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Date of Issuance
March 16, 2009

Decision 09-03-027

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)

ORDER DENYING REHEARING OF DECISION (D.) 08-10-037

I. INTRODUCTION

On September 27, 2006, Governor Schwarzenegger signed into law Assembly Bill No. 32 ("AB 32"), Stats. 2006, ch. 488, "The California Global Warming Solutions Act of 2006." Among many things, AB 32 requires the California Air Resources Board ("CARB") to adopt a greenhouse gas ("GHG") emissions cap on all major sources in California, including the electricity and natural gas sectors, to reduce statewide emissions of GHGs to 1990 levels. (AB 32, Stats. 2006, ch. 488, pp. 1 & 6; Health & Saf. Code, §38550.) The legislation also requires CARB to consult with all state agencies with jurisdiction over sources of greenhouse gases, including this Commission and the California Energy Resources Conservation and Development Commission ("CEC") in CARB's implementation of AB 32. (Health & Saf. Code, §38561, subd. (a) & §38562, subd. (f).) Although CARB is required to consult this Commission and the CEC, it is CARB that is charged with the implementation and enforcement of AB 32, whereby regulations involving GHG emissions in California will be designed and adopted in an open public process, and subsequently enforced as required. (See generally, Health & Saf. Code, §§38500, et seq.)

Decision (D.) 08-10-037 (or "Decision") in Rulemaking (R.) 06-04-009 represents the joint efforts between this Commission and CEC[1] in preparing recommendations on GHG regulatory strategies to present to CARB as mandated in AB 32. (D.08-10-037, p. 3.) In a collaborative proceeding, this Commission and the CEC developed and provided recommendations to CARB on measures and strategies for reducing GHG emissions in the electricity and natural gas section.

Los Angeles Department of Water and Power ("LADWP") timely filed an application for rehearing of D.08-10-037.[2] In its rehearing application, LADWP essentially challenges the policy determinations in the Decision. Specifically, LADWP argues: (1) the allowance recommendation creates a tax that violates Article XIIIA of the California Constitution ("Proposition 13"); (2) the auction structure violates Article XI, Section 5(a) ("Home Rule") of the California Constitution; (3) the allocation option that redistributes payments is unlawfully discriminatory, and thus, violates Article XIII, Section 19 of the California Constitution; (4) the decision violates Article XVI, Section 6 ("No Gifts of Public Funds") of the California Constitution; and (5) the cap and trade recommendations to the CARB reached by the joint agencies (this Commission and CEC) are not supported by the record because of modeling deficiencies and inadequate information.

Southern California Edison Company ("Edison"), San Diego Gas & Electric Company ("SDG&E"), Pacific Gas and Electric Company ("PG&E"), and Northern California Power Agency ("NCPA") filed responses. Edison, SDG&E, and PG&E oppose the application for rehearing. NCPA asks this Commission to disregard

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[1] The CEC formally adopted the "Final Opinion on Greenhouse Gas Regulatory Strategies" ("CEC Order"), filed on October 28, 2008, in its Docket #07-OII-1.

[2] LADWP also submitted essentially the same filing at the CEC, in the form of a request for reconsideration of the CEC Order. (Rehrg. App., pp. 1-2.) Because this Commission's Decision (D.08-10-037) and the CEC Order are identical in substance, LADWP raises the same issues in its rehearing application of the Decision and request for reconsideration of the CEC Order. (Rehrg. App., p. 2.) In an order adopted on February 25, 2009, the CEC denied LADWP's request for reconsideration and affirmed its Final Opinion.

arguments against allocation of emission allowances to low- and zero-GHG emitting resources in considering LADWP's rehearing application.

We have reviewed each and every allegation set forth in the application for rehearing and are of the opinion that LADWP has not demonstrated grounds for granting rehearing. Accordingly, the application for rehearing of D.08-10-037 is denied.

