

## **Restructuring in the Rearview Mirror – a 10-Year Retrospective of California's Doomed Experiment with Electric Deregulation. By The Energy Overseer**

### **Solutions and Nonsolutions**

Perhaps it's too early to pass final judgment, but it should be obvious to everyone involved that so far most of the attempts at imposing "solutions" to California's energy crisis have made matters worse instead of better.

Actions taken to date by the governor and the Legislature appear to be aimed more at bolstering their public opinion poll numbers and restoring investor confidence than at understanding and fixing the underlying causes of the problem.

By taking control over the California Independent System Operator, stacking the board with political appointees, muzzling the flow of public information and putting operational decisions in the governor's office, the state sets itself up for a dangerous confrontation with federal regulators and threatens to destroy Cal-ISO. We've already lost the Power Exchange as a meaningful market tool, direct access is all but dead, and interregional relations are precarious at best. I know the administration believes the market to be a "dangerous and colossal failure," but it seems like it is making that a self-fulfilling prophecy.

The designation of the California Department of Water Resources as purchasing agent for power is almost a joke to anyone familiar with the agency; even its employees cannot believe they are being asked to do a job for which they are ill equipped and understaffed.

The CDWR auction this week was poorly designed and oversold. Those 39 bids received will probably translate into about a dozen bidders, since several have said they sent in multiple versions, and everyone knows the state will not respect their terms but will try to arm-wrestle them into lower prices. The governor touted an "average" cost of \$69/MWh but excluded "super-peak" periods in the calculation and made no allowances for the variance between times of day.

When it all comes down, the auction results will be a minor aid to the crisis, at best repackaging power already in the system.

Meanwhile, the Legislature keeps trying to win back the confidence of credit ratings agencies and utility shareholders by mortgaging consumers' future with bonds.

The CPUC is typically schizophrenic, rushing past its own procedures and jurisdictional limits while bogging everyone down with new investigations without finishing up old ones, issuing emergency orders to address problems that don't exist, and alienating everyone in the process.

Attempts to make policy during a panic continue to be a huge barrier to finding long-term, lasting solutions. Even as we try to stanch the flow of red ink and hold the system together, we have to start working on ways to prevent this from becoming a recurring nightmare for the next two years.

The fastest and best way to get supply and demand back into balance is to work on more effective conservation programs for the summer. Some \$70 million has been allocated for peak-demand reduction, and more will be earmarked in the state budget--although we have no idea what will be proposed.

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The interruptible contracts, which are quickly depleting, must be quickly revised and renegotiated to ensure this important line of defense against blackouts. Municipal utilities are forging new types of agreements with customers that do not cause all power to be curtailed but meet "critical load" to allow business to continue even during outages. This is a model that should be instituted by all utilities.

A new "conservation ethic" must be promoted. California has begun with a plan to conserve 15 percent of peak load. That plan was required as a condition of the federal emergency order, and it must not be forgotten when the federal order expires for the last time in February. Newspapers, TV and radio can help spread the word--even at the expense of forgoing dramatic headlines in order to promote positive solutions.

If the state is serious about creating a public agency to invest in generation and transmission infrastructure, as proposed by Senator John Burton and state treasurer Phil Angelides, it must realize that taking over existing assets and making the state a big utility will cost a lot of money, does nothing to bring in new resources and may scare away projects already in the works. Rather, the emphasis must be on developing new resources and fixing transmission constraints that prevent efficient flow of energy to where it is most needed. Cal-ISO knows where the bottlenecks are.

A highly beneficial use of state money would be to put new technologies to work--real-time metering, automated energy management systems, localized generation that allows commercial customers to pull off the grid and relieve demand pressures at peak times, incentives to allow customers of all types to become their own generators.

These ideas have been around for years; it is time to put them into action.

Finally, the CPUC and Governor Davis must understand that retail prices have to be raised. Not to cover all of the utilities' claimed losses--the big utilities continue to exaggerate their true undercollections, and it has come back to haunt them by undermining confidence in their viability--but to ensure that service continues. Big write-offs by the utilities are inevitable.

It will be a tough call, guaranteed to raise ire from some quarters, but it is becoming apparent that there is no escape from some level of higher retail costs.

In the long run, the nature of California's energy market must be reexamined and a new plan devised that protects citizens while encouraging new competition for the future to overcome the mistakes made with restructuring law AB 1890.

One of the ideas gaining currency is to reinvent electric industry restructuring to look more like what was done in the gas industry. The market is split into core and non-core segments. Residential and small commercial customers remain under a traditional cost-of-service regime, served by the utilities that devote sufficient assets and resources to keeping power flowing at regulated rates. Larger customers are free to enter the competitive market by signing contracts with power marketers or other energy service firms.

Some may choose to remain under regulated service, or core-elect status. Similarly, some core customers may opt to join aggregated classes and enter the marketplace, especially if they want to access green power as a choice rather than an obligation.

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This idea is being promoted by The Utility Reform Network, which also has its hands full trying to fight off the demon of securitization of utility problems. The concept has been embraced in legislation introduced this week by state Senator Martha Escutia under the title of the Small Consumer Rate Protection Act.

There are good things and bad things about this idea, with the bad part mostly related to timing. It would have been a worthy idea five years ago as an alternative to the incompletely competitive market structure we got, but right now it looks like retribution against industrial customers that pushed for retail choice. As such, it can expect resistance from influential groups of manufacturers, agribusiness and other commercial entities, which are now also itching for rate protections.

There is probably a direct conflict between legislative attempts to save the utilities through bond issues and this Small Consumer Rate Protection Act, just as there is an unfortunate conflict between grasping for immediate fixes and forging long-term solutions.

How it all turns out will color the future of California for the next decade or more **[Arthur O'Donnell]**.

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