The Washington Post

SUNDAY, DECEMBER 2, 1984

WHOOPS

DARKNESS TO DAWN

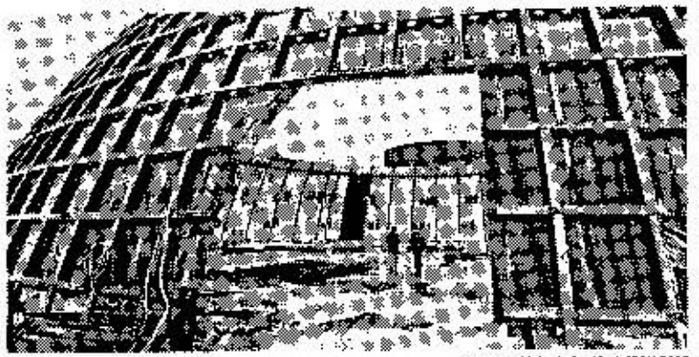
An Ambitious Nuclear Empire Goes Awry

First of four articles

By Chip Brown
Washington Post Staff Writer

OKANOGAN, Wash.—Nick Cain has been growing apples for 32 years in a blossom-scented valley south of here in the shadow of the North Cascades. Each spring he takes out a loan to be repaid come fall when the apples are boxed. The paperwork is the sort of formality big men in small towns suffer lightly. Cain had harvested a reputation long before his tenure as president of the Washington Public Power Supply System. He was the founder of a juice company, a trustee of the Malott Methodist Church and an officer of the Okanogan Fly Fishing Club. Most mornings he could be found at the Cariboo Inn, drinking coffee with the boys.

Applying for his loan this year, Cain had to pause.



BY MAY LUSSIG—THE WASHINGTON POST

A containment building dome at Project 4 on the Hanford Reservation cost the supply system $1.3 million, but later was sold for scrap for $14,000.

Are there any lawsuits for or against you?

He wondered would *only* 21 sound better than *just* 21?

What for?

Facts were facts: *Securities fraud.*

How much money is involved?

The hazard of public life! Cain scribbled in the amount, trying to imagine the reaction down at the bank: *Seven billion dollars.*

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In the thrall of the atom, the Washington Public Power Supply System aspired to one of the most ambitious nuclear empires in the nation. Having never built a nuclear plant, the consortium of utilities known as Whoops tried to construct five all at once. It let contracts, cleared forests, cut roads, hired armies of craftsmen and printed more than $8 billion in tax-exempt bonds, more municipal bonds than any private or public corporation in American history.

Of the five reactors, Whoops finished one. Two were mothballed. Two others known as Projects 4 and 5 were abandoned, and last year Whoops defaulted on $2.25 billion in bonds held by 78,000 people from all parts of the country.

In Whoops the story of nuclear power is written on an almost legendary scale. From conception to collapse, everything about it was colossal. Whoops was premised on exorbitant predictions of growth and a misplaced faith in the economies of scale. During its rise in the late 1970s the costs rocketed upward at an

See WHOOPS, A20, Col. 1

Nuclear Vision Fails On Colossal Scale

WHOOPS, From A1

average rate of half a million dollars an hour. After its fall it became the focus of more than 60 lawsuits, including the nation's largest securities fraud case. For that suit alone more than 140 million documents have been produced.

To many Whoops marks a massive breach of responsibility that has tarnished both the Northwest and the nation's financial community. History's largest municipal bond default points up the lessons of New York City's money crisis in 1975, and raises once more the question of Wall Street's duty to scrutinize the product it sells. Were major underwriters not so reluctant to investigate their clients, they might have paid more attention to the signs of impending political and economic trouble.

Big institutions with multimillion-dollar positions got burned by Whoops. So did affluent bondholders like the Minnesota Vikings Football Club, sacked for a $200,000 loss, and Peanuts cartoonist Charles M. Schultz, who had a $75,000 security blanket of Whoops bonds. But most of those who suffered were not so well-to-do. Thousands of nurses, teachers, veterans and retired couples who depended on the income saw the value of their modest holdings all but destroyed.

Even the musical comedy name—Whoops—seems larger than life, something dreamed up by a puckish showman to encapsulate the history of an epic pratfall. Sportswriters and account executives use the name as a synonym for fiasco. Cartoon galleries equate it with the Hindenburg, Frankenstein and the Titanic. The judge hearing most of the legal cases has banned the word Whoops from his courtroom in favor of the less prejudicial "Supply System."

Down the Road to Eden

It seems fantastic now, the hope that was held out for nuclear power when President Dwight D. Eisenhower proclaimed Atoms for Peace in 1953. Few technologies have ever been attended by so much promise only to be humbled so swiftly. After the bombs at Hiroshima and Nagasaki had demonstrated the darker power of nuclear physics, the country set out to find the "sunny side" of the atom. It was a mission with a moral impetus, as if nothing less than a paradise wrought by the same force could redeem the hell visited upon those cities. The early champions of the peaceful atom dreamed about an Eden where electricity would be, in that priceless phrase of physicist Lewis Strauss, "too cheap to meter." Breaking ground for the first atomic plant at Shippingport, Pa. in 1954, Eisenhower waved a radioactive magic wand and showed the country to a new frontier.

A generation later the nation reels from that adventure. More than an eighth of the country's electricity is produced by atoms; the amount may rise to as much as a fifth. But in the last dozen years 113 nuclear plants have been cancelled at a cost of more than $18 billion. No new reactors have been ordered since 1978. The decline in electric consumption since the 1973 oil embargo also has forced the cancellation of 67 coal plants, but this year the nuclear industry captured the spotlight with a series of spectacular setbacks. In a trend that began with Whoops, utilities quit largely completed projects in Indiana, Ohio, Michigan and Tennessee. Utilities once crowed about their nuclear plants in annual reports. Now some stress their fortune to be without them.

"Without significant changes in the technology, management and level of public acceptance, nuclear power in the United States is unlikely to be expanded in this century beyond the reactors already under construction," notes the congressional Office of Technology Assessment. The cover of that report, Nuclear Power in an Age of Uncertainty, shows a Whoops plant rising in a place once dubbed Atomsville USA where the ironies in the decline of nuclear power are sharper because doubts about its merit have never been entertained.

From the start the stakes were higher for Whoops. Populated by a blend of energy romantics and meliorists, the Pacific Northwest was given to atoms from the early days. A year and a half before he worked himself onto an operating table for quadruple bypass heart surgery, Whoops' managing director, Robert L. Ferguson, declared: "The nuclear and utility community of the entire nation is looking to the Supply System and its board to successfully complete this major commitment to nuclear energy. For if we cannot do it here, nuclear [power] may very well not make it in this country."

Today, a sense of waste pervades the deserted reactor sites. Project 5 molders in a Douglas fir forest on the rainy side of the mountains. Project 4 bleaches in the desert sun 200 miles to the east, surrounded by tumbleweed. Where workday sirens once split the air, only rock doves flex their wings. Jack rabbits scurry among piles of rusty steel. This spring a salvage company carved up one of the reactor domes for scrap. The bond default will not be as easily dispatched, for with interest, it totals more than $7 billion. Rancor and disillusionment are widespread; careers in ruin. People had a vision of a nuclear world, a faith in the atom matched by a sense of mission. Somewhere along the way the road to Eden went awry.

Men and Women of Vision, or Fools?

A protracted struggle over energy reveals a society's philosophy and values. The word favored in the Northwest is *vision*. A Whoops official named H.R. Kosmata addressed the supply system's annual meeting i 1979, the year the wheels were wobbling badly on the nuclear wagon an soon to come off altogether. "In your quiet private moments, or whe you're under fire in your service areas, you must wonder if we made th right choice," said Kosmata. "Were we men and women of vision, fools?"

Events would seem to make no bones about the answer. Thanks main to Whoops, Northwest electric rates increased more than 500 percent five years. Whoops plants roused a public lulled by more than three de ades of the cheapest power in the nation and made conservation a ne creed. Northwest power is still a bargain, but few people leave the lights burning all day, or clamor for all-electric, gold medallion homes, expect the future will be as the past has been. The world has shifte Many old-line utility commissioners caught in the sea change have quit been voted from office. Until Whoops, they had never been under fire in their service areas or anywhere else.

To appreciate the rise and fall of Whoops, and its broadest meanin one must first gather the history of a four-state, 275,000-square-m region known as the West's West. Nearly eight million New York Ci residents get their electricity from one private utility. The eight and half million residents of the Northwest are served by a mosaic of 1 public and private utilities.

The political structure of Whoops was similarly diffuse. Constructi proceeded with three designs, three architect/engineers and over 4 contractors. Three of the plants were backed by the federal Bonnevi Power Administration, the region's electric wholesaler that markets h and transmits 80 percent of the region's power. Projects 4 and 5 we backed by 88 utilities at a time when nuclear cancellations were overti ing starts. Down the road lay a period of wicked inflation: the deep economic decline since the Depression; a near-meltdown at Three M Island that changed the way nuclear plants were regulated; bid-riggi strikes, overruns, shortages, mudslides and volcanic eruptions.

The case against Whoops devolves mainly onto those who ran it. M agement problems may have been exemplified best in the travels o metal support known as pipe hanger #1847 located outside the Projec control room. Over a period of years, it was put up and torn down times before revised designs eliminated it once and for all. Whoops little incentive to hold down costs. The projects were funded with a gi credit card, and the sponsoring utilities bore the ultimate liability. M of them had only a take-it-or-leave-it, "Book of the Month Club" cont over Whoops, as one lawyer put it.

The Whoops board has been depicted as a well-meaning but ov matched band of sheep ranchers, muffler-shop owners and apple fa ers—men like Nick Cain, who were captives of its staff and contracto But even the sophisticated members from big utilities seemed to deve a cavalier attitude about money. They took time instead to debate shape of the boardroom table. Under siege, their pride and belief in th mission turned to hubris.

Roll On Columbia, Roll On

In Eugene O'Neill's play "Dynamo," a romantic young fellow worsh an electric generator as the mother of creation. "It all comes dow electricity in the end!" he cries. He embraces the dynamo, which re rocates by electrocuting him. Not one of O'Neill's better efforts, perh the play may best be read as a caution against getting overly emotic about utility issues. But there is one place in the country—the Pac Northwest—where everything does come down to electricity, wh electric power has an almost religious significance and the people k what O'Neill meant by "the hymn of electricity."

The hymn can be heard in the Columbia River as it thunders thro the turbines of the world's most powerful hydroelectric system. The lumbia is the economic aorta of the Northwest. It runs for 1,242 mile deep canyons and broad bends, its headwaters in the Canadian Rock its mouth at the Pacific near Astoria, Ore. One of the river's early exp ers was the eponymous Capt. Benjamin Bonneville, who impressed Indians with his bald head and plaid overcoat. But it was Woody Gut who put the river's music to words. During a month-long songwri stint at Bonneville in 1941, he batted out a tune a day on a guitar said "This Machine Kills Fascists." The ballad "Roll on Columbia" bec the energy anthem of the Northwest, and today it is sung in element schools and at utility picnics: "*Roll on, Columbia, roll on! Your powe turning our darkness to dawn, so roll on, Columbia, roll on!*"

Of the river's dams, none turns more darkness to dawn than Gr Coulee, the muscular monument revered here as what Guthrie ca "the mightiest thing ever made by man." Grand Coulee impounds the lumbia for 151 miles. Its 21 turbine generators spin like bewitched n ry-go-rounds. Transformers crackle as 500,000 volts of electricity ga into cables slung from tower to tower in long silver arcs. The tow stand like hierarchical figures on the horizon, relaying energy over pl and mountains to manufacture aluminum in Wenatchee, to power airc

See WHOOPS, A21, Col. 1

Northwest Fiasco Ends Atomic Dream

WHOOPS, From A20

and mountains to manufacture aluminum in Wenatchee, to power aircraft wind tunnels in Seattle factories, to push water through sprinkler pipes crouching over the fields in Ephrata. The old Bonneville motto was Power for Progress. Power and progress were one and the same.

The people who built Grand Coulee triumphed over more than 20 years of opposition. Rufus Woods, publisher of the Wenatchee Daily World and a tireless advocate of the dam, once declaimed in a speech: "Could you come back here a thousand years hence, or could your spirit hover around this place ten thousand years hence, you would hear the sojourners talking as they behold this 'slab of concrete,' and you would hear them say, 'Here in 1942, indeed there once lived a great people.' "

Whoops' nuclear empire was meant to be a rendezvous with the spirit of Grand Coulee. Conversations about the struggle to build five nuclear plants unfailingly hark back to that slab of concrete and the "vision" of that legendary generation.

Going to Hell and Back for Water

The North Cascades mountain range divides Washington state into two landscapes and two cultures. The dense, high-masted forests of the western slope yield abruptly to the eastern half where the ground rolls out in a hot, stringent landscape of sagebrush and rattlesnakes. The geographic centerpiece of eastern Washington is the Columbia Basin. Western writer Owen Wister passed through in the late 19th century. "20 miles to water," read a sign he saw. Underneath someone had scrawled, "One mile to hell."

