

Decision 14-05-021 May 15, 2014

**BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA**

Order Instituting Rulemaking to Address  
Utility Cost and Revenue Issues Associated  
with Greenhouse Gas Emissions.

Rulemaking 11-03-012  
(Filed March 24, 2011)

**DECISION AUTHORIZING ELECTRIC AND NATURAL GAS INVESTOR-  
OWNED UTILITIES TO SELL LOW-CARBON FUEL STANDARD CREDITS**

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**DECISION AUTHORIZING ELECTRIC AND NATURAL GAS  
INVESTOR-OWNED UTILITIES TO SELL LOW-CARBON FUEL  
STANDARD CREDITS**

**1. Summary**

The decision authorizes the investor-owned electric and natural gas utilities subject to the California Public Utilities Commission’s jurisdiction to sell Low-Carbon Fuel Standard (LCFS) credits and establishes criteria and reporting requirements for the sale of LCFS credits, pursuant to Public Utilities Code Section 853(b). Utilities that have opted-in to the LCFS program and wish to sell LCFS credits are directed to file a Tier 2 Advice Letter (AL) proposing a plan for doing so in accordance with the direction provided in this decision no later than 60 days of the issuance of the decision adopting policies for the return of LCFS revenue to customers. Utilities that choose to opt in to the LCFS program in the future must file and receive approval of a Tier 2 AL containing their LCFS credit sale plans developed in accordance with the direction provided in this decision prior to commencement of the sale of LCFS credits.

This proceeding remains open.

**2. Background and Procedural History**

On March 24, 2011, the California Public Utilities Commission (Commission) opened Rulemaking (R.) 11-03-012 to address issues related to greenhouse gas (GHG) costs and revenues resulting from the implementation of California’s GHG Cap-and-Trade program pursuant to Assembly Bill (AB) 32.<sup>1</sup> The September 1, 2011 Scoping Ruling established three tracks in R.11-03-012 to address these issues. Track 1 focuses on the use of revenues generated by the

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<sup>1</sup> Statutes of 2006, Chapter 488.

auctioning of GHG allowances by the electric utilities as required by the California Air Resources Board (ARB); the Commission adopted rules for the use of this revenue in Decision (D.) 12-12-033. Track 2 addresses the use of revenues that the electric and natural gas utilities may receive from the sale of Low-Carbon Fuel Standard (LCFS) credits pursuant to ARB's LCFS regulation.<sup>2</sup> Track 3 was to address GHG cost and revenue issues for natural gas utilities; Track 3 was removed from the scope of R.11-03-012 and will be considered in a separate rulemaking, R.14-03-003.

This decision pertains to Track 2 of R.11-03-012 and addresses the authority required by electric and natural gas utilities subject to Commission jurisdiction to sell LCFS credits.

### **2.1. Low-Carbon Fuel Standard Background**

In December 2011, ARB finalized its LCFS regulation.<sup>3</sup> Under the current LCFS regulation, entities that voluntarily opt in to the LCFS program will earn credits for using transportation fuels with lower levels of carbon intensity.<sup>4</sup> For example, natural gas utilities that choose to opt in to the LCFS program that own natural gas fueling stations will receive LCFS credits associated with the use of approved alternate fuels to supply their own vehicle fleet as well as credits associated with customer purchases of alternative fuel if public access to

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<sup>2</sup> Executive Order S-1-07, the LCFS (issued on January 18, 2007), calls for a reduction of at least 10% in the carbon intensity of California's transportation fuels by 2020. ARB's LCFS regulation was developed in response to this executive order.

<sup>3</sup> <http://www.arb.ca.gov/regact/2011/lcfs2011/froalapp.pdf>.

<sup>4</sup> Utilities subject to Commission jurisdiction, as providers of low-carbon fuels, will only generate LCFS credits that can be sold in the market; the utilities will not be purchasers of LCFS credits.

utility-owned fueling stations is available. Under the LCFS regulation, electric utilities act as a proxy regulated entity on behalf of their customers and will therefore receive credits generated by their residential customers when those customers charge electric vehicles through their home electric service.