II. DISCUSSION

A. LADWP's rehearing application challenges regulations that have not been adopted by the CARB, and thus, the issues raised are premature and not ripe for consideration, and are presented in the wrong forum.

LADWP filed its application for rehearing pursuant to Rule 16.1 of the Commission's Rules of Practice and Procedure. (See Rehrg. App., p. 1.) Rule 16.1 is the Commission's implementation of the statutes involving applications for rehearing. (See Pub. Util. Code, §§1731 & 1732.)[3]

In its response to LADWP's rehearing application, PG&E argues that the rehearing application is a non-ripe challenge to AB 32 regulations that have not yet been adopted. (PG&E's Response, pp. 1-2.) PG&E contends that since recommendations in D.08-10-037 are merely advisory, challenges under Public Utilities Code sections 1731(b)(1) and 1732 are premature, and thus no rehearing lies. (PG&E's Response, p. 2.) By fulfilling its consultation obligations under AB 32, the Commission has committed no legal error. (PG&E's Response, pp. 2-3.)

Public Utilities Code Section 1731(b)(1) defines the requirement for filing an application for rehearing. It states, in relevant part:

> After any order or decision has been made by the commission, any party to the action or proceeding, . . . , may file for rehearing in respect to any matters determined in the

[3] Public Utilities Code section 1732 states: "The application for a rehearing shall set forth specifically the ground or grounds on which the applicant considers the decision or order to be unlawful." (Pub. Util. Code, §1732.)

> action or proceeding and specified in the application for rehearing. (Pub. Util. Code, §1731, subd. (b).)

Under the literal words of the statute, LADWP was permitted to file its application for rehearing of D.08-10-037. Since we issued a decision and LADWP was a party, the rehearing application was permissible under Public Utilities Code section 1731.

However, the issues presented in the rehearing application are prematurely raised and in the wrong forum. In its rehearing application of D.08-10-037, LADWP alleges legal error on determinations yet to be decided by CARB. By its own terms, LADWP's rehearing application purports to challenge the legality of the recommendations in D.08-10-037, "if adopted" by CARB. (See e.g., Rehrg. App., pp. 5, 8, 9, & 12.)[4]

Although D.08-10-037 is our opinion on GHG regulatory strategies, it is an order that presents advisory recommendations to CARB consistent with the provisions in AB 32. Obviously, such recommendations by this Commission do not constitute the final determinations of CARB.

AB 32 requires CARB to adopt a GHG emissions cap on all major sources in California, including the electricity and natural gas sectors, to reduce statewide emissions of GHGs to 1990 levels. (Health & Saf. Code, §38562.) Because CARB is required to consult the state agencies, the role of this Commission and the CEC is merely advisory, and the recommendations are not binding on CARB, who is required to make the determinations that will implement AB 32. (See Health & Saf. Code, §38530.)

The Decision makes it clear that our determinations constitute merely advisory recommendations, and it is CARB that will make the final decision on the reduction of state-wide GHG emissions. (See D.08-10-037, pp. 3-5.) We even

[4] LADWP also states: "If the recommendation is not changed and is adopted wholesale by the ARB, the LADWP will have no choice but to raise every available legal argument in opposition . . . ." (Rehrg. App., p. 3, emphasis added.)

acknowledge that our recommendations are not final, and might need to be revisited. (D.08-10-037, p. 5.)

Thus, it is clear that our recommendations in D.08-10-037 are not binding on CARB, and CARB is the agency charged by the Legislature under AB 32 for making the final determinations for state-wide reduction of GHG. (See e.g., Health & Saf. Code, §§38500, subd. (h) & 38510, subd. (n).) Obviously, CARB is required to make these determinations through an open public process. (AB 32, Stats. 2006, ch. 488, p. 1 [Legis. Counsel Digest]; Health & Saf. Code, §38560.)[5] During this process, all interested parties will have the opportunity to present their positions on how best to reduce GHG emissions, including whether CARB should or should not adopt these recommendations from this Commission and the CEC. Thus, the proper means for challenging the recommendations lies during CARB's open public process.