Nick Cain knows the lengths to which farmers would go to cultivate the basin, where the land is so thirsty that farmers would sometimes dig every blade of grass from the ground to eliminate the competition for water. Growing up in Wenatchee, Cain learned that nothing was more precious than water and power. His father used to set an alarm clock that he might rise every two hours and patrol the orchard to keep gophers from tunneling into his irrigation ditches. It takes two tons of water to produce the wheat in a one-pound loaf of bread, and before the hydroelectric development of the Columbia, the power to pump that water was prohibitively expensive. Grand Coulee began a process of transformation. It raised a storage lake, and provided the energy to boost water up into a network of prehistoric coulees and man-made aqueducts.

Hell flowered.

More than a half-million acres in the Columbia Basin have been turn into some of the most productive land in the world. Sateilite photograp show the distinctive, round alfalfa fields watered by pivoting sprinkle From high in space, on infrared film, they appear as little discs too merous to count.

"You're damn right!" said Nick Cain, whacking the countertop at Cariboo Inn. A waitress stopped off with a pot of decaffeinated coff "People don't remember the dry years. They forget what it was li When I came here there was nothing in Ephrata, nothing in Quincy, nc ing in Moses Lake. Look at the farms there now. I think the people of t region are peppier than the rest of the country. That's the way it's ways been. Every time I think I see the frontier spirit getting subjugat I turn around and see a guy plant an orchard, or raise a herd of calves drive them up into the mountains. This is the West."

At 62, a bluff, foursquare man-of-the-west with white combed-b hair and a dapper mustache, Cain has an emphatic personality that l him to whack countertops and punctuate conversations with "Your da right!" He is frank, good-humored, and loyal—perhaps to a fault. One his critics, former state senator King Lysen said: "Bob Ferguson co tell Nick Cain 3 and 3 was 20 and Cain would go to the electric chair that."

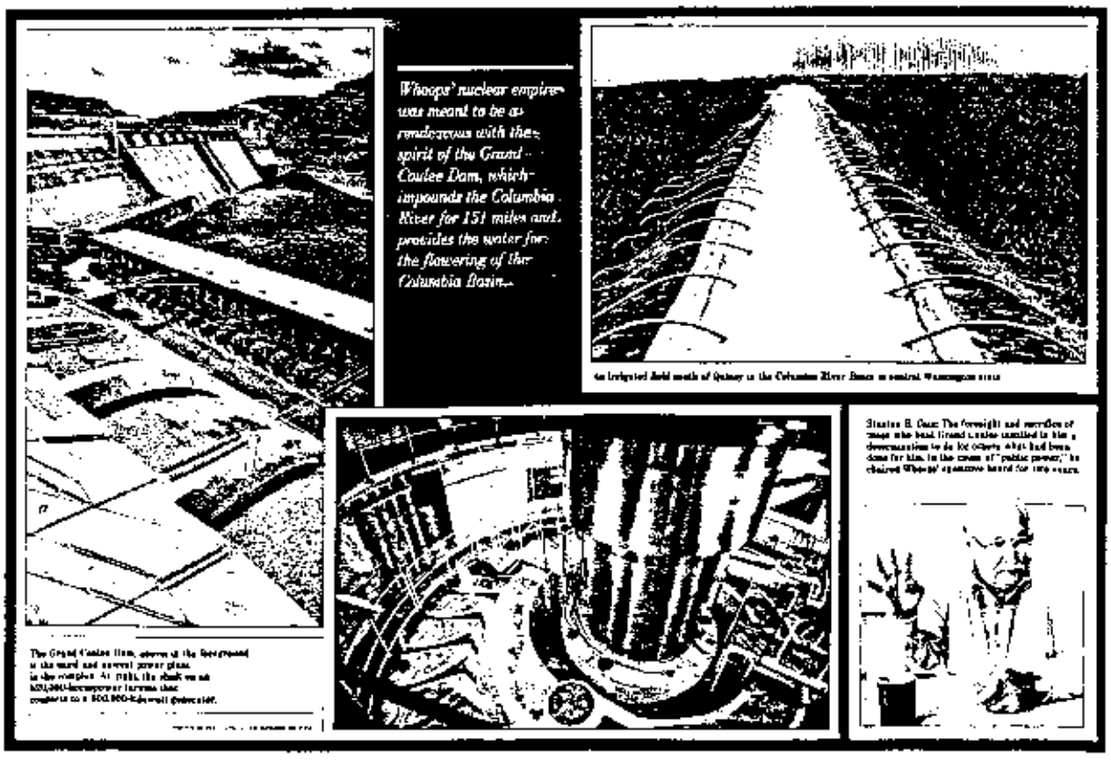
Stanton H. Cain (as he signed board resolutions) joined the board Whoops in 1976 as the representative of Okanogan County's Public U ity District No. 1. He had no idea what he was getting into. For two c cial years he served as chairman of the executive board that met ev two weeks. He drew a minuscule stipend. "I was president of the larg construction firm in the world at $38.49 a day. It was probably the wc job in the Northwest," he recalled last spring with a laugh. In 1981 compensation reached the $5,000 limit after 129 days. He worked 2 He put 52,000 miles on his blue Cadillac. His name appeared in Nor west newspapers 1,400 times.

The foresight and sacrifice of those who built Grand Coulee instille Cain a determination to do for others what had been done for him. wanted to continue the cause of "public power." In the late 1930s se out of 10 farms were without electricity in Washington state. Priv utilities wouldn't serve outlying farms. Farmers rode on horseback enroll people in public power districts. It wasn't hard to persuade fa wives scrubbing laundry by hand. They brought coffee and doughnuts work crews stringing line, and many wept when they could switch o light and enjoy what city folk took for granted.

"The people who built Grand Coulee provided power for me and generation and took the drudgery out of life," said Cain. "Everyb thought the people who developed the Columbia Basin were loony. drive through there today and there are schools and farms and hous It's beautiful."

Cain's cup jumped as a demonstrative h ..d smacked the table.

"Why the hell would I, at $38.49 a day, work my ass off? I don't o



Whoops. I don't get anything out of it. It has to be a labor of love, you're damn right! If you're going to have a future, you've got to have energy. Jesus, I'm a fly fisherman and I missed out on three or four good years of fish!"

To Cain, as to most people who linked the future to the abundant supply of electricity, the best chance seemed to lie with the fissile properties of uranium.

A President Waves His 'Atomic Wand'

The exigencies of wartime prepared the ground for the atom in Washington, "The Nuclear Progress State" as it was known on official letterhead. In 1943 farmers living near the town of Hanford along the Columbia River were evicted to make way for a top-secret atomic complex. The Hanford Engineering Works produced the plutonium that destroyed Nagasaki.

In 1957 the Washington Public Power Supply System was established just down the road in Richland. Pro-nuclear feeling is strong in Richland, and in the other communities of the Tri-Cities area where the engineers and technicians of the government-run Hanford reservation make their homes. The helmets of the Richland High School football team, the Bombers, are emblazoned with mushroom clouds. The city celebrated its incorporation by setting off a mock nuclear warhead.

"We ought to have a sign at the entrance to Hanford that says 'Bring us your harassed and unwanted nuclear plants yearning to stand tall,' " said John Goldsbury, a past president of Whoops speaking to the crowd assembled for the supply system's annual meeting in 1980.

With three employes and a storefront office, Whoops began modestly enough, building a small hydroelectric dam at Packwood Lake in the foothills of Mount Rainier. In 1964, in concert with the Atomic Energy Commission, it installed two turbine generators to harness steam furnished by a new government reactor, and produced the first nuclear-generated power in the Northwest. For more than a decade the Hanford Generating Project stood taller than any reactor in the country.

President John F. Kennedy broke ground for the Hanford Generating Project on a broiling September afternoon 21 years ago, two months before he was assassinated. It was the first time the public was able to tour Hanford. The Tri-City Herald advised women against wearing high heels in the scrub country. Kennedy's green, U.S. Marine helicopter dusted the shirtsleeved, short-haired crowd. On the podium grandees sweated in dark suits. Fortunately for the president, who had been rubbing his sore right hand after being greeted by a Basin farmer with a bone-crushing grip, his "atomic wand" was smaller than the mace Eisenhower had cradled nine years earlier. Its tip contained a piece of uranium from the first test reactor at Hanford.

"Does this thing really work?" Kennedy asked, pointing the wand at the microphone. Loudspeakers chirred. The bucket of a large red crane thudded to ground. So the nation was reminded of "the role destiny has given the Northwest to play in the transition to the nuclear age," the Wenatchee Daily World said the next day. Three years later, when power from the joint project flowed onto the grid in April 1966, Washington Sen. Henry M. Jackson stood on the floor of the Senate and declared " . . . in many ways it is a turning point in the power history of the North west."

A Fighter Waits for the Cycle to Come Round

In many ways it was, and when events came full circle less than 20 years later, they hit Nick Cain hard. He attended his first executive board meeting as ground was being broken on Project 4 in 1976. Cain heard managing director Robert L. Ferguson recommend a construction slowdown five years later, and then in January 1982, termination. As he reviewed his speech announcing the end, Cain's eyes behind his gold-framed glasses filled with tears.

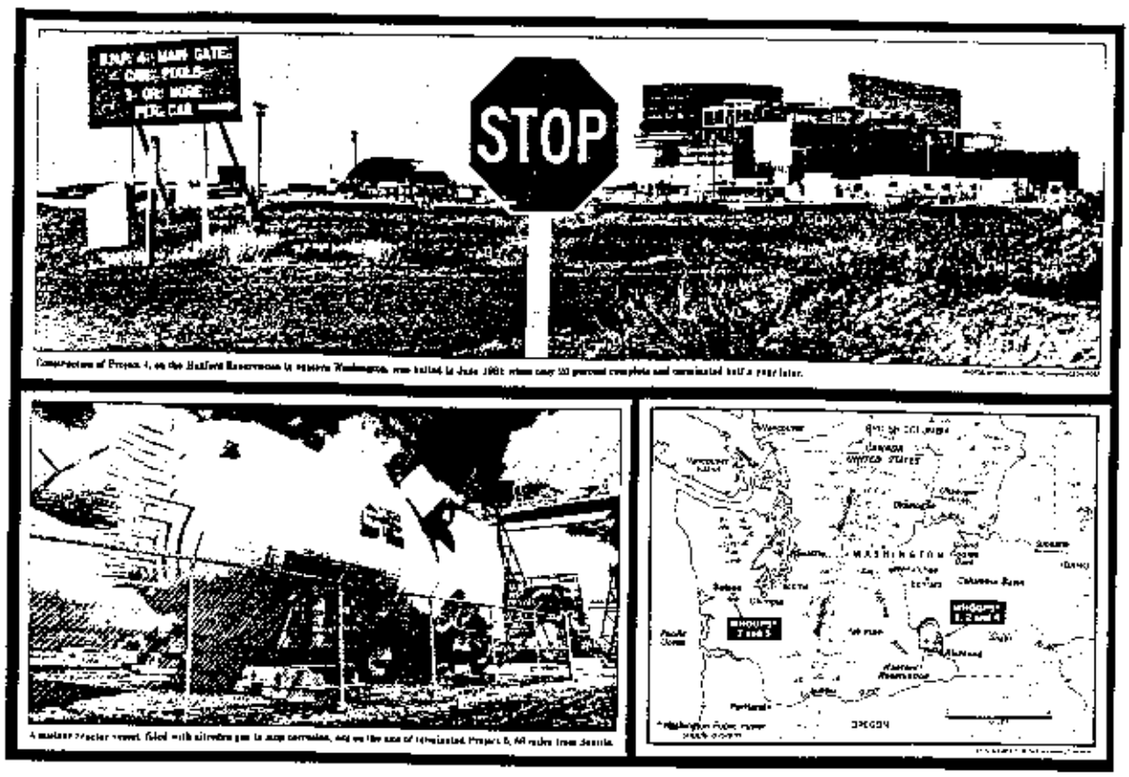
He stayed on, a self-described fighter, and in the summer of 1982 ran for reelection to the Okanogan utility district. He was opposed by a 30-year-old manager of a vocational school who was a disciple of conservation and offered a clear, philosophical break from Cain. At the time, Cain's wife was doing genealogical research and had discovered her husband was a fifth cousin of General George Armstrong Custer. "I told her, 'Play this down; it's two months before the election,' " he recalled. Suddenly overtaken by giddiness after a long day thrashing over life's complexities, he arrived good-naturedly at a simple, comic conclusion: "Custer screwed up at Little Bighorn and I screwed up at Whoops!"

Cain lost the election but not the faith. Retiring in December 1982, he received a Hamilton watch and a framed picture of an executive board meeting. Today he proudly notes his Distinguished Service Award from the Northwest Public Power Association. He believes the bondholders should be paid, and he still nourishes hope that Projects 4 and 5 will one day be built. "I guess I'm one of the crazies," he said, "I think we're going to need the power."

Between trips to the Chewack River in search of trout and to Seattle to confer with lawyers, Cain scans the monthly reports on the Cascade snow pack. The storehouse of the region's water is visible as a white mantle glittering on blue mountains over the Okanogan valley. It is easy to see from the sidewalk outside the Cariboo Inn. Some season the snow pack will have dwindled and the cycle will come round. Cain is sure of it. Farmers have long memories. In 1916 the grain was so thick harvesters could rest their scythes on its tassel tops, like a knife on a scrub brush. The cycle came round. No one forgets the fire that burned in the peat bottom of Rat Lake where 30 feet of water had stood.