In addition, natural gas and electric utilities may receive LCFS credits through other means, for example fueling of utility natural gas vehicle fleets, fueling of third party natural gas vehicles at utility-owned refueling stations, or assignment of LCFS credits to a natural gas utility from an independently-owned natural gas refueling station that chooses not to opt in to the LCFS regulation. Utilities that earn LCFS credits from the use of low-carbon fuels may then sell those credits, regardless of how those credits are received; however, electric utilities, which act as a proxy for their customers, must use revenues in accordance with requirements set by ARB,<sup>5</sup> which are:

1. LCFS value must be used to the benefit of current plug-in electric vehicle (PEV) drivers;
2. The utility must administer PEV adoption education/outreach programs; and
3. The utility must provide rate options that encourage off-peak charging.

On February 8, 2012, the then-assigned Administrative Law Judges (ALJs) in this proceeding issued a ruling requesting proposals for the use of revenues from the sale of LCFS credits and proposing policy objectives by which the Commission could evaluate LCFS revenue use proposals. The ruling also set

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<sup>5</sup> The Commission will adopt a methodology for the use of LCFS revenues in accordance with the requirements set forth by ARB in a subsequent decision in Track 2 of R.11-03-012.

forth deadlines for parties to submit initial and revised proposals, provide comments on the proposals, and file reply comments; deadlines were modified in a March 14, 2012 ruling. A May 1, 2012 ALJ ruling requested additional information from the investor-owned utilities (IOUs) to supplement the record and set a new deadline for parties to submit revised LCFS allocation proposals of May 14, 2012. Pursuant to the November 25, 2013 Amended Scoping Memo, discussed below, parties were invited to submit updated proposals on January 8, 2014 with comments and reply comments due on January 22, 2014 and January 29, 2014, respectively.

#### **2.1.1. Authority to Sell LCFS Credits**

In 2013, the Commission's Energy Division conducted an evaluation of the Commission's implementation of the LCFS regulation and determined that, while utilities that have opted-in to the LCFS program have been receiving LCFS credits, they may lack the appropriate authority to sell those credits in the marketplace. To address the issue of what authority the utilities might need to sell LCFS credits, the Assigned Commissioner and assigned ALJ issued on November 25, 2013 an Amended Scoping Memo expanding Track 2 of R.11-03-012 to address the following questions:

1. Is any Commission-specific authority, outside of the authority granted in D.12-04-046 to procure GHG compliance products, required for the utilities to sell LCFS credits?
2. What requirements or restrictions, if any, should the Commission place on the sale of LCFS credits by IOUs?
  - a. Should the requirements to sell LCFS credits differ from the requirements related to GHG allowance procurement as established in D.12-04-046 in R.10-05-006?

In response to the questions posed in the November 25, 2013 Amended Scoping Memo, eight parties timely filed comments on December 18, 2013: The Office of Ratepayer Advocates (ORA), Pacific Gas and Electric Company (PG&E), the Natural Resources Defense Council (NRDC), Chargepoint, San Diego Gas and Electric Company (SDG&E), Southern California Edison Company (SCE), Green Power Institute (GPI), and Southern California Gas Company (SoCalGas) filing jointly with SDG&E (representing natural gas operations). Reply comments were filed on January 6, 2014 by NRDC, GPI, SDG&E/SoCalGas, and SCE.

### **3. Issues before the Commission**

In order for utilities to begin selling LCFS credits to generate the revenue needed to fulfill the state's policy goals with respect to the LCFS program, the Commission must resolve two issues. First, the Commission must determine whether and by what means authority should be granted to the utilities to sell LCFS credits. Second, the Commission must determine what safeguards, requirements or restrictions (if any) should be placed on the sale of those credits.