Moreover, after the CARB issues its determinations on its implementation of AB 32, any legal appeal of a CARB decision should be through the legal process governing challenges of CARB's decisions. Thus, LADWP's legal challenges to AB 32 regulations that have not been adopted by the CARB in its application for rehearing are premature and not ripe. Accordingly, LADWP's rehearing application raises premature and unripe issues, and is also in the wrong forum. Therefore, we deny this application for rehearing on procedural grounds.

B. The substantive issues raised in LADWP's application for rehearing are without merit.

Although we deny the rehearing application on procedural grounds, we believe that the substantive issues raised in LADWP's rehearing application have no merit for the reasons discussed below.

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[5] "It is the intent of the Legislature that CARB consult with state agencies, as well as consult with the environmental justice community, industry sectors, business groups, academic institutions, environmental organizations, and other stakeholders in implementing this division." (Health & Saf. Code, 38501, subd. (f); see also, AB 32, Stats. 2006, ch. 488, §1, p. 3.)

1. Since the allowance does not constitute a tax, LADWP's argument that the Decision has violated Proposition 13 has no merit.

The Decision explains the nature of a cap-and-trade program with allowances as follows:

> In a cap-and-trade program, electricity deliverers would be responsible for surrendering permits (allowances) for emitting carbon dioxide (CO2) and other GHGs equal to their actual emissions. The deliverers would obtain allowances either through administrative distributions, through auctions, or through a combination of these approaches, as discussed further in this decision. We also expect that a secondary market would develop for allowance trading. The total supply of emissions allowances would decline over time and this, in conjunction with the mandatory measures adopted by ARB, the two Commissions, and other governing entities, would ensure that the overall targets for 2020 and beyond are met. Under a cap-and-trade program, electricity deliverers would have the option of reducing their own GHG emissions or purchasing emission allowances from others who have made emissions cuts beyond their obligations, so long as the total emissions stay below the cap.

(D.08-10-037, p. 9.)

LADWP argues that the allowance allocation method recommended in the Decision, specifically the revenue creation from an allowance auction, constitutes a tax, in violation of Proposition 13 (Article XIIIA of the California Constitution). (Rehrg. App., pp. 5-8.) Proposition 13 requires that a tax can only be enacted by not less than a two-thirds vote of the Legislature.[6] Since AB 32 was enacted by less than a two-thirds vote of the Legislature, LADWP reasons that charges for an allowance via an allowance auction are equivalent to a tax, and thus, the allowances are unlawful. LADWP's argument lacks merit.

[6] See Cal. Const., art. XIIIA.

As described in the Decision,[7] the law distinguishes between a regulatory fee and a tax. Regulatory fees, unlike taxes, are imposed under the state's police power and do not require a two-thirds vote of the Legislature. Taxes are imposed for the purpose of raising revenues for general governmental purposes, whereas a regulatory fee is imposed to pay for the expense of a regulatory program or to mitigate the actual or anticipated adverse effects of the payor's action. (See *Sinclair Paint Co. v. State Board of Equalization ("Sinclair Paint")* (1997) 15 Cal. 4th 866, 874-878.) In order to be considered a regulatory fee, including a "mitigation effect" fee, any amount allocated to a payor must "bear a reasonable relationship to those adverse effects." (*Id.* at p. 870.)

Revenue generated from an allowance auction, as proposed by the Decision, conforms with the notion of a permissible regulatory fee under *Sinclair Paint.* The Decision specifically recommends that "all auction revenues be used for purposes related to AB 32" and "not . . . for General Fund purposes." (D.08-10-037, p. 236.) The sole purpose of the fee is to mitigate the adverse environmental and health effects of GHG emissions from electric generation. Moreover, the Decision specifically recommends that revenue generated from the auction of allowances be "reasonable in relationship to the adverse effects caused by the corresponding emission of GHGs." (D.08-10-037, p. 236.) Under the proposed structure, the amount a payor is required to pay is reasonable in that it will be based on the actual market value of GHG emissions determined at auction, and the amount paid will accurately reflect the degree to which the payor's activities adversely affect the environment.

