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THE CALIFORNIA ENERGY CRISIS

PG&E Declares Bankruptcy; State's Crisis Plans Collapse

■Power: Chapter 11 filing, third-largest in history, puts the utility's fate in a judge's hands. Company says rescue talks were 'going nowhere,' but an angry Davis blames it for acting 'selfishly.'

By: TIM REITERMAN and DAN MORAIN and MITCHELL LANDSBERG
TIMES STAFF WRITERS

SAN FRANCISCO -- California's largest utility, Pacific Gas & Electric, filed for federal bankruptcy protection Friday, unraveling the state's efforts to resolve the energy crisis and effectively turning the utility's future over to a federal judge.

Caught in a vice, with its debts surpassing $9 billion and its negotiations with Davis "going nowhere," the San Francisco-based utility said it had no choice but to file for Chapter 11 reorganization.

It was the third-largest Chapter 11 filing in the nation's history, and by far the largest by a utility company. The only larger filings were those by Texaco Inc. in 1987 and Financial Corp. of America in 1998.

Under Chapter 11, the company can continue to operate while the court holds its creditors at bay. Eventually, the judge will work out a plan by which the creditors will be paid, though not necessarily the entire amount they are owed.

PG&E, which serves about 13 million people in Central and Northern California, has been squeezed ever tighter in the past year, during which the wholesale cost of electricity has risen tenfold and more. Under California's 1996 deregulation plan, the wholesale prices were allowed to rise untethered, while the rates that PG&E charged customers were held in place.

The timing of PG&E's filing prompted speculation that it was a slap at Davis, who had gone on statewide television the night before to reassure Californians he had the crisis in hand and proposing for the first time a rate hike, albeit a smaller one than the state's private utilities have sought.

Davis and PG&E Chairman Robert D. Glynn Jr. have sparred for months over how to solve the power crisis, sharply disagreeing over PG&E's need for a rate increase and Davis' plan to take over the utilities' transmission grid in exchange for the state's financial help.

Glynn left no doubt Friday about whom he blamed for the company's fix, castigating unidentified state officials--by implication, Davis--for their failure to steer the state out of its crisis.

"The negotiations that we have been involved in since last November are going nowhere. We've been negotiating in good faith," Glynn said. "We've reached agreements that have not been upheld and, over the last month, the kindest thing to say is, progress has dramatically slowed. . . . We think that the federal Bankruptcy Court is a better venue to get a deal closed."

Davis reacted angrily.

"I believe PG&E has dishonored itself and has created undue alarm among 34 million residents," Davis said, appearing grim-faced at a late afternoon bill-signing in San Diego. "They have acted selfishly and with a very narrow perspective. They have dishonored themselves."

Davis said he expects that within two or three days he will strike a deal to rescue the state's other financially strapped utility, Southern California Edison, and then negotiate with San Diego Gas & Electric. If he can complete those two deals, Davis said, he hopes the bankruptcy judge will give the state first crack at PG&E assets.

The governor said he remains intent on buying the system of high-voltage electricity transmission lines from the utilities, for roughly $7 billion. The utilities could use money from the sale to restructure their multibillion-dollar debts.

Reaction from legislators ranged widely, but at least one acknowledged that the bankruptcy filing signaled a failure by state government.

"It's really a shame that we just watched a 100-year-old company with a great history in California go under," said Assemblyman Roderick Wright (D-Los Angeles). "It's a pox on all our houses. We sit here and talk about how we need to protect the big California companies. Well, we just let one go under."

Actually, under Chapter 11, PG&E is not technically bankrupt.

However, the filing symbolized the failure of the state to solve one of the most serious economic crises in its history. And it promised to add yet another layer to the complex strata of policymakers searching for a solution.

PG&E is a subsidiary of San Francisco-based PG&E Corp., which has energy-related operations nationwide. The parent company and its other, profitable subsidiaries are effectively sealed off from the utility's Chapter 11 filing.