#### **3.1. Parties' Positions**

With regard to authority to sell LCFS credits, SCE states that the authority granted in D.12-04-046 in the 2010 Long-Term Procurement Plan proceeding, which governs electric utility transactions of GHG compliance instruments using upfront standards and criteria in the utilities' respective AB 57 Bundled Procurement Plans, does not include the sale of LCFS credits. SCE requests that the Commission provide authority for the utilities to sell LCFS credits through amendment of their AB 57 Bundled Procurement Plans and recommends the Commission adopt a process similar to the Advice Letter (AL) process used to establish AB 57 authority to transact sulfur dioxide products, which SCE deems

are the most similar products to LCFS credits. SDG&E, noting that the LCFS is a voluntary program, states that it is not clear that Commission authority is required to sell LCFS credits; however, SDG&E also recommends an update to approved AB 57 Bundled Procurement Plans to authorize the sale of LCFS credits. ORA agrees that updating AB 57 Bundled Procurement Plans is the correct procedural vehicle to authorize the sale of LCFS credits.

PG&E states that additional authority is needed beyond D.12-04-046 to authorize the sale of LCFS credits; however, PG&E proposes a list of upfront criteria, similar to those adopted in the utilities' AB 57 Bundled Procurement Plans, under which the utilities can sell LCFS credits. PG&E does not propose that the sale of LCFS credits be expressly authorized as part of AB 57 Bundled Procurement Plans.

SDG&E/SoCalGas state that it is unclear whether the natural gas utilities need specific authority from the Commission to sell LCFS credits, but they request that the Commission grant them that authority in the event that the natural gas utilities elect to participate in the LCFS program. NRDC agrees with SDG&E and SoCalGas that the need for authority to sell LCFS credits is unclear; however, the Commission should grant such authority to provide certainty.

GPI states that the procurement authority granted in D.12-04-046 pertaining to GHG compliance mechanisms is not a good model for the sale of LCFS credits. GPI argues that GHG compliance products are a commodity that the utilities are required to procure and surrender on behalf of GHG emissions for which the utilities are responsible. GPI notes that these compliance instruments are separate from the GHG allowances that are allocated to the utilities to be used on behalf of ratepayers, and D.12-04-046 does not require the



sale of any compliance products. The sale of LCFS credits, GPI argues, is not a procurement activity.

With regard to what, if any, requirements or restrictions should be placed on the sale of LCFS credits, parties offered proposals varying from unrestricted authority, as proposed by SDG&E/SoCalGas, to a specific list of upfront criteria, as proposed by PG&E and SCE. SCE requests that the Commission apply greater flexibility to the sale of LCFS credits than the requirements related to GHG compliance instruments noting several factors, including lack of available auctions or approved exchanges. SCE suggests that the utilities be given authority to propose specific standards in their AL filings amending their AB 57 Bundled Procurement Plans.

SDG&E argues that the LCFS market is illiquid and has few participants; therefore utilities should be allowed to sell LCFS credits without restrictions on transaction methodology; SDG&E provides a list of transaction methodologies for which it seeks approval. SDG&E further argues there should be no restrictions on the timing of LCFS credit sales and suggests that utilities keep the Commission up to date on LCFS transactions through Quarterly Compliance Reports.<sup>6</sup>

ORA argues that administrative simplicity is paramount and offers suggestions, such as ordering the utilities to consign LCFS credits to a third-party broker, to maximize LCFS credit value to ratepayers. ORA recommends that the Commission include protections for ratepayers, including

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<sup>6</sup> Quarterly Compliance Reports are mandated in D.02-10-062.

reporting requirements, such as the requirement to report to a utility's Procurement Review Group.

GPI generally agrees that burdensome restrictions should be avoided and suggests that, in order to serve the interests of ratepayers, early transactions should be short-term in nature to avoid locking ratepayers into long-term, below market prices. GPI further suggests that the Commission set a schedule for the periodic sale of LCFS credits until a mature and functioning market is established. NRDC notes that the sale of LCFS credits imposes no direct cost burden on electric utility customers; thus, utilities should be granted the flexibility to maximize the value of credits.

