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BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

Order Instituting Rulemaking to Implement the Commission's Procurement Incentive Framework and to Examine the Integration of Greenhouse Gas Emissions Standards into Procurement Policies.	Rulemaking 06-04-009 (Filed April 13, 2006)

ADMINISTRATIVE LAW JUDGES' RULING REQUESTING COMMENTS ON TYPE AND POINT OF REGULATION ISSUES

1. Summary

Today's ruling requests comments on the general type and point of regulation to be used to reduce greenhouse gas (GHG) emissions in the electricity sector. Parties are invited to file comments on the questions contained in this ruling, and any other issues they deem to be related to this topic. Parties may file comments no later than November 28, 2007 and reply comments no later than December 12, 2007.

2. General Instructions

We are requesting comments on the following issues and questions in order to address gaps currently in the record. Parties should not repeat any comments previously submitted, and should instead focus on questions and areas where they have not already provided comment. In addition, at the end of the questions, parties are asked to submit their comprehensive proposal for the general type and point of regulation for the electricity sector, taking into account

any other information provided in response to the specific questions. Parties should explain their reasons for each answer in detail.

3. Questions to be Addressed in Comments

3.1. General

Q1. What do you view as the incremental benefits of a market-based system for GHG compliance, in the current California context?

Q2. Can a market-based system provide additional emissions reductions beyond existing policies and/or programs? If so, at what level? How much of such additional emission reductions could be achieved through expansion of existing policies and/or programs?

3.2. Principles or Objectives to be Considered in Evaluating Design Options

Public Utilities Commission Staff proposes that the following principles or objectives be used to evaluate GHG program design options and to develop recommendations regarding a GHG regulatory approach. The objectives are not presented in any particular order.

- **Goal attainment:** Does the approach being considered have any particular advantages in terms of meeting overall emission reduction goals? For example, does the approach have any advantages to promoting energy efficiency, combined heat and power, or renewable energy?
- **Cost minimization:** Is the approach likely to minimize the total cost to end users of achieving a given GHG reduction target?
- **Compatibility with wholesale markets and the Market Redesign and Technology Upgrade:** What are the implications of the approach on efficient functioning of wholesale markets generally and the California

Independent System Operator day-ahead and real-time markets?

- **Legal risk:** Is the approach at greater relative risk of being delayed or overturned in court?
- **Environmental Integrity:** Does the approach mitigate or allow contract shuffling and the leakage of emissions occurring outside of California as a result of efforts to reduce emissions in California?
- **Expandability:** Would the approach integrate easily into a broader regional or national program? A related consideration is the suitability of the approach as a model for a national or regional program.
- **Accuracy:** Does the approach support accuracy in reporting and, therefore, ensure that reported emission reductions are real?
- **Administrative Simplicity:** Does the approach promote greater simplicity for reporting entities, verifiers, and state agency staff? How easy will the program design be to administer?

Q3. Do you agree with this set of objectives? Are there other objectives or principles that you wish to see included? If so, please include your recommendations and reasoning. Finally, please rank the objectives above, and any additional factors you propose, in order of importance.

3.3. Load-Based Cap-and-Trade System Design

Under a load-based approach, the regulated entities would be the retail providers of electricity to California consumers. Retail providers would be required to surrender allowances for the GHG emissions associated with all power sold to end users in California. Generators would not have a compliance obligation under this system, except possibly for exported power, as discussed in more detail below.

Q4. With a load-based cap-and-trade system, should exports from in-state generation sources be included and accounted for under the cap? Why or why not? If so, how? For example, exports could be captured in a cap-and-trade system by regulating in-state sources that export, or by counting the emissions associated with exported power, without any compliance obligation on the exporter. There may be other options as well.

Q5. How extensive do you view the threat of contract-shuffling under a load-based program, given the accessibility of clean resources within the western interconnect? What mechanisms do you propose to combat this possibility? On what basis do you support your position?

Under a load-based system, three basic options may be used to match a retail provider's load to the sources of electricity used to serve the load: (1) the use of contracts and settlements data, (2) the development of a tracking system to facilitate matching sources to loads, with unclaimed sources pooled and assigned to all retail providers for any electricity that cannot be accounted for on a specified basis, and (3) the use of a tracking system and tradable emission attribute certificates (TEAC) to ensure that all electricity is assigned.

Q6. Which of these systems best accounts for all imports? What are the advantages and disadvantages of each potential tracking system in terms of accuracy, cost of development and administration of tracking systems, costs of administration to the parties, and overall costs to ratepayers? Are there alternative tracking approaches that you would recommend, and for what reasons?