LADWP insists that charges for allowances at auction must be viewed as taxes, based on its argument that revenue generated will exceed costs reasonably incurred by the state in administering AB 32.[8] This contention is speculative and ignores the

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[7] D.08-10-037, pp. 235-236.

[8] In further support of this contention, LADWP cites the following language from Speaker Nuñez's Letter, dated August 31, 2006:

(*footnote continued on next page*)

Decision's explicit recommendation that auction revenues be utilized to implement the mandates adopted by CARB as well as other GHG-reducing activities. (See D.08-10-037, pp. 225-229.) Moreover, case law supports the state's broad discretion in allocating costs of regulation. As the Court of Appeal stated in one such case:

> The legislative body charged with enacting laws pursuant to the police power retains the discretion to apportion the costs of regulatory programs in a variety of reasonable financing schemes. An inherent component of reasonableness in this context is flexibility.

(*California Association of Professional Scientists v. Department of Fish and Game* (2000) 79 Cal. App. 4th 935, 950.)

For the reasons stated above, revenues generated from an allowance auction legally constitute a regulatory fee and not a tax. Accordingly, LADWP's contention lacks merit and is rejected.

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> AB 32 authorizes the California Air Resources Board to adopt a schedule of fees for the direct cost of administering the reporting and emission reduction and compliance programs established pursuant to the bill's provisions. It is my intent that any funds [provided by these fees] be used solely for the direct costs incurred in administering this division.

(Letter from Fabian Nuñez, Speaker of the Assembly, Cal. State Assembly to Mr. E. Dobson Wilson, Chief Clerk of the California Assembly, dated August 31, 2006, Assembly Daily Journal (2005-2006 Reg. Sess.) p. 7454; available at http://www.assembly.ca.gov/clerk/billslegislature/srchframe.htm.)

According to LADWP, had Speaker Nunez believed that AB 32 included revenue generating provisions besides charges pursuant to the fee schedule, such as an auction, he would have crafted his letter to cover those too. (Rehrg. App., pp. 6-7.) This argument lacks merit. We do not contest that any fees collected must be used in furtherance of the GHG reduction program as set forth in AB 32, and the Decision's recommendations regarding an allowance auction structure are consistent with this understanding. Speaker Nunez's letter does not support the contention that AB 32 explicitly or implicitly disallows auctions as a means of generating revenue in the implementation of the legislation. Accordingly, the recommended auction structure is not inconsistent with AB 32, and LADWP's reliance on the letter in support of their contention is misplaced.

2. The proposed auction structure does not violate Article XI, Section 5(a) (Home Rule) of the California Constitution.

LADWP contends that the Decision's proposed allowance auction structure would violate its right of "Home Rule" as provided by Article XI, Section 5(a) of the California Constitution. (Rehrg. App., pp. 8-9.) This contention lacks merit.

California case law establishes three necessary steps in resolving a Home Rule controversy. First, "a court must determine whether there is a genuine conflict between a state statute and a municipal ordinance."[9] To qualify as a genuine conflict, the purported conflict must be "unresolvable short of choosing between one enactment and the other."[10] Only after concluding that a genuine conflict exists will a court proceed with the second determination: whether the state statute qualifies as a matter of statewide concern.[11] Lastly, if the state statute impacts a statewide concern, the court requires it to be "both (i) reasonably related to the resolution of that concern, and (ii) 'narrowly tailored' to limit incursion into legitimate municipal interests."[12]

LADWP here has failed to satisfy the threshold test that requires a showing of a genuine conflict. That is why we rejected this same claim in an earlier decision in this proceeding.[13] As we observed: "LADWP has not shown that any purported conflict is unresolvable short of choosing between one enactment and the other."[14]

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[9] *Cobb v. O'Connell ("Cobb")* (2005) 134 Cal. App. 4th 91, 96, citing *Barajas v. City of Anaheim ("Barajas")* (1993) 15 Cal.App.4th 1808, 1813.