Assembly Speaker Bob Hertzberg (D-Sherman Oaks) said lawmakers had known from the outset that bankruptcy was a likely possibility, and had drafted legislation with that in mind. Nonetheless, Hertzberg said he was disappointed by the onset of bankruptcy.

"It's been a hard day. It's a very, very unfortunate thing for California," he said. "It doesn't send very positive signals about our economy."

Although the filing strips a good deal of power away from the state, the reaction was by no means entirely negative. In fact, many of those in the thick of the crisis believed it might offer the best answer yet to the state's problems.

The filing is "not the end of the world," said state Senate leader John Burton (D-San Francisco). "A lot of bankruptcy lawyers have said that in a way, this is the best solution because they've got money going forward, and now they just figure out how to restructure their debt."

State Sen. Jackie Speier (D-Hillsborough) said she believes that PG&E decided to file for bankruptcy protection after company officials figured they would fare better in court than in the Capitol.

"PG&E was willing to pursue the political route when it looked like they'd get what they want," Speier said. "I think they made a calculated move. I think we are better off with them in Bankruptcy Court. The lights stay on. I think a bankruptcy judge is going to act prudently and not necessarily give PG&E exactly what they want."

Stephen L. Braun, chairman and president of Sempra Energy, which owns San Diego Gas & Electric, agreed Bankruptcy Court might be the best place to fix the state's power problems.

"On the other hand," he said in an interview, "the bankruptcy of PG&E is a harbinger of higher rates in California, and obviously we're very concerned about the negative effects on the economy, the impacts on the customers. That's a sea in which we all swim."

Braun said Sempra, whose rates were allowed to float freely before being capped last summer, is in no danger of filing for bankruptcy.

Officials with Southern California Edison, which has faced difficulties similar to PG&E's, insisted that their company will not voluntarily follow PG&E's lead, but noted that the risk has increased that unhappy creditors could force the utility into Bankruptcy Court. A spokesman for a group of renewable energy producers said they may well force Edison into involuntary bankruptcy protection if the utility fails to pay the producers by April 16, as ordered by the state Public Utilities Commission.

"If we're not paid, there's almost zero chance they will not be in bankruptcy," said Kelly Lloyd, chief financial officer for Enxco Inc., which owns 2,500 windmills in Southern and Northern California.

A misty rain dampened San Francisco as PG&E officials arrived before 9 a.m. Friday at a financial district office building that houses the federal Bankruptcy Court.

The filing took place in the clerk's office on the 19th floor, just beyond metal detectors operated by U.S. marshals.

"We open our doors at 9 a.m. and they were here," said Gary Hender, manager of the Bankruptcy Court. "It took four minutes by the time the clerk got through the process." The filing was finished by 9:04.

PG&E's headquarters building was sealed as hundreds of employees arrived for work. Only those with identification cards were admitted.

Workers headed to the company auditorium to hear Chairman Glynn, but the room quickly filled. Those who were not admitted streamed back out of the building and were planning to dial into the gathering by phone.

When approached by a reporter, many refused to talk, saying they had been instructed to refer media inquiries to company spokesmen. Those who did speak refused to give their names, fearing the consequences.

Like a number of others, a senior electrical distribution employee characterized the session as "upbeat," or as upbeat as possible under the circumstances.

"The CEO was applauded for taking a stand on the energy crisis," the employee said. "It was a breath of fresh air, because it will bring [the crisis] to fruition. We want this crisis over with."

The filing brought relief to independent power producers and marketers that are owed hundreds of millions by PG&E and Edison. They said the filing will take the issue of their debt out of the political arena and into the more orderly environs of Bankruptcy Court.

"It's like an exhale, a sense of relief," said Gary Ackerman, executive director of the Western Power Trading Forum, an industry group. "I don't think that anybody felt that the governor and Legislature were meant to tackle a problem of this enormity."