Cain knows the dams will not be always overflowing. Without water to shunt through turbines, where will the power come from to entice the orchards into blossom, push the wasteland back and fashion a future? What will those sojourners say beholding dead nuclear plants? How will dawn be wrested from darkness?

"Keep watching that snow pack!" Cain shouted as he climbed into his car. "When it gets low, I'll get rid of my lawyer and we'll build the plants!"



The Washington Post

MONDAY, DECEMBER 3, 1984

Nuclear Frontiersmen Blazed Errant Trail in Northwest

New Plan Takes Conservation Route

Second of four articles

By Chip Brown
Washington Post Staff Writer

Out of the nuclear empire that was to be Whoops, there is now just one atomic plant, known officially as Project 2. It staggered across the finish line in eastern Washington state last spring after 12 years and $3.2 billion.

Anything so pervasive in the lives of more than 8½ million people certainly deserved a less prosaic name, so the publisher of a Whoops litigation newsletter held a contest. Suggestions flowed in: Spectacost II, Faulty Towers and, in memory of Whoops' four canceled or suspended sisters, E Pluribus Unum—One From Many. The winner was Moby Deuce, a witty tribute to a nuclear leviathan.

In a way Whoops was an obsessed voyage, and three contest entries remembered the man who helped launch it: Hodel II, Hodel's Hurrah, Hodel's Folly—all for U.S. Secretary of Energy Donald P. Hodel.

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As they peer toward the year 2000, energy planners in America wonder which of two paths will lead to a plentiful supply of electricity. In the tradition of the "hard path," a U.S. Department of Energy study recommends a trillion-dollar investment for building the equivalent of 438 giant nuclear power plants.

WHOOPS
PROPHETS OF SHORTAGE

Beckoning toward the "soft path," a report by the Congressional Research Service argues that power demand can be met largely by "least-cost" methods such as conservation.

The experience of the Pacific Northwest is an overture to this energy debate. The mid-1970s were a time of unprecedented economic growth in that corner of the country. The future was darkened by the prospect of huge power shortages. People had different ideas how to solve the crisis.

They defended their views with the kind of emotion that makes sense when energy is understood as an expression of deep political beliefs. Power was bound up in ideology.

Today the dispensation of power has been changed. The Northwest has struck a new course, with conservation the resource of first resort.

But the shift did not come cheaply. More money per capita was wasted on unneeded power plants there than anywhere in the country.

The multibillion-dollar lessons of Projects 4 and 5 were most expensive of all. Their shockproof buildings and useless cooling towers loom above the land in memory of a future that was prophesied but never came to pass.

An old forecasting saw warns

See WHOOPS, A18, Col. 1

Conservation Snares Atomic Behemoth

WHOOPS, From A1

that if you give a year, never give a number, and if you give a number, never give a year. In a regional version of the job he holds now, Hodel furnished numbers and years, and made them the basis of a crusade.

The Duke of Kilowatts

Today he has some doubts about the wisdom of that program, but back then, more than a decade ago, when the world looked much different, he had none. At the time, Hodel was head of the Bonneville Power Administration, a federal agency set up to distribute hydroelectricity from the great dams of the New Deal. The BPA administrator is a leading light in Northwest power circles, a Duke of Kilowatts wielding broad authority to fix rates, back bonds and control the flow of juice to paper mills, aluminum plants, irrigation districts and more than 100 public and private utilities.

Portland-born, Harvard-educated Hodel, a lean, athletic man with deep-set eyes and brows as dark as a blacked-out town, took charge of Bonneville in 1972. He faced more than his share of hardships. BPA transmission towers were blown up by an extortionist, and Hodel's life was threatened. He sometimes left a pebble on the hood of his car to make sure no one had tampered with the engine. In a personal tragedy, his eldest son, Paul, took his own life.

During his tenure, Hodel became the chief promoter of a sweeping regional energy plan to build a fleet of nuclear and coal-fired power plants. He painted a grim picture of the economic consequences the region would suffer were the so-called Hydro-Thermal Power Program thwarted.

"Homes will be cold and dark or factories will close or both because the [power] deficits are no longer manageable," he warned, echoing a note of hysteria widespread at the time. In July 1975 he appeared at Oregon's most prestigious forum to deliver an address that soon became famous in the annals of Whoops, a call to arms entitled "The Prophets of Shortage."

At a luncheon at the Portland City Club, Hodel declared that the environmental movement "has fallen into the hands of a small arrogant faction which is dedicated to bringing our society to a halt. I call this faction the Prophets of Shortage. They are the anti-producers, the anti-achievers. The doctrine they preach is that of scarcity and self-denial. By halting the needed expansion of our power system, they can bring this region to its knees."

With no franchise in the debate, no part in planning, no responsibility for constructive action, the anti-producers could run a guerrilla campaign against a dam here, a nuclear plant there, a coal-fired plant somewhere else. Hodel was accustomed to a different tradition. His father had fought an Army Corps of Engineers project in Oregon and not simply been a "spoiler" and a "negativist," but had proposed alternatives.

And so Hodel lashed out at the adherents of a "new McCarthyism" who were using environmental laws to "obstruct the orderly progress of obtaining the power supply this region must have if we are to continue to provide for a reasonable life style for ourselves, our children and the generations to come."

As a phrase, the Prophets of Shortage better described Hodel than it did his adversaries. Hodel was the one who belabored the theme of shortage. In 1976, he put Bonneville's utility customers on notice: after 1983 the federal power wholesaler could no longer meet the growth in their electric loads. Hodel helped enlist the utilities who took the financial risk of building Projects 4 and 5.

Studies such as the 1978 General Accounting Office report suggested that power growth might be less, but Hodel insisted the projects were needed. Speaking as a private consultant at the Whoops annual meeting in 1980, the year regional power consumption actually *declined* and two years before it dropped dramatically, he said: "I know no responsible authorities who believe that the completion of these projects on their present or any other schedule will produce a vast amount of power in excess to the needs of this region. So what is my message? The five Supply System plants are needed—regionally, nationally and internationally."

Came the year of reckoning—1983—and the Northwest was awash in surplus power.

Under one set of views, Projects 4 and 5 seemed to be needed. Under another set, they did not. Hodel's political antithesis was Rep. James Weaver (D-Ore.), a former real estate developer with strong conservationist views and a pronounced antipathy toward the power establishment, that closed-door, close-knit group of private utilities, aluminum companies, Northwest politicians, big public utilities and Bonneville. Whoops was not alone on the hard path. The region's private utilities invested more than $700 million in four reactors of their own before cancelling them.

Now chairman of the Bonneville oversight subcommittee in Congress, Weaver condemns the federal agency for its role in what he calls "the greatest scandal in the history of the Northwest."

In the Contrary Tradition

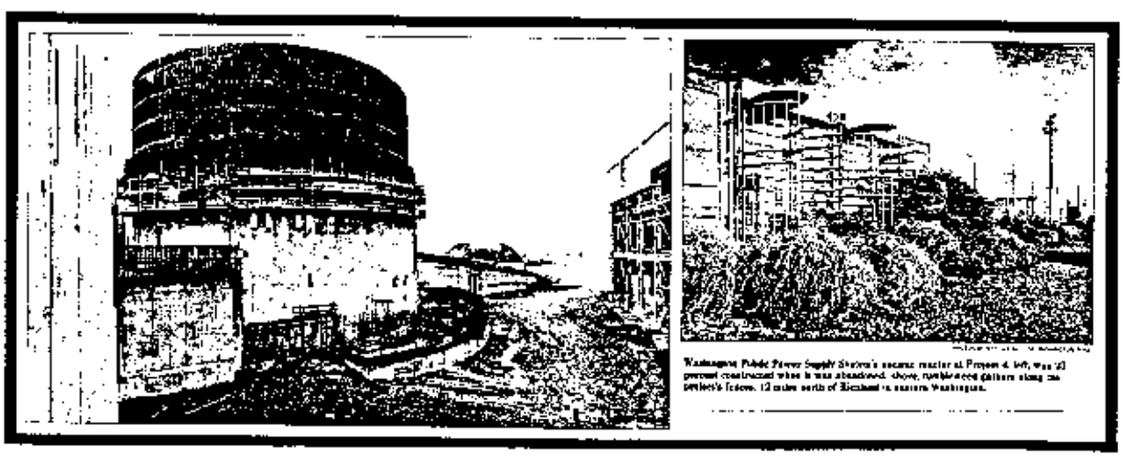
A brash, oval-faced man, Weaver keeps the contrary tradition of his populist ancestor, James B. Weaver, who got 21 electoral votes in the 1892 presidential election. Weaver calls his unpublished memoirs "Taking on the Establishment." He owns few suits and makes do without a car. He represents the most productive timber region in the country outside of Alaska, but his support for wilderness areas have made him junk wood to the timber industry. (When he shed his toupee, his staff dubbed him Clearcut.)

His hunch about Whoops was from the start, Weaver says. He was certain electricity from nuclear plants would be expensive. When the price went up, he thought, people would use less. In 1971, he narrowed the windows of one of his office projects to save money on heating bills. Conservation had enormous potential in a region that used power as profligately as the Northwest.

Weaver gathered his congressional staff in 1976: "I told them, 'We're going to do everything possible to stop these idiots before they break us. They have too much political power. We'll probably lose, but we've got to try.' I just had a gut reaction the plants weren't going to be needed."

In his prescience, Weaver was the exception (so much so that one cartoon today suggests defaulted Whoops bonds still have value if stuffed into the mouth of the gentleman from Oregon to keep him from saying, "I told you so!").

By the fall of 1980, he was under heavy pressure to quit blocking federal legislation sought by the power establishment. Aluminum companies,



which consume more than a third of the region's federal hydroelectricity, wanted new long-term contracts with BPA. The private utilities wanted access to cheap federal power for their customers. Public utilities and Wall Street wanted Bonneville to back Projects 4 and 5 and spread the financial risk of building these newest additions to the great power plan.

Weaver stood in the way.

Full-page newspaper ads paid for by private utilities and others said, "Without You, Jim Weaver, It Could Be Lights Out." In that precious phrase, Weaver was entreated to bring his vision to bear on this important issue—a polite form of "Fall in with the delegation, chowderhead!"

Weaver had declined to fall in line with the political establishment. He pressed for conservation and provisions that opened energy planning to the public. Trying to hold up the bill, he read more than 70 amendments on the floor of the House.

Given the pressure on Weaver just before the 1980 election, he was braced for a hostile reception from a brotherhood of mill workers when he stopped by a beer bust outside Coos Bay on a campaign visit. A hostile reception is no trifle in Weaver's rough-and-tumble district where bumper stickers invite Sierra Club members to Kiss My Axe, and 600 loggers once circled a courthouse with signs saying Up Weaver's Rump with a Cedar Stump.

(Oregon's Fourth District, says Weaver's longtime chief aide, Joe Rutledge, is the kind of place where "they don't even shut down the chipper at the mill when people fall in, they just put out a load of crimson wood." One of the first things a Weaver staff member learns is how to shake hands with people faring without a full set of fingers.)

Striding into the hall, the congressman was met by a crush of muscular constituents. Up stepped one, as if to proffer a pair of coconuts.

"Weaver!" he growled, "You got balls this big!"

To the congressman's amazement, the mob pressed round, not to dismember him but to slap him on the back like as if her were some sort of hero.

That moment marked the turning of the tide: ratepayers had begun to have their fill of Whoops. In 1979, when Bonneville passed its first major increase since the creation of Grand Coulee dam, the impact of Whoops hit home. As power costs went up, people began to use less and resent Whoops more. A new political force of irate consumers was born.

Mistaking Trend for Destiny

Anyone who has ever glanced at a page of power statistics will vouch that the nuances of energy forecasting are difficult to grasp, much less enjoy. Predicting power demand is still a gypsy's job, all the computer printouts aside. The crystal ball in the Northwest historically belonged to the Pacific Northwest Utilities Conference Committee, which added up the projections of more than 100 private and public utilities (40 percent of which relied on Bonneville for their figures) and issued the annual 20-year "sum of the utilities" forecast. The methods have changed, but for many years utilities charted the future by extrapolating from the past, a method sometimes likened to driving a car by looking in the rear-view mirror.

For nearly 30 years the forecasts were accurate. The Northwest's power demand climbed 7.5 percent a year. The price of electricity declined against inflation. Power companies vied to set retail rates low enough to qualify for a One Cent a Kilowatt Hour club. The trend in building new dams and power plants was, the more the merrier.

As Whoops labored on five plants, these happy circumstances began to unravel. The regional forecast of demand proved to be greater than what demand actually was. By the late 1970s, the margin of error was 10 percent, a huge overestimation when extended over the 12 to 14 years it takes to bring nuclear power to bedroom wall sockets. From 1974 to 1981, the forecasted growth rate dropped by an equivalent of a dozen Whoops plants. The further Whoops got with its five, the weaker became the reason for building them.