[10] *California Federal Savings & Loan Association v. City of Los Angeles* (1991) 54 Cal.3d 1, 16-17.

[11] *Cobb*, *supra*, at p. 96, citing *Barajas*, *supra*, at p.1813.

[12] *Johnson v. Bradley* (1992) 4 Cal.4th 389, 404.

[13] See *Interim Opinion on Greenhouse Gas Regulatory Strategies* ("*Interim Opinion*") [D.08.03.018] (2008) ___ Cal.P.U.C.3d ___, pp. 97-98, fn. 32 (slip op.).

[14] *Id.* at p. 98, fn. 32 (slip op.).

In its application for rehearing, LADWP attempts to resuscitate its claim of a conflict between the auction under AB 32 and its Home Rule authority to operate its municipal utility. (Rehrg. App., pp. 8-9.) LADWP, however, has not demonstrated that the recommended auction in any way would interfere with its authority or ability to operate its municipal utility. Thus, contrary to LADWP's allegation, no conflict, let alone a genuine one, has been shown to exist.

Therefore, LADWP's application for rehearing provides no additional facts or new legal analysis to establish the existence of a conflict, and simply reasserts an argument we previously rejected. Accordingly, LADWP's contention is rejected here for the same reason.

Notably, even if LADWP were able to establish a genuine conflict, LADWP still has failed to establish a Home Rule violation under the remaining two steps of the court's analysis, as described above. In its rehearing application, LADWP skips to the third prong of the analysis and insists that an allowance auction is not reasonably related to the resolution of a statewide concern nor narrowly tailored to limit incursion into LADWP's legitimate municipal interests. (Rehrg. App., pp. 8-9.) In support of this contention, LADWP argues that an allowance auction is a wealth transfer scheme that would divert billions of dollars from, and thus undermine, the renewable procurement program adopted by LADWP in the exercise of its Home Rule powers. This contention lacks merit.

There is no dispute that the reduction of statewide GHG emissions as mandated by AB 32 qualifies as a matter of statewide concern. This includes our proposed allowance auction structure pursuant to reduction goals in the statute. An allowance auction structure as recommended is intended to reduce GHG emissions for the electricity sector, which is reasonably related to the statewide concern of reducing GHG emissions. (See D.08-10-037, pp. 8-10.)

In addition, the recommended allowance auction is narrowly tailored to meet the statewide concern of reducing GHG emissions. Regarding LADWP's premise that a "wealth transfer" is involved here, SDG&E and SoCalGas correctly point out that

"regulation that assumes that every ton of emissions creates the same burden on the environment does not produce wealth transfers -- it imposes the same cost on every emitter for every ton of emissions it creates (or for which it is responsible)." (Response of SDG&E and SoCalGas, pp. 8-9.)

Equally without merit is LADWP's claim that an auction structure is not narrowly tailored because of the costs it will impose on LADWP's own procurement program. Specifically, LADWP argues that there will be a diversion of funds from its own program. (Rehrg. App., pp. 8-9.) Under the recommended cap-and-trade program, LADWP would only be required to purchase allowances if its renewable procurement and other programs designed to reduce GHGs do not meet the targets inherent in the allowance structure. By purchasing an allowance from another entity, LADWP in effect will pay the other entity to reduce emissions more than that entity would have otherwise been required to, thus ensuring that the reductions LADWP has not made will be made by someone else.

LADWP has failed to establish that the recommended allowance allocation structure violates any portion of the necessary steps in resolving a Home Rule controversy. Accordingly, LADWP's contention lacks merit and is rejected.

3. The allocation option is not a discriminatory license charge, and thus, there is no violation of Article XIII, Section 19 of the California Constitution.