Duke Energy, a major power generator, issued a statement saying it regretted that PG&E was forced to file for reorganization, but added that the filing "provides a defined process to collect our past receivables and keep PG&E in business going forward."

Duke was not among the major creditors listed by PG&E. The largest was the Bank of New York, owed $2.2 billion, followed by the California Power Exchange at just under $2 billion. The Power Exchange is a now-defunct agency--itself in Bankruptcy Court--that was intended to serve as the state's main electricity marketplace under deregulation.

"It's dueling bankruptcies," said Joseph Eisenberg, the Power Exchange's bankruptcy attorney.

Some analysts said the impact of the bankruptcy could be profound for the California economy.

Aside from the effect of higher electricity rates that could be on the way for PG&E customers, the bankruptcy will make life harder for the many people who invested in or lent money to the utility, as well as for companies that sell products or services to PG&E.

The stocks of PG&E Corp. and Edison International fell sharply in the wake of the PG&E filing.

PG&E Corp. lost 37% of its value, falling to $7.20 a share, while Edison tumbled nearly as far, by 35% to $8.25 a share, both on the New York Stock Exchange. Both were above $30 a share last year.

Stocks of PG&E's bank lenders and power suppliers also fell sharply. Investors fear that the reorganization could result in those creditors getting less than full payment for their debts--a not uncommon occurrence in a Chapter 11 reorganization, though Glynn insisted that it would not happen this time.

At the PUC, the filing set off a flurry of activity. Throughout the PUC headquarters in San Francisco's civic center, staff members were busily reading the agency's announcement and listening to a presentation for shareholders, hoping to glean insights into what the filing might mean.

From the lowest ranks to the commission itself, one of the most frequently asked questions was whether a bankruptcy judge could take action that would strip the PUC of its power to regulate retail utility rates.

Commissioner Geoffrey Brown said he was concerned that the court would "take the PUC out of the regulatory business as far as PG&E goes."

The timing of PG&E's filing was disturbing, Brown said. "This comes a day after the governor's cogent speech on this issue where he made it clear he wanted to see the utilities regain solvency," he said. "But [the filing] really undercuts the impact of that speech in a very material way."

PUC President Loretta Lynch said she heard about the filing from PG&E officials after it was completed.

"I was disappointed because we have taken extraordinary action to stabilize the utilities, and from my perspective they did not need to do this. The pieces were falling together, and PG&E made a business decision to go down a path" to Bankruptcy Court.

Lynch disputed PG&E's assertion that a rate increase requested last October would have averted the utility's financial problems. Calling PG&E's criticisms "disingenuous," Lynch noted that the commission had granted rate increases in January and March 27.

In Washington, the utility's decision to file for bankruptcy protection stoked a debate about the federal role in the state's energy crisis.

President Bush has insisted the problem is chiefly the state's to resolve. But Democratic lawmakers say the Bush administration can and should do more to stabilize electricity prices in the nation's most populous state.

Sen. Dianne Feinstein (D-Calif.) called the bankruptcy filing "a sad day" for the state. "It should not have come down to this. There is no question that it . . . makes the outlook for this summer even more precarious."

Republicans in Washington replied that the federal government stands ready to help Sacramento--but only if the state has the will to address the crisis itself.

"Let's make sure the federal government is doing everything it can to not be standing in the way," said Rep. Jerry Lewis (R-Redlands), leader of the state's GOP delegation to Washington.

There was no official reaction from the Federal Energy Regulatory Commission, which regulates wholesale power. But one panel member, William Massey, a Democratic appointee who is usually on the dissenting side of the panel's votes, called it "the result of a massive failure of policy makers at all levels to effectively respond to a crisis caused by a wildly dysfunctional wholesale electricity market."

Massey said he is concerned that PG&E's bankruptcy "will reverberate through the Western region and perhaps more broadly."

Consumer advocates reacted acerbically to PG&E's announcement--if not unhappily.