What made the load projections so high and unreliable? In essence, the forecasters mistook trend for destiny. History is riddled with economic downturns, but utilities have been hard-pressed to plan for anything but boom times.

It was politically more acceptable to build too much than too little, and until recently there had never been a penalty for guessing high. Demand kept catching up with bullish estimates. Bonneville and Northwest utilities alike used population figures that were were exceptionally optimistic—higher in some cases than the U.S. Census Bureau's, according to court papers. A region with a population not much bigger than the five boroughs of New York City was forecast to need more electricity in 1995 than the entire country consumed in 1950.

The forecasts also took little account of the impact of price on the demand for power. The power was supposed to come in at a reasonable cost. But electricity from Moby Deuce today costs 10 times more than had been estimated. As costs went up, conservation became an economical alternative.

A number of studies concluded that regional forecasts were high, beginning in 1975. Deciding it could get power cheaper through conservation, Seattle opted out of Projects 4 and 5, and tried to hire Arlo Guthrie to update Woody Guthrie's Northwest energy anthem. Numbers were symbols of political attitudes. In June 1976, the Oregon Department of Energy predicted much lower growth than the Pacific Northwest Utilities Conference Committee, a conclusion then-Director Lionel V. Topaz says cost him his job.

"The governor said the way we were going about our job was creating problems. People were unhappy with our findings," recalled Topaz, now general manager of the Emerald People's Utility District. "Electricity is the currency of economic development, and our forecast threatened the supply. The whole thing is money, that's all. The early forecasters were the messengers with the bad news that got slaughtered."

'That Men May Use It as the Air They Breathe'

It was an article of faith among utility officials that the demand for power had to be met, no matter how great. High demand was a sign of a vigorous economy and a virile outlook. Their hearts lay with Emile Zola, quoted in Whoops' 1980 annual report. The French novelist observed in 1885 that "electricity should not merely be supplied, but lavished that men may use it as the air they breathe."

To conservationists, Emile Zola on power made about as much sense as the Maginot Line. Electricity ought to be husbanded like any precious commodity, they argued. Why not find ways to wring more work out of a watt before building expensive new plants? Demand for power should not be viewed as some uncontrollable public appetite that had to be satisfied at any cost, but as a social phenomenon that could be tailored and managed by policy.

In one of the early skirmishes between conservationists and utility officials, Doug Scott of the Sierra Club and Larry Williams of the Oregon Environmental Council tried to crash a meeting in Portland attended by officials from Bonneville and private utilities. As Scott recalls it, someone

See WHOOPS, A19

Drop in Energy Use Unplugs Power Plan

WHOOPS, From A18

of their views were not welcome. Williams parked his bright orange Porsche at the far end of the lot. The license plate would have tipped off the power brokers that environmentalists were afoot: NEPA, it said.

Under the National Environmental Policy Act of 1969, the wellspring of environmental law, activists such as Scott and a group of lawyers from the Natural Resources Defense Council were trying to open up the power-planning process in the Northwest. The resources council and five environmental groups sued in 1975 to force Bonneville to study alternatives to the Hydro-Thermal plan. Hodel has never identified the Prophets of Shortage by name, but council lawyers consider themselves the suspects.

Power officials acknowledged the importance of conservation as it came into vogue, and President Jimmy Carter donned his cardigan sweater by the White House fireplace. Hodel today cites his testimony and his 1974 federal conservation award as evidence of his early support for conservation. But until the 1980 Northwest Power Act, Bonneville was chartered to promote the widest possible use of electricity, and the agency was so throughly wedded to the doctrine of "build and grow" that it backed more than $6 billion in Whoops bonds before conducting its own independent regional forecast.

And Hodel's critics contend that conservation influenced his policies hardly at all. In 1976, for instance, he denounced a BPA-commissioned study by the planning firm Skidmore, Owings & Merrill that said conservation could meet energy demand six times more cheaply than new nuclear plants, and entailed "no significant changes in life style." The draft was completed in May when Bonneville was helping to round up utility sponsors for Projects 4 and 5.

In January of 1977, the Natural Resources Defense Council concluded that two-thirds of the projected nuclear plants of the Hydro-Thermal plan could be eliminated by conservation measures. The report was novel in that it did not challenge the accepted growth rates, but focused on the use of power. To symbolize their "secret plan" to save the Northwest from its plunge into atoms, the publicity-savvy conservationists held up a piece of insulation at a press conference.

The first "alternate scenario" had little influence. In August 1980, the organization published a second, written by Ralph Cavanagh, a Yale Law School graduate who had worked at the Department of Justice for a year before finding his metier with the resources defense council in San Francisco. He argued that even with the most ebullient growth projections, conservation could save the region more than 12,000 megawatts of energy. In November 1982, Cavanagh and two colleagues wrote a third scenario, a 395-page model energy plan. Many of the ideas have been incorporated by the new Northwest Power Planning Agency.

Meanwhile, the world of energy-efficient appliances has been revolutionized. Cavanagh, 31, works amid the advances in heat-retaining film for windows, low-flow shower heads, heat pumps, high-efficiency fluorescent lights and house caulking. He notes with esoteric pleasure the new Sumitomo aluminum manufacturing process. His colleague, David Goldstein, traveled to Japan not for sushi but to have a close look at the latest superefficient Toshiba refrigerators.

Alternate scenarios and conservation studies undercut the rationale for new nuclear plants. But the friction between the power establishment and conservationists may have had something to do with their respective philosophies. A power plant is a cultural monument no less impressive than an opera house or a suspension bridge. Plaques honoring obscure officials and engineers are affixed to central generating stations nationwide. For a utility official, the legacies of house caulking and passive solar heating pale beside the glory of huge turbines innervating distant cities.

Voyage to the New World

Today the conservationists possess the franchise they sought in the energy-policy planning process. Cavanagh occasionally has lunch with Peter Johnson, the beetle-browed businessman who now sits as the Duke of Kilowatts. Johnson came in the spring of 1981 without a background in utilities. He found "a vacuum of authority," a situation unlike anything he had ever seen in the construction business. He ranged through history in search of parallels. The one that offered the most insight was how Europe was restructured after Napoleon.

Once again the demand for power is expected to outstrip the supply in seven years or so, but the whole psychology has changed. Where Hodel envisioned a wasteland, seers today are less apocalyptic. No one speaks about factories closing, homes going dark. The calm may be the confidence of planners with new flexibility—or part of the complacency that seems to have overtaken the country now that it's not fashionable to view energy as "the moral equivalent of war."

In an interview a few months ago, Hodel said the Prophets of Shortage was a departure from the cooperative style he prefers. He emphasized that nuclear power is a vital part of America's energy mix. He feared what's in store for the nation when utilities, burned by unneeded power plants, no longer include energy for industrial growth. The country seemed to be turning away from its own future, Hodel argued. Cavanagh has dismissed the DOE's hard-path report as "a blueprint for fiscal suicide." Hodel wondered if the likes of Cavanagh and Weaver had not fulfilled their own prophecies with the vigor of their opposition. The image of those lost years that sailed into his mind was of Columbus' voyage to the New World.

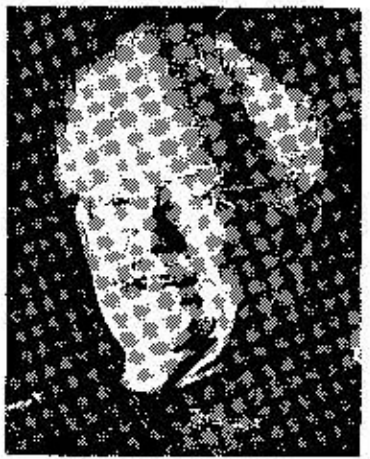
"When Columbus sailed to the New World, his crew became very concerned," Hodel said. "He feared mutiny. Through his perseverance, he went on. Of course, he didn't find India. In fact he must have been shaken. I'm sure if there had been a congressional oversight committee, one of the questions must have been, how can you justify spending the queen's money on a trip to a place that has no benefit to us?

"What Weaver's saying is, 'Now it's clear it's time to turn back, forget this New World crap, there is no such thing.' And in all honesty, he may be right. He may be right. Statistics may make him look right five years from now," Hodel said. "It's a bootstrap argument that he is able to make today. Partly because of the things he has done, and fought for, and partly because of circumstances, we've reached the situation where it looks like what he said had a lot of validity."

NEXT: The seat of sedition

The Washington Post

TUESDAY, DECEMBER 4, 1984



LEON FONNESBECK
. . . "We're fighting for our life"

Islanders Reject Nuclear Due Bill

Third of four articles

By Chip Brown
Washington Post Staff Writer

SAN JUAN ISLANDS, Wash.—These rainy green islands near the Canadian border were once home to pirates and smugglers, and to a farmer named Lyman Cutler who shot a pig and touched off a border war with the British. There is still a certain iconoclasm afoot—a provocative tradition that continues most visibly in the person of Leon Fonnesbeck, a retired lawyer and sometime playwright who led a pint-sized

WHOOPS
SEAT OF SEDITION

public utility against a giant nuclear consortium.

In the fall of 1980, the Washington Public Power Supply System was riding toward disaster without any help from Fonnesbeck. The costs of five Whoops nuclear plants were climbing like the ridgelines on Mount Rainier. Ratepayers were mad as hornets. Cartoonists had appointed Laurel and Hardy to the management team.

But for San Juan Islanders, Fonnesbeck arrived in the nick of time. The islands' electric company, Orcas Power and Light Co., had put itself at risk by agreeing to share the cost of two nuclear

See WHOOPS, A14, Col. 1

Islands' Utility Firm Draws Line Against Nuclear Consortium

WHOOPS, From A1

reactors known as Projects 4 and 5 whether they produced power or not. Two years later, when the partially completed reactors were scuttled, never to generate a watt, a formidable array of Whoops officials, financiers and political patrons said a deal was a deal—i.e., pay up. Opalco had 5,300 customers. The bill including interest came to $45 million, due over 30 years.

"The idea of paying all that money for nothing had an element of unreality about it," Fonnesbeck said one day last spring.

Three weeks after the Whoops plants were scrapped, Fonnesbeck went to work in earnest, allied with a newly militant majority on the seven-member Opalco board. In his camp: John Goodrich, a retired Boeing engineer, Charles W. (Bill) Worman, the former president of a prefab building company, and Roy Franklin, the pilot and founder of San Juan Airlines who had converted to Fonnesbeck's view after some prickly exchanges.

When push came to shove in February 1982, the tiny power company's board passed a resolution instructing its lawyer to "follow his nose" and get Opalco off the hook, making it the first of the Northwest's utilities to repudiate publicly a share of the $2.25 billion debt.

Soon Orcas Power and Light, best known until then as the only utility to hold annual meetings on a ferry boat, emerged as the catalyst of a rebellion that swept across the territory. "It was like the Boston tea party," Opalco's lawyer, Edward B. O'Connor, recalled. Greeting a special conference in April 1982, then-president Goodrich said, "Welcome to Orcas Island, the seat of sedition."

Those were feverish times. Fearing that any further effort to boost rates would backfire, reducing electric consumption and revenues, the utility took the unprecedented step of filing for bankruptcy in December 1982. As Bill Worman put it in a quote reprinted last fall in the New Yorker magazine under the heading Block That Metaphor!, in bankruptcy Opalco had found itself a "frying pan" that might "serve as a good umbrella."

To know how a little co-op obtained such a versatile item is to appreciate the course of events that led an entire region into a nuclear fiasco, and the local sense of justice and expedience that rationalized the way out. Before turmoil flowed in through the power lines, life had a decidedly more innocent flavor in the San Juans. People were more detached from mainland complexity. Frying pans were frying pans and almost no one had heard of Whoops.

People on the World of a Ship

Throughout the San Juan Islands, the sea insinuates itself in long arms and placid coves. Northern coastal weather suspends the land in fog one moment, washes it with sun the next. There are a dozen main islands and more than 150 others, many mere dollops strewn about like geologic apostrophes. Some are highly prized, but Dinner Island is said have gotten its name when its owner traded title to the land for a meal.

The islands' residents are an eclectic collection of fishermen, weavers, pilots, sailors, biologists, novelists, ex-professors, tidal wave experts, trust-fund dropouts, draft-dodgers, wealthy industrialists and specialists in out-of-body travel. In "The Roaring Land," author Archie Binns observed that the islanders have "more convictions and are better drinking men." Said Binns: "They stand out more sharply like people on the small world of a ship. [They] understand their own problems and face them more realistically."

Binns was writing in 1942, but he could have been describing Leon Fonnesbeck, a pink-cheeked, white-haired man with tufted white eyebrows curling over rimless glasses. Fonnesbeck worked as a personal injury trial lawyer in San Francisco before migrating north to the San Juans, where he planned to retire on Shaw Island. Shaw is home to 150 people, including two orders of nuns who do stand out more sharply in their habits, offloading cars and running the winch at the ferry dock like the heirs of Charon.

