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

Where Do We Go from Here?

For the foreseeable future, California's electricity market will be scarred by the "crisis" events of the summer of 2000 and winter of 2001. While the conditions underlying the emergency declared exactly one year ago have passed, we all will be paying for the residual effects for at least a decade into the future.

To my mind, some of the heaviest costs are not the immediate impacts of the crisis, measured in price spikes, lost business and bankrupt utilities or market players, but the lingering liabilities of the emergency response--the heavy debts associated with power procurement, the loss of confidence in markets and market structures, the consistent compulsion of politicians to cast blame and regulators to try to reassert control over markets rather than fix the problems.

No one has come out of the emergency unscathed by the costs or untainted by recrimination for their actions, inactions or downright foolish behavior.

The question is, what can we do about it now? With the worst of the crisis behind us, and a growing body of analysis that tells us what went wrong and some educated guesses as to why, this seems to be a perfect time to look at where we've been and determine a better course for the future.

Is anyone willing to do that? I'm not entirely certain. Recently, the California Energy Commission hosted a day-long event meant to begin such a process, and while it received good presentations and entertained several valid ideas, there was practically no interest from the people and institutions that might actually do something to put those ideas to work--little representation from the Legislature and none at all from the governor's office, the California Public Utilities Commission or the California Independent System Operator.

While the CPUC has opened more than a half-dozen investigations to review various aspects of the crisis and consider policies for the future, the common threads running through them is to find someone to blame and to assert control over entities and operations where it either had been relinquished to the restructured market or had never before been exercised.

The Legislature and the governor are now occupied with other crises--both the budget emergency and the need to be reelected--and energy matters have moved to the back burners in Sacramento.

Which might be a good thing. About the best one can say about the first extraordinary session devoted to the energy crisis is that it ended, and the best thing about the second session is that virtually all the proposed legislation failed or withered away. The two dozen emergency orders issued by the governor have lapsed, although some of their pronouncements have been cemented in statute.

As a new legislative session begins, there will be a review of the past year and a half, in the context of informational hearings by the Assembly Utilities and Commerce Committee chaired by Rod Wright (D-Los Angeles). Following that review may be an opportunity to look forward, to determine what might be done to secure a more stable energy market, but more importantly, what should be done about the other great failure of the California marketplace--the continued fragmentation of policy and ill coordination among the growing body of regulatory commissions, market entities and other state agencies involved in energy.

In recent weeks, I have been conducting a series of interviews with noted economists about California's market. The work is being done at the behest of the Energy Foundation and funded by the Hewlett Foundation, which has an interest in economic and societal issues broader than the fate of the proposed Hewlett-Packard/Compaq merger.

The economists are generally familiar to readers of this newsletter and other energy policy journals:

* Paul Joskow, director of the Center for Energy and Environmental Policy Research at the Massachusetts Institute of Technology.
* Severin Borenstein, director of the University of California Energy Institute.
* Frank Wolak, professor of economics at Stanford University and chair of Cal-ISO's market surveillance committee, as well as an associate at the UCEI.
* Mark Bernstein, senior policy analyst at RAND Corporation.
* Bill Marcus, principal economist at JBS Energy.
* Robert Michaels, economics professor at California State University, Fullerton, and affiliate consultant with Tabors, Caramanis & Associates.
* And to address the practical implications of the state's response to the emergency, Dave Freeman, chair of the California Consumer Power and Conservation Financing Authority.

As might be expected, what I'm discovering from such a diverse body of thinkers is that there are no simple solutions to the problems that triggered the California blackout crisis and few areas of consensus about how to proceed in the future.

Over the next several weeks, I intend to visit some of the issues raised by these academic and practical economists, less to review what they think was wrong with California's market structure than to think about what might have been right about it and to offer ideas about what to do next and over the long term **[Arthur O'Donnell].**