

Needed: Regulation To Fit the Times

"May you live in interesting times," was the curse inscribed in my high school yearbook 20 years ago by an admired teacher of history. I felt I got off easy. In others' books she wrote, "May you get the future you deserve."

These are interesting times in the energy and utility business, and as I survey the debates over the numerous proposed national energy strategies and track regional and California developments, I often get the feeling that we are on the cusp of a new era that will offer choices never before available and that will make demands previously unforeseen. Commonly accepted practices will prove out-dated and inadequate to the tasks we face. The institutions that have traditionally ruled over the field--regulatory commissions and utility corporations--will be forced to undergo major changes.

The regulatory agencies that dominate California's energy scene--the CPUC and CEC--are also in flux. In some policy areas, like natural gas, the regulatory landscape seems to be going through an earthquake; where things will settle is unpredictable. Other changes, possibly revolutionary, are in the works.

In recent weeks, the legislative Joint Committee of Energy Regulation and the Environment issued a report that calls for both policy changes and structural changes to meet new energy needs. The most dramatic proposal, now formalized in legislation from Senator Herschel Rosenthal, is for a restructuring of these agencies, with a possible consolidation of functions into a single, new entity. The committee will hold a hearing in Sacramento to discuss the report and recommendations, and there will be great debate on the desirability of change of this sort.

By way of background to the debate, I thought it might be valuable to cast an eye to the origins of these two agencies, to better understand how they came to be what they are today.

What I discovered is that our commissions are children of two distinct historical eras that strongly influenced their behaviors. With or without the structural reform envisioned by Senator Rosenthal, they are also institutions that are bound to change with the times.

The heyday of the Progressive Movement (1900-1916) saw political reformers across the nation combating corruption and monopoly abuses by railroads, oil companies and "Big Business." Legendary Republican progressive Hiram Johnson captured the California governorship in 1910 and immediately recast the constitutionally established, but thoroughly corrupt Railroad Commission into a shield against both the railroads and newly powerful electric and gas utilities.

Of interest is the fact that the state constitution specifically places the Railroad Commission--now the CPUC--in San Francisco, a reaction to the control that special interests held over Sacramento even in those early days. The commission that evolved was not the complete answer to Progressives' dreams, but it is credited with severing an unhealthy relationship between local politicians and utilities.

The theory of utility rate regulation is essentially that of monopoly control. The eternal question is whether the agency controls the monopoly or the monopoly controls the agency. As Progressive voices were drowned out by the roar of the '20s, the politically appointed commission became a rubber stamp for utility rate and facility demands, with territory expansion justified by the incredible growth experienced in the Golden State. The agency was in step with a world that valued industry and saw utility services as an unqualified good. By today's standards, regulatory staff would be considered "sleepy rate engineers" who hardly questioned utility assumptions. If citizens objected to high rates, their only recourse was to establish municipal electric utilities, as did Los Angeles in 1925 and Sacramento in 1948.

California's more recent flirtation with progressivism came during the administration of Governor Jerry Brown, although the seeds of regulatory reform were planted during the Reagan reign. The first attempt to create an Energy Commission was vetoed by Governor Ronald Reagan in 1973, but the shock of the first OPEC oil embargo motivated the Legislature to pass the Warren-Alquist Act, establishing the CEC. Among its most valuable contributions, the CEC pioneered end-use planning models, and promoted alternatives to traditional ways of utility thinking.

The CEC was born at a time when utilities predicted unrelenting growth in electric demand and proposed a string of nuclear projects throughout the state to fill the need. The CEC first flexed its muscles when utility San Diego Gas & Electric proposed the 1300 MW Sundesert nuclear station at Blythe near the Arizona border. Agency staff attacked utility growth projections with Nader-like zeal and refuted the idea that nuclear power was the best--or even an acceptable--alternative.

Brown-appointed commissioners and their staff savored the challenge of taking on the utility and saw an opportunity to champion resource alternatives. Armed with provisions of a new state law, The Nuclear Safeguards Act of 1976, the CEC approved a notice of utility intent to build Sundesert, but imposed such stringent conditions that SDG&E abandoned the project in 1978. This seminal experience greatly shaped the CEC's later certification practices, and many power developers purposefully scaled down project size below the 50 MW limit to avoid the CEC.

The 1970s and 1980s saw similar utility/regulator skirmishes at the CPUC. Activist staff members began turning rate cases into tribunals, challenging utility assumptions and, especially, the costs of nuclear power. But their recommendations were not always accepted by commissioners, even those of a more liberal bent. In Southern California Edison's rate case for the San Onofre nuclear projects, for instance, CPUC staff proposed a \$1.7 billion cost disallowance, with the commission eventually slashing that to \$345 million. In 1986, the CPUC staff was renamed the Division of Ratepayer Advocates to better reflect its role as regulatory watchdog and to build a perceptual barrier between DRA's strident positions and the official actions of commissioners.

Although designed to oversee rates, the CPUC found that changes in the power industry outstripped traditional regulatory mechanisms. The commission

did its best to compensate with new policies to cover areas like independent power generation and "unregulated" utility affiliate development. The CPUC also bolstered other divisions such as Strategic Planning and its administrative law department, sometimes recruiting top talent from the CEC.

These two regulatory spurs have moved California and its utilities to the head of the nation in the development of wind, solar, geothermal and more efficient natural gas-fired cogeneration--reducing oil-burning to a fraction of former use and avoiding new nuclear construction. The process is contentious, but honest, and California has achieved an amazingly integrated energy grid, with no loss of reliability or pain of unbearably high rates.

Current regulatory efforts include promoting energy efficiency as a top priority, creating a market for electric and clean-fuel vehicles, breaking down transmission access constraints for independent producers and municipal utilities, fostering competition in the natural gas business and establishing environmental costs as key criteria in resource choices.

The question is whether the existing agency structures help or hinder progress toward these goals. Dan Richard, a former CEC staff member and now a principal in the consulting firm MRW & Associates, puts it this way: "We've solved the problems of the 1970s. Now the institutions need to be redefined to deal with the problems of the 1990s."

As California faces a new era, claims Senator Rosenthal, there is a critical need to create new regulatory tools to meet the changing times. The fragmented nature of energy regulation and lack of unified policy direction is cited by the joint committee as justification for structural reform. Whether the time is right to give birth to a new, consolidated, energy agency is the issue of the day. Let the debate begin, but remember the curse of history; we get the future we deserve [Arthur O'Donnell]

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