Fonnesbeck has a pragmatic streak that proved essential in escaping Whoops. Not one to dwell on formalities, he's been known known to shorten his name to Beck when making dinner reservations because it is easier to spell. He spends his time tending a garden, repairing clocks, practicing the violin and writing plays with large casts, including one about the adventures of Michael O'Paleglow, who discovers a secret way to make electricity. Fonnesbeck became a protagonist in the drama of Whoops in a fashion that seems peculiar to the homespun nature of local government. He stood for election to represent Shaw on the board of Opalco because it had become apparent to him that if he couldn't be bothered, nobody else could either.

Then They Said, 'Fellas, You're in Luck'

Orcas Power and Light was organized by islanders in 1937 under the federal Rural Electrification Administration, a New Deal agency created when one U.S. farm in 10 had electricity. The islands were wired up to the regional power grid in 1952, and since then the federal Bonneville Power Administration has furnished virtually all of the islands' electricity via a four-mile armor-plated cable beneath the whales and fishing boats in Rosario Strait. Dirt-cheap power from Bonneville heats the soup at Dottie's A-1 diner, churns the Jacuzzi at the Rosario Resort, highlights the crucifix at the Eastsound Episcopal Church and runs the machine that makes the electronic implants used to track salmon.

The system is a precarious one, vulnerable to falling trees and boats dragging anchors over underwater cables. Island blackouts are of perennial interest. A crow shorted out the lights on Shaw and Orcas for three hours, and a picture of the bird's frazzled corpse appeared in the Opalco Beacon newsletter. When blackouts are scheduled for routine maintenance work the co-op alerts owners of word processors, such as Richard Bach, author of "Jonathan Livingston Seagull."

As a nonprofit public utility, Opalco is one of BPA's "preference" customers. It has first dibs on the power from some 30 federal dams and power plants. Private utilities selling power for profit and industrial customers such as aluminum companies (whose profits depend on a big supply of cheap hydro power) come second.

But in the spring of 1976 there was panic in the air, whipped up by Bonneville. Its charts seemed to say that in seven years the sky would fall

Charles W. (Bill) Worman in his workshop: "At the time I thought, 'They must know what they're doing.' Of course I was completely wrong."

Leon Fonnesbeck at home on Shaw Island: "It took the [Opalco] board a long time to become convinced there was a problem."

in and there would not be enough power to maintain economic growth. For the board members of Opalco, the forecasts promised the worst: people flicking their light switches and having *nothing happen.*

Roy Franklin, a trim, easygoing man with a knack for yarns, had been on the Opalco board since 1958. He was a pilot. When he settled in the islands after World War II, he founded Island Sky Ferries. (He changed the name to San Juan Airlines after a brawl with some smart alecks who wondered if Franklin and his fellow aviators were homosexuals.) At night Franklin dynamited stumps from the cow pasture serving as his airstrip. By day he hopped about the islands. Sometimes he flew pregnant women to the hospital in Bellingham, and buzzed back over the house of the anxious father to toss a roll of toilet paper from the cockpit—blue for a boy, pink for a girl. He worked hard. Once in a while the job caught up with him at dinner. He would lay his head down on the table and sleep.

In April 1976 Franklin received a letter from Bonneville advising him of a meeting that month at the Sheraton Hotel in Portland. "We consider this to be one of the most important meetings ever held between BPA and its preference customers," it said. "To further emphasize the severity of the problems we all face we have enclosed a copy of our March 1976 Power Outlook. With critical water conditions, deficits are forecast for every year." Similar letters had gone out to public utilities all over the Northwest.

It was not easy for an outfit like Orcas Power and Light to second-guess the experts. The power outlook was not pretty. It had been compiled with contributions by the region's utilities, including Opalco, but it bore Bonneville's imprimatur and, Franklin remembers, it had arrived in a Bonneville envelope. Opalco's own forecasts jibed with the regional consensus that electric demand would grow. In 1975 alone, the amount of electricity Opalco sold had jumped 14 percent.

Bonneville's administrator then, now Energy Secretary Donald P. Hodel, had done much to create the atmosphere of crisis. He mailed Opalco a letter that said: "Only by utilities signing these agreements can these generation projects be constructed on schedule required to meet the loads." There was a sense of urgency to the All Preference Customers meeting in April 1976, as Franklin remembers it.

"They wanted to know what our plans were," he recalled. "If we didn't show that we were taking an active part in covering our shortage, we might lose our preference standing. They let us hang on the hook for a while while we sweated. We looked at each other and said, 'What the hell are we gonna do?'

"Then they said, 'Fellas, you're in luck, we've got these nuclear power plants . . . .' "

Franklin knew little about nuclear power. He had read stories about submarines circling the globe nonstop, but he had no occasion to see the February 1975 issue of Technology Review, with its minatory report about cost trends in nuclear power. Instead, the region's political leaders beat the drum of impending shortages, curtailments, blackouts, people freezing in the dark.

Hodel's BPA estimated the cost of Whoops 4 and 5 at $2.4 billion at that April meeting. A regional council of public power companies insisted that little utilities had a "responsibility to the region" to participate. A week later a contract from Whoops arrived in the mail at Opalco. The co-op had 90 days to act.

One provision in the 70-page contract, clause 6 d, was as important to Wall Street as the commandments Moses brought down from Mount Sinai. It stated that Opalco would pay for the plants whether they worked or not.

George McKush, the snowy-haired lawyer who had incorporated Opalco in 1937 and served as the utility's attorney for more than 40 years, reviewed the contract and the so-called hell-or-high water provision. "I told them it was a tough contract," he recalled. "You had to read it two or three times to get what they were driving at. The board members mostly took [manager] Bob Scharnhorst's word for the meat of it."

The board of Orcas Power and Light was uneasy with the arrangement but at a loss for alternatives, Franklin remembers. While they brooded, a helicopter appeared. Franklin forgot the names of the passengers a long time ago, but not the timing and drama of the visit—Bonneville emissaries dropping in by chopper to jolly Opalco into a nuclear future. The power could be sold as surplus if Opalco didn't need it immediately, they said. Whoops had letters from the Los Angeles Department of Water and Power and others expressing an interest in buying electricity. The implication was, How could Opalco lose? So in July 1976 Opalco signed up for a share of Projects 4 and 5.

"They wanted everybody to sign that sucker," Franklin recalled ruefully.

'We Don't Have Anything to Do With These Nukes, Do We?'

The late senator Henry M. Jackson (D-Wash.) was a friend of the San Juan Islands ever since the 1946 election. Against a Republican trend, a large block of island votes carried the day for Jackson. He liked to joke that the islands were so out of touch that the people hadn't heard Republicans were fashionable. It was the same with Whoops, in many ways. News filtered to the islands like reports of a distant war, even though Opalco's manager, Bob Scharnhorst, served as an alternate on the committee of participants set up to monitor the progress of the plants. Board member Bill Worman wasn't even aware of Opalco's stake in the plants until he'd been sitting for the better part of a year. So it was throughout the Northwest. Until 1979, when Bonneville was forced to raise its rates to cover Whoops' costs, the public for the most part was uninterested.

Worman is a meticulous man, a stickler for perfection. He sits at meetings nervously clicking a pen. He moved to Orcas Island in the early 1970s, built a house on a cove favored by a great blue heron, and immersed himself in restoring Fairchild 22 airplanes. His business background was extensive. He founded a portable building company, was later forced into bankruptcy, and emerged to guide another firm onto the American Stock Exchange. In the summer of 1980 he had read and heard enough about Whoops to put furrows in his brow. He went to see Scharnhorst with a question.

"We don't have anything to do with these nukes, do we?"

There was a long pause. Then Scharnhorst replied, "Yes, we do."

"How many?" he said.

"Five."

"At the time I thought, 'They must know what they're doing,' " Wor-

See WHOOPS, A16, Col. 1

Roy Franklin at home: "It didn't take any kind of mathematician to figure how 5,300 people could dig up $45 million in the next 30 years."

Steel reinforcement bar originally intended for the Project 5 nuclear power plant is salvaged for shipment to the People's Republic of China.

Repudiation of Debt Helps to Catalyze Northwest Rebellion

WHOOPS, From A14

man recalled not long ago. "Of course I was completely wrong. I didn't know how wrong I could be."

Still, who could be sure? At the time, Sterling Munro, who had worked for two decades as Sen. Jackson's administrative assistant, had succeeded Hodel as BPA administrator. In 1980 Munro said the Northwest was in for "10 years of the damnedest shortages this region has ever seen." After one Munro speech, Worman was back in the fold, defending the projects on the grounds that the power was needed.

Leon Fonnesbeck turned him around.

"Leon was the spark plug," Worman recalled.

"Leon brought a new-wave California rebelliousness," said Cyrus Noe, the publisher of Clearing Up, a Whoops litigation newsletter.

"I came as a stranger without a utility background," said Fonnesbeck, sitting in overalls in back of his house last summer. "You could see all the problems. It was like an impending storm. It took the board a long time to become convinced there was a problem. They kept saying, 'We need the power!' But power was running out of their ears."

Fonnesbeck got copies of the participants agreement and Bood Resolution 890, and set about figuring Opalco's position. Worman had tried the same tactic himself, with less luck. "One day I said, 'Man, I'm going to sit up tonight and try and understand this. After a couple of nights, I thought, 'Oh the hell with it.' "

Of the five plants, three were backed by Bonneville, Opalco and 87 other utilities had assumed the risk of building Projects 4 and 5 after being persuaded that the plants would pay for themselves once they started producing power. When Whoops terminated the projects in January 1982, it was clear that Projects 4 and 5 would produce nothing but bad feelings. In oil parlance, they were dry holes, and Opalco bore the dry-hole risk.

At board meetings, Fonnesbeck stood with the growing crowd of ratepayers mad enough to burn utility commissioners in effigy. Environmental guerrillas had been waging a fight against Whoops for six years, but now an army was mobilizing behind them, incensed that Whoops, Bonneville, contractors, the nuclear industry, Chemical Bank and Wall Street should try to fob off a nuclear debacle on them.

Franklin found himself in the other camp with those who believed that the region's credit and good name, not to mention "the sanctity of contracts," were at stake if the ratepayers spurned debts incurred in good faith.

"I was probably as deeply steeped in the old tradition as anybody," Franklin said. "We had some new members on the board, but I thought, a deal's a deal. We had gambled, we thought it would work."

Standing before a wood stove and a portrait of a Fairchild painted by famed aviation writer Ernest K. Gann (also an island resident and former pilot for San Juan Airlines), Franklin recounted his conversations with Fonnesbeck.

"I said, 'We're caught with it.'

"Leon would say, 'Wait a minute! We've been sold a bill of goods. The little co-ops have been taken in. The aluminum companies aren't taking any risk. They came and got us by waving the flag. The trouble with you, Franklin, is that you've lived so long in an isolated area you can't see the big picture.'

"And I'd say, 'What the hell are we talking about? Jesus Christ, Fonnesbeck, you're with a bunch of buddies on a rock, you've only got one lifeboat—you're going to slip out in the middle of the night? You dirty bird!'

" 'Christ, Franklin, get off your damn rock and see what the world is about.' "

Slowly, Franklin came off his rock. "I hated to admit it," he said, "but Leon could see all these things that were happening. I disliked him with a passion to begin with, but there are large forces in the world—Wall Street, Chemical Bank—and hey, we're not gonna be one of the fall guys. It didn't take any kind of mathematician to figure how 5,300 people could dig up $45 million in the next 30 years."

Fonnesbeck drafted letters asking to rescind the agreements. He schemed legal defenses. "Whoops hadn't done what they said they would do," Fonnesbeck said. "They said a deal was a deal. What do you mean a deal's a deal? If you get married at gunpoint, it's not a deal. Then they would fall back on clause 6d. It doesn't even mention [the word] termination. Whoops was trying to twist the clause into a position that it didn't fit."

And so, the Opalco board voted to commence the legal maneuvering that today has engulfed the Pacific Northwest in the largest securities fraud suit in the country. And the utility bulletin, Opalco *Beacon*, began to refer to the "alleged debt."

A Meeting on the Water

No one is freezing in the dark on the San Juan Islands today. The all-black postcard captioned Orcas Island at Night is just a joke about the dearth of things to do after dark. The main legacy of Whoops may be the smell of wood smoke on chilly evenings. It is hard to find a house without a wood stove. Even the stove models for sale in the village of Olga seem of a piece with islander character: Resolute, Defiant, Intrepid and Vigilant. "You should add Pleasure-Loving and Inattentive," said Marcie Lund, serving pie at the Olga Cafe.