Q7. If a load-based approach is pursued, would the potential benefits of a full TEAC system be great

enough to warrant the start-up and administrative costs?

3.4. Source-based Cap-and-trade System Design Options

3.4.1. Pure Source-based (GHG Regulation of In-state Generation Only)

Under an in-state-only source-based approach, the regulated entities would be the power plants located in California that generate electricity and emit GHGs. Under such a system, electricity use associated with imports would not be directly regulated under the cap-and-trade system. Instead, other policies and programs such as energy efficiency and the Renewable Portfolio Standard (RPS) would be utilized to decrease reliance on imported GHG-intensive power sources.

Q8. Do you view this approach as compliant with Assembly Bill (AB) 32? Please support your answer.

The threat of leakage can be viewed over two time horizons: short-term and long-term.

Q9. In light of the relatively high capacity factors of carbon-intensive facilities outside the state, how extensive do you expect the short-term threat of substituting higher-carbon imports for in-state generation to be? Might this possibility be dealt with through specific program design (e.g., allocations, limiting conditions, etc.)?

Q10. Given existing procurement oversight and the prospect for a regional or federal GHG program in the foreseeable future, how extensive do you expect the threat to be of a longer-term shift of production to regions beyond the reach of a California source-based cap-and-trade regime?

Q11. If emissions associated with imported power are excluded from a cap-and-trade program, what policies beyond the existing suite of program including energy efficiency, California Solar Initiative, RPS, and Emission Performance Standard (EPS) do you recommend that California employ to achieve the necessary reductions from the electricity sector?

Q12. As the Public Utilities Commission does not currently have authority to oversee all energy efficiency and renewable procurement programs for all kinds of retail providers (investor owned utilities (IOUs), community choice aggregators (CCAs), electric service providers (ESPs), and publicly owned utilities (POUs)), which agency(ies) should fill in any gaps? Which agency should be responsible for overseeing energy efficiency and renewable procurement for POUs? Would the California Air Resources Board (ARB) have the authority to require certain energy efficiency and renewable targets be met by POUs?

Q13. What sources would a source-based system cover? Could it cover California utility-owned facilities located outside of California?

Q14. Would a strengthened EPS assist in reducing emissions due to California imports? What recommended changes would you make to the EPS?

3.4.2. Deliverer/First Seller

The term "deliverer/first seller" generally refers to the entity that first delivers or sells electricity into the electricity grid in California. For generation within California, the deliverer/first seller (the regulated entity) would be the generator, similar to a source-based system. For imported power, the

deliverer/first seller would be the entity that delivers the electricity into the California grid (the first sale within California), which could be a retail provider (an IOU, POU, ESP, or CCA) or wholesale marketer.

Q15. Please comment on the "First Seller Design Description" paper, which is Attachment A to this ruling. Does the paper accurately describe the deliverer/first seller program? If not, describe your concerns and include an accurate description from your perspective.

3.4.3. Source-based for In-state Generation, Load-based for Imports

Under this approach, the point of regulation would be the electricity generators for in-state generation and the retail providers for imported power.

Q16. Please describe in detail your view of how this option would work.

Q17. Do you support such an approach? Why or why not?

Q18. Does this approach have legal issues associated with it? Provide a detailed analysis and legal citations.

Q19. If retail providers are responsible for internalizing the cost of carbon for imported power, all power generated in-state may need to be tracked to load to avoid double regulation of in-state power. Do you agree?

Q20. If that is the case, does a mixed source-based/load-based approach offer any advantages compared to a load-based approach in terms of simplifying reporting and tracking? What if the load-based system uses TEACs? How could imports be differentiated from in-state generation in a way that

reduces the complexity of reporting and tracking compared to a load-based approach?

3.5. Deferral of a Market-based Cap-and-Trade System

In this scenario, a California-only cap-and-trade system would not be implemented for the electricity sector at this time. Instead, California would work with other Western states to develop a Western Climate Initiative cap-and-trade system and/or work toward a national cap-and-trade program. In the meantime, existing policies and programs in the electricity sector may need to be ramped up to meet the AB 32 goals.

Several variations of this option may be possible. For example, a load-based cap could still be developed for retail providers, with assignment of individual entity obligations and trading available within the California electricity sector only, but not with other sectors. A second alternative would be to develop individual entity caps (or carbon budgets) which entities could not exceed without facing penalties or fees, but not allow for any trading of allowances at this time. Another option would be to ramp up the mandatory levels of existing programs such as the energy efficiency and RPS programs to higher goals, and make all retail providers obligated to meet these additional goals, without assigning specific cap levels to individual entities.