In its rehearing application, LADWP alleges that D.08-10-037 violates Article XIII, Section 19 of the California Constitution.[15] (Rehrg. App., pp. 9-12.)

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[15] This constitutional provision provides, in related parts:

> The Board shall annually assess (1) pipelines, flumes, canals, ditches, and aqueducts lying within 2 or more counties and (2) property, except franchises, owned or used by regulated railway, telegraph, or telephone companies, car companies operating on railways in the State, and companies transmitting or selling gas or electricity. This property shall be subject to taxation to the same

(*footnote continued on next page*)

Specifically, LADWP argues that the payments under the recommended cap-and-trade scheme constitute prohibited and discriminatory "license charges" for the emission of carbon dioxide under this constitutional provision.[16] (Rehrg. App., p. 10.) LADWP alleges that electric utilities, including investor owned utilities ("IOUs") as well as publicly owned utilities ("POUs"), would pay differently than members of other economic sectors, and this difference is prohibited by Article XIII, section 19 of the California Constitution. (Rehrg. App., p. 10.)

In D.08-10-037, we rejected this argument. The Decision stated:

> LADWP argues that Article XIII, Section 19 and Article XVI, Section 6 of the State Constitution may be violated by an allowance allocation option. Article XIII, Section 19 requires that taxes or license charges be imposed on public utilities in the same manner in which they are imposed on private entities. However, LADWP has not shown that the requirement that deliverers of emitting power purchase some allowances at auction would establish "license charges" as that term is used in Article XIII, Section 19 of the State Constitution. Moreover, we recognize that Article XIII, Section 19 "does not release a utility from payments … required by law for a special privilege …. (CA. Const. art.

(*footnote continued from previous page*)

> extent and in the same manner as other property.
>
> No other tax or license charge may be imposed on these companies which differs from that imposed on mercantile, manufacturing, and other business corporations. This restriction does not release a utility company from payments agreed on or required by law for a special privilege or franchise granted by a government body.
>
> The Legislature may authorize Board assessment of property owned or used by other public utilities.

(Cal. Const., art. XIII, §19, emphasis added.)

[16] As discussed above, the allowance does not constitute a tax, and thus, the Decision does not violate Article XIII, section 19.

> XIII, Section 19.) Additionally, LADWP's argument that the cost of programmatic measures is an additional tax or license charge that utilities will pay while other sectors will not, and thus is a violation of Article XII, Section 19 of the State Constitution, is unconvincing.

(D.08-10-037, p. 236.)

LADWP is simply incorrect that the allowance constitutes a license charge. For the allocation option to be a license charge, it must be a tax. For example, a license charge can be a tax for the privilege of operating a business. (See generally, *Pacific Gas and Electric Company v. City of Oakland* (2002) 103 Cal.App.4th 364, 370; *City of San Diego v. Southern California Telephone Corp.* (1954) 42 Cal.2d 110, 117; *Pacific Gas and Electric Company v. Roberts* (1914) 168 Cal. 420, 428-431; *City and County of San Francisco v. Pacific Telephone and Telegraph Co.* (1913) 166 Cal. 244, 249-250.) As discussed above, the allocation option does not constitute a tax, and thus, Article XIII, section 19 of the California Constitution does not apply.

Contrary to LADWP's assertion, the recommendations in D.08-10-37 do not "require the public utilities to pay for the 'special privilege' of polluting." (Rehrg. App., p. 11.) Rather, the purchase of allowances is related to the historical emissions of the retail providers' portfolios, and not the acquisition of a special privilege. Thus, the allowances correlate with GHG costs the public utilities, whether IOUs or POUs, helped to incur. (See D.08-10-037, pp 170 & 213.) Accordingly, since the allowance is neither a tax nor a license charge, Article XIII, section 19 has no applicability. Consequently, LADWP's allegation based on this constitutional provision has no merit and is rejected.