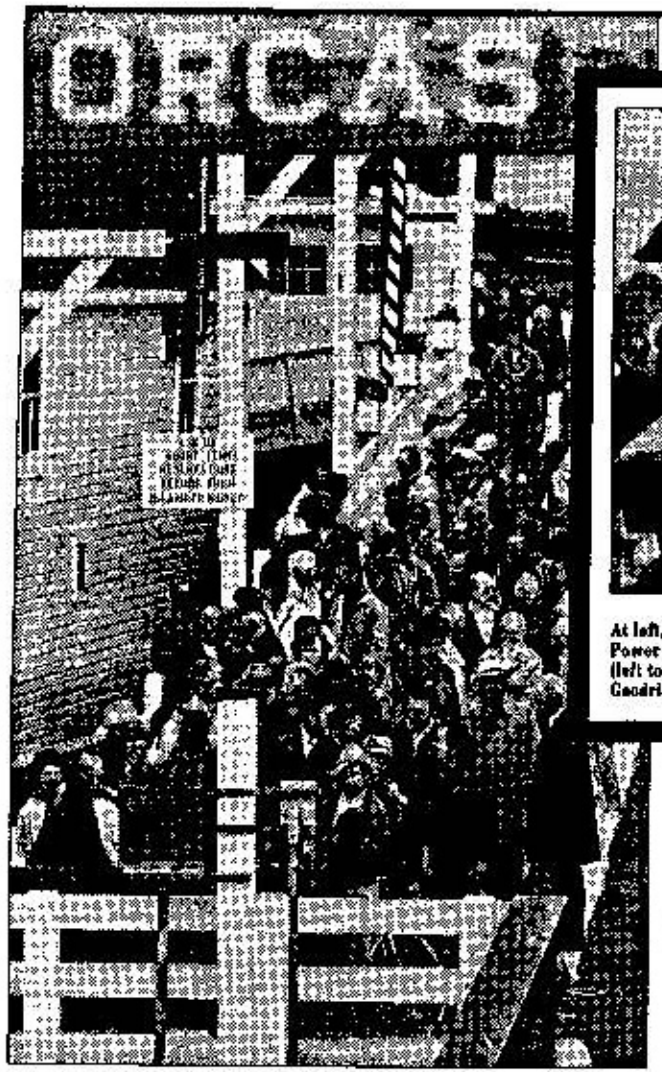
Ironically, Opalco is now promoting consumption, hoping to build demand to spread costs and keep rates down. The staff brainstormed a new bumper sticker: Save a Tree, Heat Electrically.

And Leon Fonnesbeck still inveighs against the powers behind the power. Last spring he addressed the crowd of ratepayers assembled on the ferry Kaleetan for Opalco's 47th annual meeting. The lectern had been taped to the main cabin deck to prevent it from rolling away in a rough sea. Fonnesbeck gave an impassioned speech, tying the utilities' plight in with aluminum companies, Wall Street brokerages, the oil embargo and Mideast policy. Prospects looked grim for Opalco, he said. The utility dispensed with the door prizes it used to pass out to lure members to the annual meeting. "We're fighting for our life," Fonnesbeck cried. "Let's learn some lessons. Never again should business be conducted like Whoops."

He sat down, to thunderous applause.

NEXT: Wall Street and the paper world

WHOOPS: SEAT OF SEDITION



PHOTOS AT LEFT AND ABOVE BY TOM REESE FOR THE WASHINGTON POST

At left, Orcas Island residents gather at the ferry dock for the 47th annual meeting of Orcas Power and Light Co. on board the state ferry Kalecton. Above, six of seven Opalco directors (left to right): Leon Fonnesbeck, Bill Worman, Tom Chamberlin, Howard Cole, John Goodrich and Allen Hyko. At right, Opalco linemen replace a power pole on Orcas Island.

BY RAY LUBIN — THE WASHINGTON POST

Opalco and 87 other utilities had assumed the risk of building Projects 4 and 5 after being persuaded that the plants would pay for themselves once they started producing power. When Whoops terminated the projects, it was clear that they would produce nothing but bad feelings.

The Washington Post

WEDNESDAY, DECEMBER 5, 1984

After Default, the Questions of Blame and Duty Linger

Last of four articles

By Chip Brown
Washington Post Staff Writer

NEW YORK—Though it had papered the market with billions of dollars of municipal bonds, the Washington Public Power Supply System was still an enigma on Wall Street when Howard Sitzer went to work at Merrill Lynch in the fall of 1980. Were Whoops bonds a buy? A sell? Sitzer was assigned to find out.

He was 28 at the time, a dark-haired analyst with a sober air and four new suits. As Wall Street was acquainted with Whoops mainly on paper, Sitzer set about sifting documents. He ate lunch over 20-year power forecasts and took bond resolutions home on the subway to Brooklyn. On weekends he went wading in utility "revenue streams." But through the prism of a paper world it was difficult to get an undistorted view of Whoops. Some nuance was lost in the hurly-burly of the financial markets.

Seeking a "feel for the credit," Sitzer boarded a flight for Seattle two days after New Year's. He had no inkling that the biggest municipal bond crisis in history was developing on Wall Street and that, in a matter of months, he would be in the thick of it.

WHOOPS
THE PAPER WORLD

Dear Sir: I am 62 with cardiovascular disease. When I told my wife about investing $25,000 in Whoops municipal bonds, she said to me David: Are they safe? to which I answered; Margaret this is the government of the United States. I cannot begin to tell you the anguish, the arguments, the humiliation, the frustration I had with my wife when we heard the $25,000 will not even earn interest. May God be with you ALWAYS. David Busuttil, Monrovia California.

It is often suggested that no one was to blame for Whoops. One of the great public-works projects of the century just unraveled on its own. Everyone handed responsibility on to the next guy. No one was accountable. In this sense Whoops may epitomize the whole structure of modern business and government, which seems to have evolved to spite the idea that people *are* accountable. When bureaucratic parti-

See WHOOPS, A16, Col. 1

Blame and Duty Are Lingering Issues

WHOOPS, From A1

tions separate people from a sense of having something personal at stake, and flow charts foster only narrow, legalistic notions of responsibility, society runs the risk of falling victim to itself.

The reactors known as Projects 4 and 5 were designed to withstand tornadoes, earthquakes and plane crashes—every catastrophe but a change in political climate. In June 1983 the highest court in the state of Washington wiped out contracts between Whoops and the major utilities sponsoring the plants. That reading of law by an elected tribunal turned the world upside down. It destroyed the value of bonds held by more than 78,000 people and paved the way for a $2.25 billion default. And it produced a welter of lawsuits and legal issues so complicated that allies on some points are opponents on others, and where the positions aren't clear yet they have reserved the right to sue each other—a new sort of futures market.

In essence, default poses hard questions for rival sides of America. What obligation do the ratepayers of the Pacific Northwest have to return money borrowed in their name? What duty does the financial community concentrated at the tip of Manhattan have to look beyond profits to the product it sells, and to share with investors its doubts about a deal?

"I considered what happened to be dishonorable," says Michael Satz, general counsel to the American Municipal Bond Assurance Corp., which insured $23.5 million in Whoops bonds. "It burns me up. You had a deal. The deal was understood. The money was borrowed in good faith. The people in the Northwest are not saying, 'I can't pay.' They're saying, 'I don't want to pay.' They have the cheapest electric rates in the country. While some old lady in the East is sitting in her apartment in a sweater freezing, these bastards are lit up like Christmas trees."

"You want to know who the villain in this story is? I'll tell you," says Jim McKenna, chief aide to Rep. George Hansen (R-Idaho). "The villain in this story is some guy wearing a three-piece suit, and right now he's getting out of a stretch limo on Wall Street, and he's taking the elevator to the 65th floor of some building, and he's smiling because there are boobs like me in checkered shirts who can't do anything about it. Underwriters don't work, they scheme. What the people needed was some lawyer from Boston or New York on *their* side who knew the minute these guys walked in that they were SOBs. This whole thing is kind of an American tragedy."

Your Honor: I have been swindled. I invested $30,000 in Whoops 4 and 5. The money was left by my late husband, and it represents my supplement to Social Security. I will be 65, too old to get a job, and this default leaves me outraged, frightened and helpless. Sara M. Stalvey, Deerfield Beach, Florida.

Howard Sitzer's flight to Seattle that day in January 1981 ended up in San Francisco. Aptly, given his confusion, Seattle was fogged in. Sitzer was primed for travel. After a stint in state government, he had taken after his father and found a job on "the Street" in the mid-1970s. The geography of the country aroused his curiosity; as a credit analyst, reviewing documents, he could travel widely without leaving the 34th floor at One Liberty Plaza where Merrill Lynch housed the fixed income research department. But here was a chance to flesh out the abstractions of the Paper World, to see "14-percent complete" translated as concrete and steel. Sitzer had never visited a nuclear plant, never tackled the concept of "dry hole risk" at the heart of Whoops bonds. For that matter, he'd never flown on a commuter airline. He had two weeks on expense account to explore the nuances of the biggest name in the municipal market.

"If you went to work on the street in 1977 or 1978, you'd hear that Whoops was an entity that was constructing five nuclear power plants," Sitzer recalled. "You'd shrug and say okay. Then you'd learn there was two types of financing. On three plants the Bonneville Power Administration, a federal agency, was guaranteeing the bonds, and on Projects 4 and 5 they weren't, so the bonds were rated lower. In late '79, a rumor germinated that some federal legislation was being considered that would create a similar financing structure for 4 and 5 as for 1, 2 and 3. The thought that many people had was, 'Aha! The bonds would be upgraded to triple A.' "

Indeed a new federal law passed in December 1980 offered the possibility that the bonds for Projects 4 and 5 would be bolstered by federal backing. No one was sure. Five times Sitzer read the Northwest Power Act, that year's candidate for the title of Most Complicated Law Ever Passed by Congress. If Bonneville did step in, Whoops bonds would be worth more, and Whoops could borrow money more cheaply, reducing the cost of its nuclear plants. The plants were $11 billion over budget already. But more alarming was the sense that the region's political commitment was ebbing. Some ratepayers in what was known as the Light Brigade were planning to disrupt meetings dressed as sponge-rubber light bulbs, fling Monopoly money at bond sales, and practice other extreme forms of "consumer resistance."

Without federal intervention, the projects might be doomed.

From San Francisco Sitzer flew to Seattle. He hopped over the Cascades to Richland, then down to Portland, and back to Seattle. He met with bankers, engineers and utility officials. He toured the Bonneville Dam, and stood under the reactor at Project 2. He heard many of the smaller utilities were running scared; he picked up contradictory opinions about the need for power. In the middle of his visit, the Washington State Senate published the report of its 11-month inquiry concluding that Whoops costs would continue to soar. It mentioned a study by a group called the Natural Resources Defense Council, which argued that power could be gotten more cheaply through conservation. Say what? Sitzer made a note to send for a copy. He began to formulate his thesis, expecting to have it written by the end of January.

His opinion? The federal government would *not* back Project 4 and 5 bonds, at least not anytime soon. Meanwhile the numbers boded ill. Whoops' credit rating for Projects 4 and 5 was then "investment grade" and good enough for banks to hold the bonds in portfolio, but as the costs went up, the rating seemed destined to decline toward the netherworld of "junk bonds." The implication: *Whoops could run out of a market for its bonds.* And without further bond sales, it was likely that Projects 4 and 5 would grind to a halt.

Sitzer knew to proceed cautiously. It was not just that opinions under the imprimatur of Merrill Lynch carried the influence of Wall Street's largest firm. There was a tremendous amount of money to be made from Whoops and a tremendous amount at risk already. Through its trust portfolios, Merrill Lynch had invested more than $230 million in Project 4 and 5 bonds. "The politics of the situation were explosive," Sitzer recalled. He returned with a foot-high pile of documents to begin a period he would remember as the "most exciting, condensed time of my career." The pressure was a measure of how high the stakes had become.

Dear Judge Bilby, Please, I beg of you, in the name of justice and the promise that was made when I purchased the bonds, hasten an equitable solution and fair repayment as soon as possible. I need the money now—not after I've expired. Ann Chast RN, Daytona Beach, Florida.

Since the Depression, the municipal crisis to rival Whoops was the New York City default in 1975. The inquiry report published in 1977 by the Securities and Exchange Commission offers a revealing parallel. The questions are similar; a number of the firms are the same. In both cases, the two major rating agencies, Moody's Investors Service and Standard and Poor's, maintained high ratings when conditions might have warranted otherwise. The law firm Wood & Dawson did legal work for New York City and Whoops; the SEC found fault with the extent of investigations made by the bond counsel in the New York crisis. Merrill Lynch, a major underwriter of Whoops bonds, was one of a group of New York City underwriters. The SEC said the role of underwriters in the New York City crisis "raise[s] the question of whether changes should be made in the process of conducting municipal securities offerings in the future, to assure that the underwriters are sufficiently independent and that their paramount concern will be their responsibilities to the investing public."

Again the SEC has launched a one- to three-year inquiry into a municipal fiasco, and again the question of Wall Street's responsibilities has been raised.

The issue goes to the nature of the Paper World. Before each of the 14 bond sales for Projects 4 and 5, Whoops prepared an Official Statement. The equivalent of a corporate prospectus, it was cobbled together by a committee supervised by Whoops' financial adviser, former Blyth Eastman executive Donald C. Patterson, 44. The 50-page Official Statements were filled with maps, charts, footnotes and some of the densest prose this side of the Federal Register. The details essential to bondholders were described on the cover: First, the high A-1 and A+ bond ratings; second, the agreements securing the bonds. Projects 4 and 5 were "revenue bonds," meant to be repaid from money earned by selling the power the plants produced. If the plants produced nothing, the risk fell to the 88 utilities that had obligated themselves to pay "whether or not the Projects are completed, operable or operating, and notwithstanding the suspension, reduction or curtailment of the Projects' output."