#### **4. Discussion**

##### **4.1. Authority to Sell LCFS Credits**

To the extent that parties cite a statutory basis for a determination that specific authority must be granted by the Commission before utilities may begin selling LCFS credits, they generally point to AB 57,<sup>7</sup> which requires electric utilities to file with the Commission a plan for procurement of electricity. Although these plans have included proposals for procuring and trading environmental compliance instruments associated with the procurement of electricity (such as GHG allowances and sulfur dioxide allowances), the Commission finds that it would not be appropriate for the utilities to use AB 57 authority for the sale of LCFS credits.

First, selling LCFS credits through AB 57 Bundled Procurement Plans would not work for natural gas utilities that might wish to participate in the

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<sup>7</sup> Codified as Public Utilities Code Section 454.5.

LCFS program; AB 57 applies only to electric utilities. It does not make sense from a policy perspective to create two separate means of authorizing the sale of a single commodity depending on whether the seller is a natural gas or electric utility.

Second, the other environmental compliance instruments transacted through the AB 57 Bundled Procurement Plans – GHG allowances and sulfur dioxide permits – are closely associated with the purchase of electricity and thus are appropriately transacted through the AB 57 plans. By contrast, LCFS credits are generated through the sale of electricity or natural gas for transportation fuel and thus are not closely tied to wholesale electricity procurement. Moreover, while GHG allowances and sulfur dioxide credits are both bought and sold - thus involving a procurement element - LCFS credits are not purchased by the utility; LCFS credits are only sold. For this reason, it would not be appropriate to include the sale of LCFS credits in the utilities' bundled procurement plans because, as argued by GPI, the sale of LCFS credits is not inherently a procurement activity.

In opening comments to the proposed decision, parties provided alternative mechanisms in order to justify the IOUs' sale of LCFS credits. SCE prefers to sell LCFS credits as an "electricity-related product", which was made available by procurement of electrical energy by the utility, subject to the existing processes established pursuant to the AB 57 plans.<sup>8</sup> SDG&E and SoCalGas suggest striking the justification to Pub. Util. Code § 851 because they disagree that LCFS credits are "property necessary or useful in the performance of the

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<sup>8</sup> SCE Opening Comments on the Proposed Decision at 4.

utility's duties to the public" and cite that LCFS regulations prohibit credits to be constituted as property.<sup>9</sup> Conversely, ORA asserts that while LCFS credits do not constitute property, the Commission has broad authority to regulate assets used to provide utility service and must consider whether LCFS credits are "necessary or useful" in this capacity.<sup>10</sup> ORA asserts that natural gas credits that are generated from utility fleet refueling purposes are necessary or useful for the performance of utility services but distinguishes them from credits generated from residential electric vehicle charging. ORA suggests to permit the sale of LCFS credits pursuant to Pub. Util. Code § 701, which authorizes the Commission to do things "necessary and convenient" to the regulation of public utilities as long as they are consistent with other statutes.

As a general matter, the sale, lease, or encumbrance of utility assets requires approval under Pub. Util. Code § 851. Although LCFS credits are not included in a utility's rate base, the sale of LCFS credits may be considered the sale of utility assets contemplated to be "necessary or useful" under § 851. LCFS credits are not necessary for the provision of utility service to the public, however their sale is useful in order to fulfill their obligation under §701.1 to "minimize the cost to society of the reliable energy services that are provided by natural gas and electricity", in this case, transportation services from plug-in electric and natural gas vehicles.<sup>11</sup> According to the LCFS regulation, IOUs are the fuel providers of electricity and natural gas which, in the case of electricity,

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<sup>9</sup> SDG&E and SoCalGas Opening Comments on the Proposed Decision at 10 and Title 17, CCR, Section 95484(d).

<sup>10</sup> ORA Opening Comments on the Proposed Decision at 6.

<sup>11</sup> Pub. Util. Code 701.1, 740.2, and 740.3.

must “use all credit proceeds as direct benefits for current EV customers.”

