value of their consumer sovereignty time is well worth it. But if it takes a protracted amount of time

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to check power prices and consider plans to mitigate power costs, the value the consumer gets may not be worth it, and then the cost to benefit net-value of their consumer sovereignty time is not worth it. Even using an automatic or AI system to check prices and possible strategies may take too much consumer time since AI systems can't go out and buy a new dishwasher. This is one of the problems with free markets for health care. You just can't obtain a lot of consumer sovereignty value when the time it takes to understand a market is high and the value you get from that understanding is low. Similarly, the whole behind the meter movement has to be looked at more articulately.

But having a Don King-like run utility can allow the CEO to use simplified prices and other easy to understand incentives for consumers to conduct demand side management techniques or even to engage in neighborhood renewables if that makes sense. With such a Don King-like utility, you will probably have more success in increasing social value of a utility then when you have a lot of inefficient consumer sovereignty in, around or outside the meter.

### 3. Next Administration Energy Team Research

When most of the general public, or for that matter competent engineers, look at all of the complex market mechanisms for free market electric utilities, they can't possibly know what is going on. On top of that, you have so much permitting for any given type of generator, it makes it impossible for the average Joe to enter the market. The real issue is that carbon emission reduction advocates are hoping to keep utilities as opaque as possible from proper economic analysis of any given renewable energy system because to them even one ounce of carbon emission reductions is worth thousands of dollars in their minds. So they don't like having transparency. If a Don King economic system were imposed, suddenly each ton of CO<sub>2</sub> reduction is going to be priced at a much lower price and the total amount of carbon reductions may not end up being as great as in a non-Don King system no matter how cost effectively carbon reductions are

done. But that needs to be tested. Nevertheless, carbon reducing advocates want to keep everything as opaque as possible which is why there is such a focus on having the so called free market utility model pushed so hard.

What the next administration's energy team needs to do is to run some experimental economic studies to see if indeed a Don King economic system for electric utilities will work, because such a system would normally take years or even decades to see if it creates good economic outcomes otherwise. What some experimental economic runs could do would be to take data from one or another past utility history, even using older data and older technologies from decades ago, and use those older situations to simulate an in laboratory test of switching technologies or even utility re-organizations. They could run with that data to see what a CEO would do if incentivized and confronted with potential technology or organizational switches. That way a real time investment scenario over years can be reduced into one hour or even a few minutes so that the experimenters can tell which type of CEO bonuses work best for inducing cheaper electric power or even reducing carbon emissions over a short and long run time frame.

They could even run consumer experiments to see what types of incentives work best for inducing the kinds of consumer side changes that efficiently reduce power prices or carbon emissions, like for example inducing demand side management.

One such Don King energy economic scenario is given by Reynolds and Zhou (2019).

### References:

- Reynolds, Douglas B. and Xiyu Zhou (2019). "An Alternative Utility Structure: Incentivized Management and The Principal-Agent Problem," at *The 4th IAEE Eurasian Conference, Energy Resources of the Caspian and Central Asia: Regional and Global Outlook*, Nur-Sultan (formerly Astana), Kazakhstan, October 17-19, 2019; <https://www.iaee.org/en/conferences/eurasia.aspx>, and <https://www.eurasianconference.com/>, *The Economist*, (2007). "Special Report on Executive Pay," January 20, 2007.