4. The Decision does not violate Article XVI, Section 6 (No Gifts of Public Funds) of the California Constitution.

LADWP contends that the Decision's proposed allowance allocation structure would result in transfers of wealth from POUs to lower-GHG retail providers and these alleged transfers of wealth constitute an unlawful "gift" of public money in

violation of Article XVI, Section 6 of the California Constitution.[17] (Rehrg. App., pp. 12-14.) Article XVI, Section 6 provides that the Legislature has "no power . . . to make any gift . . . of any public money or thing of value to any individual, municipal or other corporation whatever." (Cal. Const., art. XVI, §6.) This contention lacks merit.

We rejected the identical argument from LADWP in the Decision, noting: "LADWP fails to show how a requirement to purchase an allowance constitutes a gift."[18] LADWP's application for rehearing simply reasserts an argument we previously rejected and provides no additional facts or new legal analysis to support a different conclusion here.

LADWP's contention that the Decision's proposed allocation methodology creates a transfer of wealth and corresponding gift of public funds is fundamentally flawed. Regarding the premise that a wealth transfer is involved here, SDG&E and SoCalGas correctly note:

> [The proposed allocation methodology] does not require a transfer of money, or require a gift to be made from high emitters to low emitters. It merely requires all emitters to pay the same market price for every ton of GHG emissions for which they are responsible, creating a situation in which they bear the actual cost of their emissions.

(Response of SDG&E and SoCalGas, p. 10.)

Further, as the Decision stated:

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[17] LADWP's application for rehearing does not explicitly allege a violation of Article XVI, Section 3 of the California Constitution. However, LADWP implicitly raises an Article XVI, Section 3 contention through the cases cited in its rehearing application. (See Rehrg. App., p. 13.) This constitutional provision prohibits the appropriation of state funds for the benefit of a corporation not under the control of the state. (Cal. Const., art. XVI, §3.) LADWP's contention fails for the same reason that its Article XVI, Section 6 has no merit. As discussed below, amounts paid by LADWP at auction are not "gifts" of any kind, but simply represent the price of purchasing the right to continue to emit a certain amount of GHGs. Thus, Article XVI, Section 3 does not apply. Moreover, neither the plan to distribute or auction allowances involves the appropriation of money from the State Treasury as described in Article XVI, Section 3. Accordingly, LADWP's Article XVI, Section 3 contention has no merit and is rejected.

[18] D.08-10-037, p. 237.

> We recommend that ARB assign allowances (or allowance value) to the electricity sector at the beginning of the cap-and-trade program in 2012 based on the sector's proportion of total historical emissions during the chosen baseline year(s) in the California sectors included in the cap-and-trade program (including emissions attributed to electricity imports). We recommend that, in subsequent years, allowance (or allowance value) allocations to each California sector in the cap-and-trade program be reduced proportionally, using the overall trajectory chosen by ARB to meet AB 32 goals by 2020.
>
> Turning to allocation policy within the electricity sector, the criteria used to evaluate each approach included the ability to minimize costs to consumers, treat all market participants equitably and fairly, support a well-functioning cap-and-trade market, and allow reasonable administrative simplicity.
>
> We examined potential approaches that would distribute allowances to electricity deliverers in proportion to their historical emissions or in proportion to the amount of electricity they deliver to the grid. We also considered auctioning of allowances, with the distribution of allowances or allowance value to retail providers in proportion to the historical emissions of their generation portfolios or in proportion to their retail sales. Other approaches that were considered include distributing allowances on the basis of economic harm (see Section 5.2.3 below) and distributing specified rights to purchase allowances at a set price (see Section 5.2.1.3).

(D.08-10-037, pp. 14-15.)