Therefore, the utility sale of LCFS credits is “useful” in order to minimize the social cost of alternative fuels and transportation. As such, the Commission must authorize the utilities to sell LCFS credits. However, because LCFS credits by nature do not constitute property,<sup>12</sup> and the nascent state of the LCFS market, then, pursuant to the authority to regulate utilities as “necessary and convenient” per §701, and § 853(b), it is appropriate to exempt the utility sales of LCFS credits from the standard requirements of § 851. Therefore, natural gas and electric utilities that opt in to the LCFS program may sell LCFS credits subject to the procedures and requirements set forth in the following sections. As the LCFS market matures and the Commission learns more about the results of the sale of LCFS credits, the Commission may revisit the procedures and requirements adopted in this decision.

#### **4.2. Requirements and Restrictions on the Sale of LCFS Credits**

The Commission agrees with the majority of parties that, given the nascent nature of the LCFS market, it is prudent to minimize restrictions on the sale of LCFS credits in an effort to maximize the value of LCFS credits for utility ratepayers. However, as raised by GPI and ORA, it is important that appropriate safeguards be put in place because the LCFS market that is not very well developed. In opening comments to the proposed decision, GPI agrees with the need for safeguards and states that oversight of IOU sales of LCFS credits is necessary because the IOUs derive no direct benefit from their sale and therefore

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<sup>12</sup> Title 17, CCR, Section 95484(d).

have no motivation to maximize their value.<sup>13</sup> GPI's statement has no factual basis. The IOUs have voluntarily opted-in to the LCFS program as regulated parties and have previously submitted proposals to achieve the ARB's policy objectives.<sup>14</sup> SDG&E and SoCalGas further state that their participation in the program is directed pursuant to Pub. Util. Code § 701.1 and §740.3.<sup>15</sup>

**4.2.1. Accordingly, the Commission adopts the following parameters and procedures governing LCFS credit sales by natural gas and electric utilities. Many of the adopted provisions mirror those suggested by SCE in opening comments, with appropriate modifications based on comments of other parties. Adopted Parameters and Procedures for the Sale of LCFS Credits**

1. Volume, Timing, and Transactional Length Limits

Given the nascent nature of the LCFS market and the corresponding lack of record, the Commission, at this time, does not adopt any specific limitations on the volume of LCFS credits that must be sold within a given timeframe and the timing of LCFS credit sales. The Commission does find with merit, however, the arguments supporting the limit proposed by SCE in opening comments – that a utility sell no more than the LCFS credits that have been provided at any point in time by ARB. Consistent with the LCFS regulation, a regulated party may not borrow or use credits from anticipated future carbon intensity reductions.<sup>16</sup>

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<sup>13</sup> GPI Opening Comments on the Proposed Decision at 1.

<sup>14</sup> Title 17, CCR, Section 95480.1(b) and Joint IOU Proposal for allocating revenue from the sale of LCFS Credits pursuant to February 8, 2012 ALJ Ruling.

<sup>15</sup> SDG&E and SoCalGas Reply Comments on the Proposed Decision at 2.

<sup>16</sup> Title 17, CCR, Section 95495(c)(2)(b).

The Commission rejects the suggestion by GPI to keep early transactions short-term in nature. GPI is concerned that longer-term transactions conducted in the LCFS market's infancy could result in locking ratepayers into long-term, below-market-price contracts; however, there is no evidence before the Commission to substantiate this concern. The Commission will have an opportunity to review the utilities' plans regarding volume, timing, and transaction length in the Tier 2 ALs discussed later in this decision.

## 2. Methods for the Sale of LCFS credits

SDG&E proposed a number of methods through which utilities could sell LCFS credits. The Commission agrees with SDG&E that broad authority should be granted at this juncture; however, some restrictions are necessary to provide sufficient safeguards. The utilities may therefore sell LCFS credits through competitive solicitations (requests for proposals) or via bilateral transactions presented by a broker registered with the Commodity Futures Trading Commission. SDG&E and SoCalGas disagree with the restriction against direct bilateral transactions due to the size of the market and the potential costs associated with brokered bilateral transactions.<sup>17</sup> However, PG&E supports the use of bilateral transactions presented by third-party brokers.<sup>18</sup> To sufficiently protect ratepayers and to ensure that LCFS credit value is maximized, the Commission does not approve direct bilateral sales at this time. The Commission will consider alternate sale methods, with appropriate justification, in the utilities' Tier 2 AL filings, as set forth below.