"They're kind of like a kid that says, you won't give me what I want so I'm going to hold my breath until I pass out," said Mike Florio, senior attorney with the Utility Reform Network in San Francisco.

"They promoted deregulation, they reaped the financial rewards of deregulation for 3 1/2 years, and now they and their shareholders are bearing the consequences of deregulation," said Harvey Rosenfield, president of the Foundation for Taxpayer and Consumer Rights.

Though the utilities did not propose deregulation, they did help shepherd it through the Legislature. In October 1997, Glynn, the PG&E chief, called deregulation "a huge opportunity for consumers to lower their energy costs, a huge opportunity for energy companies to prosper as national energy providers."

(BEGIN TEXT OF INFOBOX / INFOGRAPHIC) How it Began

* May 2000: Wholesale electricity prices in California's deregulated market begin surging to record levels. Pacific Gas & Electric Co. and the other big utilities ultimately rack up billions in debt, because a rate freeze prevents them from passing their costs to customers.

* December 2000: PG&E reports that since May, it has spent $6.6 billion more buying electricity than it has been allowed to collect from customers. Wall Street analysts raise doubts about the utility's ability to dodge bankruptcy.

* March 2, 2001: The utility's parent company secures a $1-billion loan to pay its own creditors but does nothing to prop up the subsidiary. Within a month, the corporation warns that it may have to write off $4.1 billion in costs that it may never recover. What's Next

* Chapter 11 will temporarily shield the company from creditors' legal claims while allowing it to continue doing business. Creditors cannot sue, seek to foreclose or take other actions to collect debts.

* Current management is allowed to stay in place to run the business, but a bankruptcy judge must approve any non-ordinary transactions, such as the sale of a substantial asset.

* The company must devise a plan to pay its debts, and creditors and the court must approve.

Source: Times research; Securities and Exchange Commission; PG&E. Researched by MALOY MOORE / Los Angeles Times and NONA YATES / Los Angeles Times.

(BEGIN TEXT OF INFOBOX / INFOGRAPHIC) Power Points

Background

The state Legislature approved electricity deregulation with a unanimous vote in 1996. The move was expected to lower power bills in California by opening up the energy market to competition. Relatively few companies, however, entered that market to sell electricity, giving each that did considerable influence over the price. Meanwhile, demand has increased in recent years while no major power plants have been built. These factors combined last year to push up the wholesale cost of electricity. But the state's biggest utilities--Pacific Gas & Electric and Southern California Edison--are barred from increasing consumer rates. So the utilities have accumulated billions of dollars in debt and, despite help from the state, have struggled to buy enough electricity. Daily Developments

Pacific Gas & Electric, California's largest utility, filed for bankruptcy, stripping state legislators of much of their control in the handling of the state's crisis and handing it to a federal judge.

More than $6 billion in bonds issued by PG&E were downgraded to "default" status by the Chicago-based Fitch Inc. credit-rating agency.

Gov. Gray Davis said he expects that within two or three days, he will strike a deal to rescue the state's other financially strapped utility, Southern California Edison. Verbatim

"It is not a slight problem now. It is way out of control. It is certainly a black mark. If Davis was toast before this, he is burnt toast today."

--Bond analyst Dan Scotto of PNB Paribas.

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Complete package and updates at www.latimes.com/power *

Times staff writers Thomas S. Mulligan in New York, Miguel Bustillo, Julie Tamaki and Nancy Vogel in Sacramento, Rich Connell, Jeffrey L. Rabin and Nicholas Riccardi in Los Angeles, and Tony Perry in San Diego contributed to this story.

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PHOTO: PG&E allowed only employees into its San Francisco headquarters.
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PHOTOGRAPHER: ROBERT DURELL / Los Angeles Times
Descriptors: Bankruptcy, Utilities - California, Pacific Gas & Electric Co, Electricity, Energy Shortages, Energy - California, Davis, Gray