What compelled Whoops to publish an Official Statement was not any law. It was the market's demand for information. Unlike corporate securities, municipal bonds are exempt from federal regulation; nothing says underwriters share responsibility for what a public agency reveals in its disclosure documents. However, issuers *and* underwriters are bound by the general anti-fraud provisions of federal securities law—which implicitly demand that investors be given the whole story. There's the rub.

Bondholders charge that they were misled by a panoply of parties: Whoops; the 88 sponsoring utilities; the three engineering firms that did technical work; the bond lawyers who signed off on the legal arrangements; the financial adviser; the four major brokerages that led the syndicates that bought and sold Whoops bonds. Bondholders claim that the mother lode of misrepresentation was the Official Statements. Somewhere in the four-year course of Projects 4 and 5, they argue, the defen-

dants knew or should have known that the Paper World did not jibe with the real world.

"Those were the most misleading Official Statements ever written," claimed Arthur Hoffer, who invested $50,000 in Whoops bonds and is now president of a 12,000-member national committee of bondholders, based in Florida.

Defendants in the fraud cases dispute the charges. "I was there; I know the amount of time spent developing the Official Statements," said Don Patterson, who entered the bond business when he was 16. "There was a good-faith effort to come up with information that was honest and forthright. You attempt to write an O.S. as if there were a Monday-morning quarterback looking over your shoulder."

The four underwriters—Merrill Lynch, Smith Barney, Prudential Bache and Salomon Brothers—contend they relied on Whoops and its cadre of experts just as investors did, and thus were victims.

The general view of the municipal securities industry is that underwriters as a practical matter cannot—and as a matter of policy should not—second-guess the economic feasibility of more than 50,000 public agencies' projects. "Do we really want underwriters making economic determinations about what gets built and what doesn't?" asked Christopher Taylor, of the Municipal Securities Rulemaking Board, set up after the New York crisis. Independent investigation, said Taylor, is basically a matter of issuers passing the "smell test."

Dear Sir: I am retired and live on—or exist—only on the income from a few investments such as Whoops. I have no Social Security or pension payments. The loss of income from Whoops 4 & 5 has meant that I again at this late time in my life must look for some type of employment. In this area, this is almost a hopeless search. Russel Radom, Key Colony Beach, Florida.

Setting aside the issue of Wall Street's duty to scrutinize its product, how forthcoming were the Official Statements? A few conclusions are possible in advance of court findings. The portrayal of Whoops in the Official Statements seems about as comprehensible as a large canvas by Jackson Pollock. In a survey that underscores the importance of both ratings and credit analysts (who guide investors through a disclosure wilderness where only accountants and lawyers are at home), the Chicago-based Whoops Bondholders Association Inc. queried more than 1,000 bondholders and found that fewer than 2 percent even tried to read the Official Statements. Of those who did, none understood them.

It would have taken an exceptionally informed investor to spot the cheery face on sorry news in the last Official Statement issued in March 1981. It notes that Whoops has over "4,700 man hours of nuclear experience." It omits the chief conclusion of the state Senate inquiry that mismanagement was the "most significant cause" of cost overruns and delays.

Investors might have been less venturesome had they known more in a number of areas:

Economics: The projects' viability was consistently distorted in the Official Statements, according to court papers filed by Chemical Bank, the bond trustee that has brought securities fraud claims against Whoops and the sponsoring utilities. Chemical's lawyers contend that Whoops always used "optimistic" numbers. In January 1979 Whoops began conducting a "risk analysis" review of its budgets. For a year and a half, Official Statements made no mention of risk analysis, much less the findings. At times the reviews found Whoops had less than a 1 in 5 chance of meeting schedule and cost goals—a fact investors were not told.

Conservation: The potential for conservation was brushed aside, yet it was very much a part of the question of power demand that ultimately unhinged Projects 4 and 5. The October 1978 Official Statement notes that the "effect of conservation on electrical energy requirements cannot be foreseen at this time." It does not mention that two months earlier, the U.S. General Accounting Office noted that electrical growth probably would be lower than the number quoted in Official Statements, and that conservation could help meet future loads. In bond sale after sale, the Official Statements claimed that the effect of conservation could not be foreseen, while other reports suggested that its potential was huge.

Market saturation: In its report on New York City, the SEC concluded: "The deteriorating condition of the markets for the City's securities was a material fact which should have been disclosed." Whoops, too, had trouble selling its bonds, and continued sales were crucial to Projects 4 and 5. Whoops needed money not just for concrete and stainless steel pipes, but to pay for the cost of borrowing money. (More than half the money raised in the last bond sales went to pay for the cost of interest.)

Before the first Projects 4 and 5 sale in March 1977, Bonneville's financial adviser had suggested that the plants be funded under another name: many institutional portfolios had guidelines limiting the number of bonds they could carry. A February 1979 Merrill Lynch report noted the "adverse impact" of outstanding Whoops bonds. By April 1980, the problem had become so crucial that Blyth Eastman's Public Power Finance Group said in a study: "There is a real possibility that the Supply System might be unable to raise the funds it needs to maintain construction cash flow at acceptable interest rate levels, or at any interest rate at all. Obviously this situation must be avoided at all costs."

This real possibility was not broached for the benefit of investors. As in the New York City crisis, underwriters considered the problem a marketing challenge. Given the equilibrium between fear and greed, the market's appetite might be restored if Whoops were willing to pay enough in the form of higher interest rates.

Legal authority: The Official Statements included a letter from Wood & Dawson saying that the law firm had examined and approved 72 of the 88 agreements signed by utilities sponsoring Projects 4 and 5. The letter did not say that the law firm had, in fact, examined all 88, and found legal problems for 16 of the utilities, mostly from Idaho and Oregon. The Wood & Dawson firm says that the authority of the 16 is irrelevant because the utilities' share of Projects 4 and 5 was less than 3 percent of the deal, and was covered by a provision which "stepped up" the contribution of other participants if one of the bunch defaulted.

But it is on this issue of a utility's legal authority to make such a commitment that Whoops came apart. The pressure of a multibillion-dollar deal gone bad bore heavily on Wood & Dawson's Brendan O'Brien. Du

See WHOOPS, A17, Col. 1

The Villains: No One or Everyone?

WHOOPS, From A16

ing a deposition in 1982, the 43-year-old lawyer grew dizzy and had to stop testifying. Severely depressed and under a doctor's care, he left work in March 1983 and spent nine months at home in Larchmont N.Y. doing chores, reading and going for long walks. He returned to work last January.

Did Wall Street know the deal was going bad and sit idly by? Did the allow investors to be comforted by inaccurate or incomplete statements? As long as contracts secured the bonds, the financial community could argue that the paper was "money good." Indeed, as the economic rationale of the two Whoops plants faded, and hope dimmed that Projects 4 and 5 would ever have a chance to generate power, many on Wall Street embraced the unconditional promise in those contracts, like a shipwrecked crew clinging to flotsam. The issue divided the Street itself: what bearing does the economic context have on an unconditional contract? When evaluating the credit of a public agency, how much weight should be given to political questions? Such concerns sent the financial community and investors back to the analysts who had been following Whoops for years.

Dear Honorable Richard Bilby. I have completely lost confidence in brokers and all financial institutions. They are all the same and just interested in their commissions. They don't even know what they are selling and don't take five minutes of their time to study what risks or what type investment you are getting into. Jean Baron, Bethpage New Jersey.

Municipal credit analysis is not a sexy profession. There were barely two dozen of the breed on Wall Street a decade ago; the job was seen as the perfect backwater where women and minorities might start careers without disrupting the status quo. An analyst on the stock side can unearth a hot prospect and ride it to fame. Bonds are not as volatile; municipal analysts mostly uncover weaknesses in credit. So they don't earn the big salaries of traders and salesmen, or have the sort of workday that begs to be toasted at Harry's at Hanover Square, where the ceiling-mounted TV sets carry the "Daily Bond Buyer" newswire and limousines are parked outside.

The New York crisis and the tax-exempt market's growth have done much to boost the lot of a municipal analyst. Now running about $80 billion a year, the municipal market is zippier and more complex than ever; more individual investors are venturing in financial territory once dominated by insurance companies, banks and other institutions.

Long before Howard Sitzer's trip to the Northwest, analysts had been looking askance at Whoops and the premises of Projects 4 and 5. Smith Barney analysts remarked on the uncertainty surrounding the need for power in 1976, according to court papers. Jeffrey Alexopulos at T. Rowe Price began lowering his rating on Whoops bonds in September 1977 and removed them from the firm's buy list in November 1979. That year Susan Linden at Merrill Lynch questioned the rationale for the plant. Analyst Elliot Greenbaum went so far as to urge the clients of Michael L. Weisser and Co. to get out of Whoops bonds. His call was thanks largely to consultation with a Northwest economist and part-time Volkswagen mechanic named Jim Lazar.

Lazar is a signal figure in the Whoops saga. In 1979, as a graduate student in Professor Richard Frye's Economics 500 course at Western Washington State, Lazar critiqued a Whoops Official Statement, citing

examples of understated costs. The estimated price of power contained in Whoops' March 1, 1979 Official Statement was lower than the estimate contained in a letter written a day later by the managing director to a congressman. "Unless a major reevaluation took place early in the day on March 2, this unexplained increase of 15% in one day reflects an unwillingness of Whoops to update their bonds statements," Lazar wrote. His overall conclusion: utilities should cancel Projects 4 and 5.

Professor Frye gave him an A.

With characteristic cheek, Lazar, who was once denounced by a Whoops board member as a "heretic," mailed 18 copies of his report to people at major investment firms whose names he had seen quoted in The Wall Street Journal. They included the rating agencies and Whoops underwriters Merrill Lynch, Smith Barney and Salomon Brothers. Only Elliot Greenbaum replied.

Lazar says today that Wall Street analysts should have noticed by 1979 that Whoops bond statements showed a "blatant unfamiliarity" with the basic economic tenet of price elasticity. When costs of a commodity go up, people use less. But Whoops was beginning to divide municipal analysts themselves into heretics and believers. Within the professional society known as the Municipal Analysts Group of New York, people were coming to contradictory opinions by the time Howard Sitzer set out for the Northwest.

In January 1981, a 47-year-old Bear Stearns and Co. analyst named David M. Breen had published a report calling Project 4 and 5 bonds, "candidates for upgrading." He had based some of his conclusions on trends in the Washington potato harvest. Though he had been the first to call attention to the New York City crisis, Breen became a self-confessed "believer" in Whoops after the consortium hired Bob Ferguson as managing director.

In April, William H. Swann, a bond salesman who did his own research at Wertheim & Co., recommended that Projects 4 and 5 be scuttled and raised "the remote possibility" that the contracts securing the bonds might be abrogated. The brass at Wertheim were averse to publicity, Swann said recently, and the report was not widely circulated.

In a report published in May, 31-year-old Eileen Austen at Drexel Burnham Lambert ventured that the chance that the projects would be taken over by the Bonneville Power Administration was equal to the chance that they would be scrapped. Heads or tails, a risky call. Many on Wall Street were expecting Bonneville to step in and back the projects. On May 29, less than a week after her report, Austen returned from lunch to see a trader at Drexel waving a printout from the Munifacts newswire.

"I thought 'Oh God, I'm wrong, BPA must have taken them over,' " Austen recalled. "I knew I was out on a limb. When I saw what it said, I couldn't believe it. Then the phone started ringing, and it didn't stop for two years."

With "saddening shock," managing director Ferguson announced that revised estimates had hiked the price of Whoops Projects 4 and 5 by nearly $5 billion. He recommended a one-year construction slowdown. The staggering cost increase—the culmination of a six-month review—got the attention of virtually every bond analyst on Wall Street, and ensured a big turnout to hear Jim Lazar at the Downtown Athletic Club a few days later.

Lazar had not come East for the meeting, which had been scheduled at the last minute, but to help his mother with some repair around the house in Rockville. By force of habit he had packed only grubby corduroys and some Immoral Minority T-shirts (an organization he founded). That outfit, Lazar realized, would not help him get his message across to Wall Street. In the office of Rep. James Weaver (D-Ore.), Lazar buttonholed staff members, asking each: "Where did you buy that suit?"

In New York the next day, Lazar presented himself in crisp pin stripes. Joining him was fellow conservationist Ralph Cavanagh of the Natural Resources Defense Council, who called Lazar's new attire, "one of the greatest personal transformations ever made in the service of a cause." The pair focused their presentation on the conservation potential of the Northwest and the implications of the new regional power act.

Such were the dynamics of Whoops and nuclear energy on that spring morning in 1981 that Dave Breen and Lazar squared off over the energy potential of wood. Breen put some pointed questions to Lazar. Lazar parried them. It was like a boxing match. Unable to score a point, Breen tried for the knockout, with a fiendishly technical query. Lazar hesitated, then from some obscure corner of his memory retrieved the number of British Thermal Units in a cord of alder wood. Punched out, Breen sat down.

Austen thought at the time that the meeting's message made an impression on some analysts, but not on Whoops defenders. She and Sitzer treated the speakers to an expensive lunch at Michael's One restaurant. "I think we were underestimating the political impact of Whoops on the Northwest, and how important electric rates are," she recalled recently. "Whoops bonds had a kind of mystique on Wall Street."

Lazar remembers: "Lunch cost more than my suit."