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<sup>17</sup> SDG&E and SoCalGas Opening Comments on the Proposed Decision at 6.

<sup>18</sup> PG&E Opening Comments on the November 25, 2013 ALJ Ruling.

### 3. Credit and Collateral Requirements

The Commission lacks sufficient record at this juncture to set parameters on credit and collateral requirements that should be required of buyers of LCFS credits; therefore, no specific credit and collateral provisions to the sale of LCFS credits are adopted at this time. However, credit and collateral requirements are prudent, and the Commission finds interesting SCE's proposal to use the same credit and collateral requirements in its current AB 57 Bundled Procurement Plans for other authorized emissions products. The Commission will consider utility proposals to address credit and collateral in the utilities' Tier 2 AL filings.

#### **4.2.2. AL Filings to Address Plans for Sale of LCFS Credits**

In comments, several parties recommended that the Commission order the utilities to file ALs proposing the methods, limits and other parameters by which they intend to sell LCFS credits. Although the ALs were generally recommended in the context of updates to the utilities' AB 57 Bundled Procurement Plans, the Commission finds that the filing of ALs proposing upfront standards and plans for the sale of LCFS credits, in accordance with the parameters adopted in this decision, is the appropriate procedural mechanism to ensure that sufficient safeguards are in place prior to commencement of operation in the LCFS marketplace. Because broad parameters for sale of LCFS credits are adopted in this decision, it is appropriate for the utilities to file ALs under the Tier 2 categorization. Utilities that have already opted-in to the LCFS program must file a Tier 2 AL proposing upfront standards and plans for the sale of LCFS credits according to the parameters adopted in this decision no later than 60 days of issuance of the subsequent decision adopting a methodology for the use of LCFS revenues in accordance with the requirements set forth by ARB in



Track 2 of R.11-03-012. LCFS credit sales may begin upon approval of the AL. Utilities that chose to opt in to the LCFS program in the future must file and receive approval of a Tier 2 AL containing their upfront standards and plans for the sale of LCFS credits prior to commencement of the sale these credits.

The utilities must, at a minimum, address the following topics in the Tier 2 AL filings proposing plans for the sale of LCFS credits:

1. Utilities must describe proposed limits on the volume of LCFS credits to be sold at any given time, the planned timing of LCFS credit sales, and any proposed limitations on the transactional length of LCFS credit sales.
2. Utilities must describe how brokers will be selected.
3. Utilities may propose and justify in their plans other means of selling LCFS credits, including organized exchanges and auctions, if such mechanisms become operational.
4. Utilities must propose credit and collateral requirements in their plans.

In addition to these requirements, the utilities must also include information pertaining to the establishment of balancing accounts to track LCFS revenues, as discussed in a later section of this decision.

#### **4.2.3. Reporting Requirements**

The Commission agrees with ORA that a reporting requirement is an important mechanism to provide ratepayer protection. In opening comments on the proposed decision, GPI asserted that the proposed decision explicitly assigns oversight responsibilities to the IOUs' Procurement Review Groups and Independent Evaluators.<sup>19</sup> GPI's statement is incorrect because the PD does not provide the PRG "jurisdiction" nor does it require the use of an IE. The

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<sup>19</sup> GPI Opening Comments on the Proposed Decision at 2.

Commission retains oversight over the program, and as SDG&E and SoCalGas reply, the PRG serves as a consultative and informal advisory function for the IOUs.<sup>20</sup> In comments to the proposed decision, ORA identified the need to determine requirements for IOUs without Procurement Review Groups.<sup>21</sup> In addition, the IOUs requested to permit greater flexibility in sales reporting and to align submission of annual reports with the Air Resources Board.<sup>22</sup> The Commission therefore adopts the following reporting requirements:

- a. Although not a procurement activity, utilities with Procurement Review Groups must report sales of LCFS credits to their Procurement Review Group at least quarterly.
- b. Utilities without Procurement Review groups must report sales of LCFS credits to the Commission's Energy Division, the Office of Ratepayer Advocates.
- c. Utilities must also file a confidential report with the Energy Division Director by April 30 of each year containing information about LCFS credit sales for the prior year, concurrent to the Annual LCFS Compliance Report that regulated parties must submit to the Air Resources Board.<sup>23</sup> Reports must demonstrate that the standards approved in the utilities' Tier 2 ALs were applied appropriately, and reports must detail the number of sales, the means by which the credits were sold, the volume of credits sold, the revenue generated by each sale, and administrative costs. Once the

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<sup>20</sup> SDG&E and SoCalGas Reply Comments on the Proposed Decision at 2.

<sup>21</sup> ORA Opening Comments on the Proposed Decision at 8.

<sup>22</sup> PG&E Opening Comments on the Proposed Decision at 1, SCE Opening Comments on the Proposed Decision at 8, SDG&E and SoCalGas Reply Comments on the Proposed Decision at 3.

<sup>23</sup> [http://www.arb.ca.gov/fuels/lcfs/LCFS\\_Guidance\\_%28Final\\_v.1.0%29.pdf](http://www.arb.ca.gov/fuels/lcfs/LCFS_Guidance_%28Final_v.1.0%29.pdf).

Commission adopts an LCFS revenue distribution methodology, utilities must also report the amount of revenue disbursed to customers and the means by which the revenue was distributed. Energy Division may, at its election, produce a report template to be used by the utilities and/or it may modify the information to be reported to ensure that LCFS sales are sufficiently monitored.

#### **4.2.4. Administrative Costs**

In opening comments, PG&E recommends that the utilities' cost of administering LCFS credit sales be recovered from the proceeds of LCFS credit sales. On its face, this recommendation appears reasonable; however, administrative costs must be kept sufficiently low so as not to materially impact the amount of LCFS revenues returned to utility customers upon adoption of a decision addressing use of revenues in Track 2 of this proceeding. We will defer final requirements on administrative costs to the subsequent decision adopting a methodology for the use of LCFS revenues in Track 2 of R.11-03-012. The utilities must also report their actual administrative expenses in the required annual report.

#### **4.2.5. Tracking of LCFS Revenues**

In comments, SoCalGas/SDG&E recommended that it be authorized to establish a memorandum account for the purpose of tracking LCFS revenue. The Commission finds this proposal to be reasonable, especially given that the Commission has not yet adopted an LCFS revenue distribution methodology. However, because the Commission will ultimately adopt approved uses for LCFS credit revenue, approval of balancing accounts, rather than memorandum accounts, are appropriate. The utilities are authorized to establish balancing accounts for the purposes of tracking LCFS revenue. Utilities must include

necessary information relevant to the establishment of LCFS revenue balancing accounts in their Tier 2 AL filings.

## **5. Comments on Proposed Decision**

The proposed decision of the assigned ALJ in this matter was mailed to parties in accordance with Section 311 of the Public Utilities Code and comments were allowed under Rule 14.3 of the Commission's Rules of Practice and Procedure. Comments were filed on April 16, 2014 by GPI, NRDC, ORA, PG&E, SCE, and jointly by SDG&E and SoCalGas. Reply comments were filed on April 21, 2014 by SDG&E and SoCalGas.

Comments and reply comments focused on several issues. These included: whether Public Utilities Code Section 851 applied to the sale of LCFS credits, periodic sale and annual reporting, requirements for program implementation, and the IOUs' participation in the program.

All comments and reply comments have been considered and, where appropriate, incorporated into this decision. Specifically, the following changes have been made from the proposed decision:

- LCFS credits are considered useful in the utility's fulfilment of its duties to the public, namely, minimizing the social cost of reliable transportation energy services from electric and natural gas fuels.
- The IOUs are ordered to report sales of LCFS credits quarterly.
- Electric IOUs are ordered to report sales of LCFS credits to their Procurement Review Groups. Natural Gas IOUs are ordered to report sales to the Commission's Energy Division, the Office of Ratepayer Advocates.

