Blackouts hit California as energy crisis deepens

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After weeks of threatened power outages, California was hit by rolling electricity blackouts Wednesday afternoon affecting 500,000 people in San Francisco, Sacramento and San Jose as well as other sections of Silicon Valley. Traffic lights, ATMs, classrooms and entire neighborhoods lost power for 60 to 90 minutes amid warnings electricity supplies would be dangerously low throughout the afternoon and into the evening. The rotating blackouts, the first ordered by California authorities since World War II, were expected to continue throughout the evening, affecting up to 2 million households.

Five hundred megawatts of power from Canada had been obtained to stop the rolling blackouts until Wednesday. The state had averted blackouts on Tuesday thanks to the shutdown of massive water pumps that send water to Southern California, temporarily making 600 megawatts available.

Energy Secretary Bill Richardson extended an emergency order requiring power suppliers to sell electricity to California until midnight Tuesday. In a sign of the attitude the incoming administration would take on the issue, however, a spokesmen for President-elect George W. Bush said the crisis was not a federal, but a California problem.

Jim Detmers, managing director of the Independent System Operator—the state agency in charge of maintaining the power grid—said several power plants that had been expected to return to full operation Wednesday after repairs did not. He also said out-of-state suppliers were not selling electricity to the state because California's two largest utilities were on the verge of bankruptcy.

Last Friday, Pacific Gas & Electric (PG&E) announced a restructuring plan to shelter segments of the company from creditors, and on Tuesday Southern California Edison defaulted on nearly $600 million in payments due to power suppliers and bondholders, including $250 million in interest due on its outstanding bonds. The latter action prompted Standard & Poor's to reduce the credit ratings for both companies to junk-bond status.

The energy crisis is the product of the state's decision to deregulate energy utilities three years ago. California utilities sold off a substantial portion of their power-making capacity to out-of-state suppliers, who in turn sold energy back to the state. Contrary to the claims that the “free market” would lower energy costs and improve service, the opposite has taken place.

There is widespread evidence that suppliers—whose profits and share values in some cases have doubled and tripled since last year—colluded to restrict supply and bid up prices. The energy squeeze has also been a boondoggle for electricity traders who purchase power at lower rates by long-term contracts and resell it to realize a massive markup.

California's crisis came to a head last summer after San Diego Gas and Electric, having sold all of its power plants, passed along its wholesale costs to customers, driving up bills by 300 percent. Unable to do the same, Edison and PG&E have paid up to $1,400 a megawatt hour for electricity, while charging customers about $120. Although the companies made $6 billion from the sale of their plants and the sale of electricity into California's market from remaining facilities, company officials claim the deregulation plan requires that those profits be applied to paying off previously built facilities—and not to cover their present losses.

Last week, California Governor Gray Davis caved in to the power suppliers' extortion and proposed a plan under which the state government will purchase energy on behalf of the utilities under a long-term contract agreement. The proposal was approved by the State Assembly Tuesday night and sent to the Senate. This amounts to a state bailout of the beleaguered utilities, which may cost as much as $10 billion in public funds.

An agreement on prices and terms is yet to be arrived at, however. The governor and the legislature would like to pay no more than 5.5 cents per kilowatt-hour. The average retail price for electricity in the state is about 12 cents, the highest west of the Mississippi River, with the exception of Hawaii, and more than twice what consumers pay in Washington, Oregon and Idaho.

Earlier this month, in his annual State of the State speech, Davis made it clear that he would not allow the utilities to go bankrupt. In light of the widespread disgust with deregulation, the governor sought to distance himself from measures he supported, saying “electricity is not an exotic commodity like pork bellies, to be traded in the chaotic equivalent of a futures market,” but rather “a basic necessity of life.” He condemned what he called “a dysfunctional energy market, driven by out-of-state energy companies and brokers, that is threatening to disrupt people's lives and damage our economy.”

A series of marathon meetings throughout the week then took place between Davis, California politicians, utility and producer executives and cabinet-level government officials to arrive at the basis of a rescue package and long-term agreement. A key participant in the negotiations has been Ken Lay, chairman of Enron Corporation, a giant transnational energy company. Lay is President-elect Bush's personal representative in the negotiations.

The agreement would have to provide debt payment relief for the utilities and a multi-year contract between producers and the state at reasonable prices of 5.5-9.0 cents per kilowatt, down from the current 40-60 cent range, but substantially higher than last year's 3.5 cents. The generators are resisting the 5.5 cent rate, proposed by Davis, demanding prices in the 7 to 8 cent range instead. There are differences over the length of the contract, since the generators are eager to lock the state into high rates for a long time.

While there is increasing evidence that generators of electricity conspired to restrict supplies and keep prices high by closing down plants for frequent “unscheduled maintenance” procedures, there have been no serious moves to investigate the energy companies, let alone impose penalties or rebates on them.

The energy crisis is touching off widespread concern in the White House about a recession, as the impact of rising costs are felt throughout the state and, in particular, are viewed as a threat to the economic health of the state's technology center, Silicon Valley. There are reports of increasing concern among those high-tech corporations, with some considering leaving the state for North Carolina and Texas. The widespread use of routers by Internet companies makes a reliable and inexpensive source of energy very necessary. A three-hour blackout on June 14 cost Silicon Valley businesses over $100 million.

The California crisis looms over the financial health of the banking sector. On January 5, trading in shares of Bank of America was halted for half an hour on the New York Stock Exchange, as investors dumped massive amounts on rumors that the bank was in serious trouble from its credit line to Edison. Other banks that are being punished by Wall Street over their loans to the California utilities are J.P. Morgan Chase, Union Bank of California and Bank One. There are indications that the surprise half-point reduction in interest rates by the US Federal Reserve Board on January 3 was engineered to bail out the ailing financial sector.

The impact on Wall Street goes further. Shares of Edison International and Pacific Gas and Electric continue to plunge. Both utilities have laid off workers and are strapped for cash. Edison's decision not to make its interest payments and pay its suppliers on January 16 brings it closer to bankruptcy, and the state closer to a bailout using public funds.