Q21. How important is it that a cap-and-trade system be included in the near-term as part of the electricity sector's AB 32 compliance strategy?

Q22. Would your answer to Q12 be different if there is no market-based cap-and-trade system? If so, please explain.

Q23. Address the following:

- How emission reduction obligations could be met if there is no cap-and-trade system for the electricity sector,
- How increased programmatic goals would impact rates, and
- How deferral of a cap-and-trade program for the electricity sector would facilitate or hinder California's integration into a subsequent regional or federal program.

Q24. How deferral of a cap-and-trade program for the electricity sector would facilitate or hinder California's integration into a subsequent regional or federal program.

Q25. If neither a regional system nor a national system is implemented within a reasonable timeframe, should California proceed with implementing its own cap-and-trade system for the electricity sector? If so, how long should California wait for other systems to develop before acting alone?

Q26. What flexible compliance mechanisms could be integrated into a non-market based GHG emission reduction approach?

Q27. If a market-based cap-and-trade system is not implemented for the electricity sector in 2012, how would you recommend addressing early actions that entities may have undertaken in anticipation of a market?

3.6. Recommendation and Comparison of Alternatives

Q29. Submit your comprehensive proposal for the approach California should utilize regarding the point of regulation and whether California

should implement a cap-and-trade program at this time for the electricity sector. If you recommend that another approach be considered besides those detailed above, propose it here. If you recommend one of the above options, give as detailed a discussion as possible of how the approach would work.

Q29. Address and compare how each of the alternatives identified in the above questions, and the proposal you submit in response to the preceding question, would perform relative to each of the principles or objectives listed above and any other principles or objectives you propose. For each alternative, address important tradeoffs among the principles.

4. Filing Requirements

All parties filing comments or reply comments shall file them at the Public Utilities Commission's Docket Office and shall serve them consistent with Rules 1.9 and 1.10 of the Public Utilities Commission Rules of Practice and Procedure and Resolution ALJ-188. The parties shall serve their comments and reply comments on the service list for Rulemaking (R.) 06-04-009 posted at www.cpuc.ca.gov when the filings are made, and shall mail a hard copy of the filings to the assigned Commissioner and assigned Administrative Law Judges.

To support the ability of the Public Utilities Commission and the Energy Commission to develop joint recommendations to ARB, we ask that parties submit their comments and reply comments, both in R.06-04-009 and to the Energy Commission's docket 07-OIIP-01.

Procedures for submitting the filings to the Energy Commission are included here for the parties' convenience. The Energy Commission encourages

comments by e-mail attachments. In the subject line or first paragraph of the comments, include **Docket 07-OIIP-01**. When naming your attached file, please include your name or your organization's name. The attachment should be either in Microsoft Word format or provided as a Portable Document File (PDF). Send your comments to docket@energy.state.ca.us and to project manager Karen Griffin at kgriffin@energy.state.ca.us. In addition to electronic filing, **one paper copy** must also be sent to:

California Energy Commission
Docket Office, MS-4
Re: Docket No. 07-OIIP-01
1516 Ninth Street
Sacramento, CA 95814-5512

Therefore**, IT IS RULED** that:

1. As directed in this ruling, parties may file comments on the questions included in this ruling no later than November 28, 2007. Parties may file reply comments no later than December 12, 2007.

2. Parties shall file their comments and reply comments at the Public Utilities Commission's Docket Office and shall serve them consistent with Rules 1.9 and 1.10 and Resolution ALJ-188. The parties shall serve their filings on the service list for R.06-04-009 posted at www.cpuc.ca.gov when the filings are made, and shall mail a hard copy of the comments to the assigned Commissioner and the assigned Administrative Law Judges.

Dated November 9, 2007, at San Francisco, California.

/s/ CHARLOTTE F. TERKEURST
Charlotte F. TerKeurst
Administrative Law Judge

/s/ JONATHAN LAKRITZ
Jonathan Lakritz
Administrative Law Judge

INFORMATION REGARDING SERVICE

I have provided notification of filing to the electronic mail addresses on the attached service list.

Upon confirmation of this document's acceptance for filing, I will cause a Notice of Availability of the filed document to be served upon the service list to this proceeding by U.S. mail. The service list I will use to serve the Notice of Availability of the filed document is current as of today's date.

Dated November 9, 2007, at San Francisco, California.

/s/ KRIS KELLER
Kris Keller