Dear Sir, I am being robbed without a gun. I cannot understand how the courts cannot see this. Arletta L. Rodgers, Cape Coral, Florida.

Sitzer had planned to have his report done long before Whoops announced the nearly $5 billion increase. But he was delayed by Whoops' complexity, and other assignments. He did not begin to write in earnest until May.

At Merrill Lynch, Sitzer faced the difficulty of working on the "sell side." The firm bought bonds from Whoops and resold them to investors. Since 1972, bonds for the five Whoops projects had been sold by competitive bid, with underwriters, grouped into two huge syndicates, bidding against against each other. By May 1980, the competition had dried up. For the last five sales, the two syndicates merged. With some help on Wall Street, Whoops in late 1980 got a new state law permitting the consortium to meet with underwriters and *negotiate* the price it would receive for its bonds, rather than just toss them on the auction block. In the spring of 1981, Whoops screened investment firms to serve as underwriters in negotiated sales. Merrill Lynch was one of 15 candidates. The stakes were high. (In June, Merrill Lynch was selected to handle bond sales for Project 1 and went on to earn handsome profits in a September 1981 bond sale.)

Sitzer's report got caught in the tension between the research and underwriting departments. The goal of research is to supply objective credit analysis for the company and the investing public. The goal of a public finance department is to sell its client's bonds and keep the market

BY RAY LUSTIG—THE WASHINGTON POST

Economist Jim Lazar in his Olympia, Wash., office. In a critique he wrote in college and mailed to major investment firms, he concluded that utilities should cancel Projects 4 and 5.

upbeat. At the September bond sale, Merrill Lynch banker William W. Moore passed out "I'm bullish on the Supply System" buttons. Public finance knit deals and earned income. Research didn't. It is not surprising that bankers were reluctant to see Merrill Lynch publish a report offensive to their client.

After much internal agonizing "WPPSS: At the Crossroads" was published on July 24, 1981. Three thousand extra copies were printed. Sitzer's boss told him: "This is going to be a collector's item." If the market for Project 4 and 5 bonds had been stunned by the cost increase and slowdown announced in May, the Merrill Lynch report delivered the *coup de grace*. It said that unless 88 utilities reaffirmed their willingness to pay for the plants, the bonds could be in "serious jeopardy," a euphemism for default. As to Bonneville backing the plants—the great hope of Wall Street and Northwest utilities—the report said such a move might well undermine Projects 1, 2 and 3. Whoops never sold another bond for Projects 4 and 5.

"At the Crossroads" was Sitzer's last major work on Whoops for Merrill Lynch. Through the fall, the firm issued updates to its network of more than 8,000 salesmen. In May 1982, it hired a new municipal bond research director, Robert A. Meyer. A June 24 memo to Meyer from James M. Ruth, then managing director of public finance, summarizes "understandings" reached after a series of meetings with public finance: "It has been agreed that opinionated hard copy research will not be undertaken on securities of issuers for which Merrill Lynch serves as senior manager."

What that meant was that research such as "At the Crossroads" would not be done on Whoops or 20 senior managed clients—some of the biggest names in municipal bonds whose business had helped make Merrill Lynch the industry leader. In deference to "extreme client sensitivities," neither would Merrill Lynch do research into select municipal bond issuers who might want to hire the firm as a senior managing underwriter. It was also decided, according to the memo, that detailed reports with a credit rating were intended for institutional investors, while individual investors were to receive "suitability comments" without a credit rating.

Merrill Lynch spokesman Tom Debow said at the time of the memo Merrill Lynch was in the process of developing a new numerical rating scheme called the Investment Quality Opinion System. The firm's 21 senior managed clients were put off limits because "it would have caused confusion during the test period."

"We chose not to do quality opinion research on current senior managed issuers and on certain others with whom we were negotiating until the new system proved out," he said. Today, he said, "No clients are exempted."

"Our policy is very clear," said Sylvan G. Feldstein, now head of municipal bond research at Merrill Lynch. "We do research opinions on our own deals. No other Wall Street firm does it on their clients."

Dear Sir, I retired having worked for the same company for 49 years. A Dean Witter Reynolds broker advised a fine purchase—the above bonds which were as 'good as gold' backed by the State of Washington, Bonneville Power and the U.S. government would have to fail before you could lose anything on them. Enough said! The Washington Supreme Court decision came as the crowning blow. There is a striking parallel to this kind of decision in the Bible—perhaps you remember it—the culprit's name was Pilate. He also washed his hands of the whole affair! H.H. Ferrell, Sun Ci. Arizona.

A Whoops official testified in 1980 that the only two limits on ho much Whoops could borrow were what the financial community woul tolerate and what the public would tolerate. When the public had its fill i 1981 and tried to shut off the money with a ballot initiative that woul have given voters the right to authorize energy project bond sales, Wa Street counterattacked, led by the four underwriters. Merrill Lynch pu up $20,000, Goldman Sachs, Smith Barney and Salomon Brother chipped in $15,000 each. A roster of utilities, construction companies law firms—many with a direct financial stake in the continuation of th plants—raised $1.3 million to fight the measure. It won anyway with 5 percent of the vote. It was eventually ruled unconstitutional when applie to energy projects already under way.

After trying for six months to mothball Projects 4 and 5, Whoops ter minated the ill-starred plants in January 1982. In March 1983 the firs lawsuits were filed by bondholders. The bonds were still technically good backed by an unconditional contract, but their value in the market ha dropped as much as 40 cents on the dollar. To some dealers, they wer good speculative buys. As it turned out, the bottom was nowhere in sight The bonds skidded to about 15 cents on the dollar when the Washingto Supreme Court, on June 15, 1983, wiped out the contracts securing th bonds, and made default inevitable.

"I had to sit down; I was totally despondent," recalled Cyril Smith o Wood & Dawson, who calls the state Supreme court decision an exampl of "banana-republic jurisprudence." Said Brendan O'Brien, taking comfor in law reviews that have found "serious flaws" in the court's decision: "I every moral sense I thought those contracts were valid." Washingto Supreme Court Justice Robert F. Brachtenbach said in a speech las spring: "We're in the business of interpreting the Constitution and not i the business of selling bonds." As bond trustee, Chemical Bank plans t appeal the decision to the U.S. Supreme Court.

And so it goes. Some months ago a power failure trapped lawyer A Malanca in the federal courthouse in Seattle. The irony delighted more than a few lawyers. Malanca was on his way to a hearing to represent the Washington public utility districts at the core of Whoops. The questio can be asked: Does responsibility for what happened to people like *Davi Busuttil, Sara Stalvey, Ann Chast, Russel Radom, Jean Baron, Arlett Rodgers and H.H. Ferrell* begin with Malanca's clients—the ones wh formed Whoops in 1957, governed as members of the board, and con tracted for the bulk of the power Projects 4 and 5 will never produce?

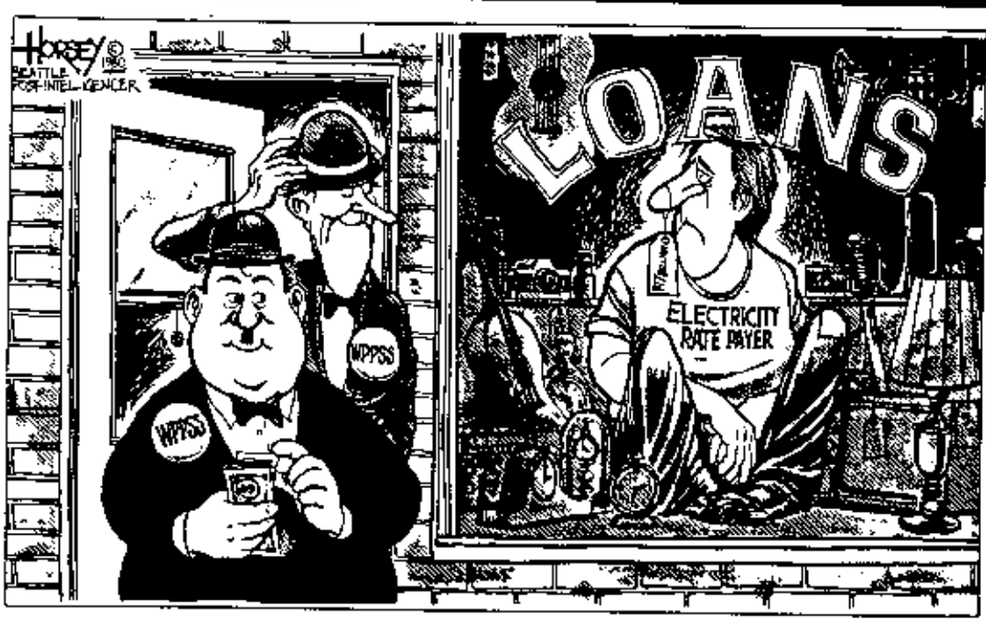
Malanca snatched the cigar out of his mouth and sprang forward in hi leather chair. The telescope in his office in downtown Tacoma wa trained on the white mantle of Mount Rainier, and on a cloudless after noon the mountain filled the window, a welcome sight vaulting over the land, above the complexity of lawsuits, beyond the Paper World.

"What do you want my people to do?" Malanca cried. "Do you wan each one of them to stand up and say, 'Yes, I was stupid enough to sig these agreements, and yes, it's okay for you to crucify me personall while Jesus Christ and all these other bastards walk?' Is that what yo want my people to do?"

The question lingered in the air.

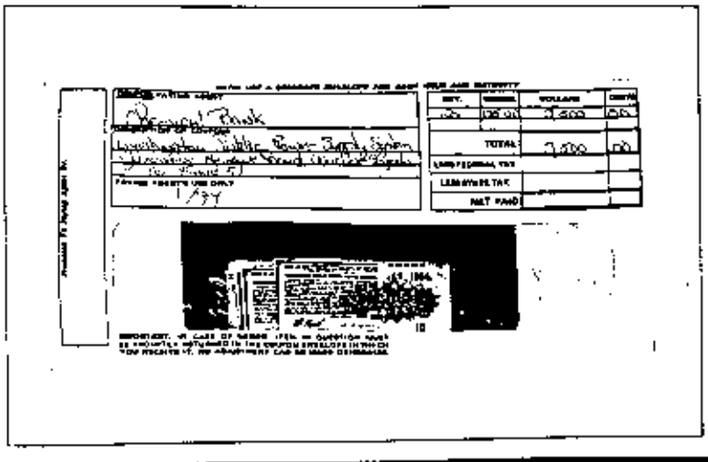
BY NANCY KAYE FOR THE WASHINGTON POST

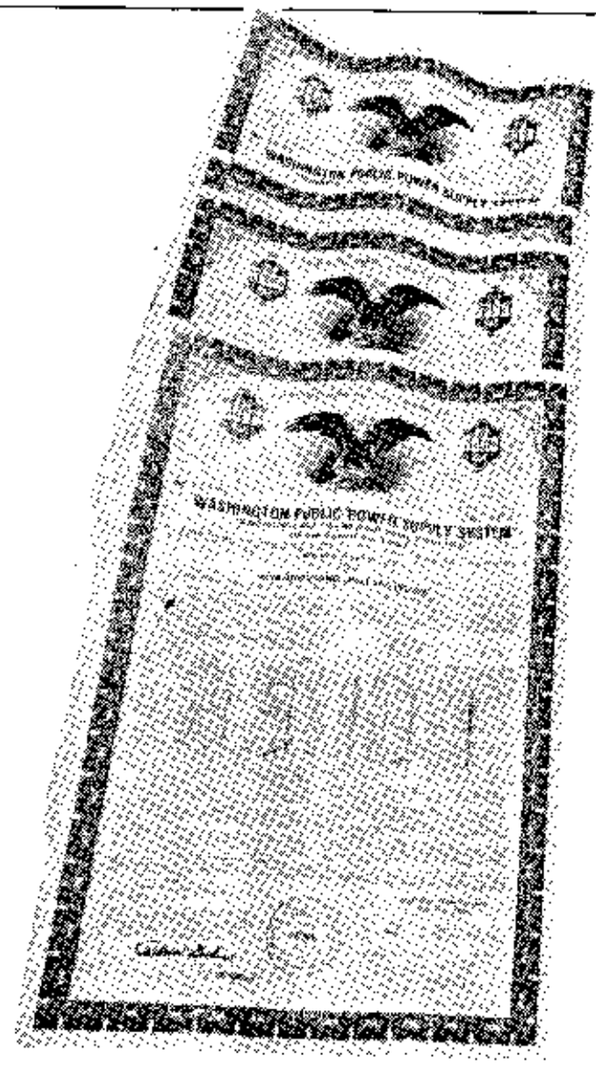
Analyst Howard Sitzer in his New York office. "The politics of the situation were explosive," recalls Sitzer, who had two weeks in the Northwest to explore Whoops for Merrill Lynch.



It is often suggested that no one was to blame for Whoops. One of the great public-works projects of the century just unraveled on its own. Everyone handed responsibility on to the next guy: No one was accountable.

CARTOONS BY DAVID HORSEY — THE SEATTLE POST-INTELLIGENCER





Nearly worthless bonds, above, and coupons, left, for Project 5.

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