Although the Decision uses terms such as "wealth transfer(s)" and "transfer of wealth," LADWP misreads how these words are used in the Decision. These terms are terms of art used by economists.[19] The Decision does not use these terms to mean an actual transfer of wealth in the manner alleged by LADWP, i.e. taking money from the

[19] See e.g. Joint California Public Utilities Commission and California Energy Commission Staff Paper on Options for Allocation of GHG Allowances in the Electricity Section ("Staff Paper"), dated April 16, 2008, p. 11, which was attached to ALJ Ruling of April 16, 2008, in R.06-04-009.

pockets of LADWP and giving it to another retail provider, namely an investor-owned utility. Rather, the Decision uses these terms of art as a short-hand for describing the different cost impacts on customers of retail providers who historically have had higher emission levels and customers of retail providers who have had lower emission levels in the past. As the Decision concludes, each retail provider and their customers eventually (after the phase in period) will be responsible for bearing the actual costs of their emissions that result from the retail providers' decisions about the resources to use to provide electricity. Thus, LADWP's literal reading misconstrues how the Decision utilizes these terms.

In addition, clearly amounts paid by LADWP at auction are not "gifts" of any kind, but simply represent the price of purchasing the right to continue to emit a certain amount of GHGs. Under the proposed GHG reduction program, LADWP will no longer have an unlimited right to emit GHGs but will need an allowance to so.

Accordingly, LADWP's contention that the Decision's proposed allowance allocation structure creates a transfer of wealth, and a corresponding unlawful gift of public funds is without merit and is rejected.

5. The record supports the cap and trade recommendations to the CARB reached by this Commission and the CEC.

LADWP contends that, due to modeling limitations, this Commission and the CEC did not have adequate information or analysis to support the Decision's recommended fuel-differentiated allocation of non-auctioned allowances. (Rehrg. App., pp. 14-15.) E3 modeling, as presented in the Decision, currently does not allow for analysis of fuel-differentiated allocation with weighted factor (2 for coal, 1 for natural gas). According to LADWP, these modeling limitations should prevent the joint agencies from asserting that a fuel-differentiated allocation option satisfies the agencies' stated

selection criteria.[20] LADWP is essentially arguing that the record does not support the Decision's recommendations to the CARB. This contention lacks merit.

Although there were some limitations in the current modeling regarding fuel-differentiated allowance allocation,[21] record evidence exists to support our recommendation of such an allocation. For example, pages 186-189 of the Decision are devoted to a discussion of various parties' comments in this proceeding regarding output-based allocation methodologies, including arguments for and against a fuel-differentiated output-based allocation.[22] A current lack of modeling for such an allocation did not prevent us from making reasonable and well-informed recommendations to CARB. Moreover, LADWP will be free to argue for more complete modeling of fuel-differentiated allocation in future proceedings before CARB.

Accordingly, LADWP's contention lacks merit and is rejected.

III. CONCLUSION

For the reasons specified above, the application for rehearing of D.08-10-037 is denied.

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[20] The stated criteria and goals we used in evaluating allowance allocation approaches were as follows:

- Minimize costs to consumers.
- Treat all market participants equitably and fairly.
- Support a well-functioning cap-and-trade market.
- Align incentives with the emission reduction goals of AB 32.
- Administrative simplicity.

(D.08-10-037, pp. 135.)

[21] D.08-10-037, pp. 214-215.

[22] Also see e.g., Staff Paper, pp. 30-32; Southern California Public Power Authority Comprehensive Comments (June 2, 2008), pp. 37-40; Sacramento Municipal Utility District's Comments on Administrative Law Judge's Ruling Requesting Comments on Emission Allowance Allocation, Combined Heat and Power, and Flexible Compliance Policies (June 2, 2008), pp. 13-16.

THEREFORE, IT IS HEREBY ORDERED that:

1. The application for rehearing of D.08-10-037 is denied.
2. This proceeding, R.06-04-009, is hereby closed.

This order is effective today.

Dated March 12, 2009, at San Francisco, California.

MICHAEL R. PEEVEY
President
DIAN M. GRUENEICH
JOHN A. BOHN
RACHELLE B. CHONG
TIMOTHY ALAN SIMON
Commissioners