- The date for filing the confidential annual report to the Commission is synchronized with the Air Resources Board's Annual LCFS Compliance Report.
- IOU plans for the sale of LCFS credits shall be filed in Tier 2 Advice Letters as appropriate, but no later than 60 days after the decision adopting policies for the return of LCFS revenue to customers. This extension of time will allow the utilities to develop processes for sales of credits and to design revenue return programs based on the direction of the subsequent decision.
- Reporting requirements for LCFS program administrative costs will be deferred to the subsequent decision adopting policies for the return of LCFS revenue to customers in Track 2 of R.11-03-012.

## **6. Assignment of Proceeding**

Michael R. Peevey is the assigned Commissioner and Melissa K. Semcer is the assigned ALJ in this proceeding.

### **Findings of Fact**

1. Under the current LCFS regulation, entities that voluntarily opt into the LCFS program will earn credits for using, or providing transportation fuels with lower levels of carbon intensity.
2. In 2013, the Commission's Energy Division conducted an evaluation of the Commission's implementation of the LCFS program and determined that, while utilities that have opted-in to the LCFS program have been receiving LCFS credits, they may lack the appropriate authority to sell those credits in the marketplace absent Commission approval.
3. AB 57 Bundled Procurement Plans apply only to electric utilities; natural gas utilities are not granted procurement authority under AB 57.

4. LCFS credits are generated through the sale of electricity or natural gas for transportation and are not closely tied to wholesale electricity procurement.

5. LCFS credits are not purchased by the utility; LCFS credits are only sold. The sale of LCFS credits is not inherently a procurement activity.

6. Although LCFS credits are not included in a utility's rate base, the sale of LCFS credits most closely resembles the sale of utility assets contemplated under Pub. Util. Code § 851; therefore, Commission approval to sell LCFS credits is required.

7. Pub. Util. Code § 853(b) grants the Commission authority to establish rules or requirements deemed necessary to protect the interest of customers or subscribers of a public utility when it is exempted from the requirements of Pub. Util. Code § 851.

8. The LCFS market is not well developed, and the Commission lacks record on which to set standards on the volume of LCFS credits sold, the timing of the sale of LCFS credits, and limits on transactional length. There is no evidence before the Commission that longer-term transactions will lock ratepayers into below-market-price contracts.

9. There are many methods available to conduct LCFS credit sales including competitive solicitations, bilateral contracts, and the use of brokers. Organized exchanges and auctions are not currently in existence for the sale of LCFS credits.

10. The Commission lacks sufficient record at this juncture to set parameters on credit and collateral requirements. Each electric utility has approved credit and collateral requirements in its respective AB 57 Bundled Procurement Plans.

11. The Commission requires additional information from the utilities regarding their plans to sell LCFS credits in order to ensure that ratepayers are sufficiently protected and LCFS credit sales are effectively monitored. The filing

of ALs is the appropriate procedural mechanism by which to obtain the necessary information to ensure that sufficient safeguards are in place prior to participation of the utilities in the LCFS marketplace.

12. Adoption of a reporting requirement is an important mechanism to provide ratepayer protection as the utilities operate in the nascent LCFS marketplace.

13. The utilities will face administrative costs associated with the sale of LCFS credits.

14. The utilities currently lack balancing accounts in which to track LCFS credit revenues.

### **Conclusions of Law**

1. The Commission should avoid creating two separate means of authorizing the sale of a single commodity, LCFS credits, depending on whether the seller is a natural gas or electric utility.

2. The sale of LCFS credit most closely resembles the sale of utility assets contemplated under Pub. Util. Code § 851.

3. Given the nature of LCFS credits and the nascent state of the LCFS market, pursuant to Pub. Util. Code § 853(b), it is appropriate to exempt utility sales of LCFS credits from the standard requirements of Pub. Util. Code § 851.

4. In order to provide sufficient ratepayer protection, it is reasonable for the Commission to adopt parameters and procedures governing LCFS credit sales by electric and natural gas utilities. It is simultaneously prudent to minimize restrictions on the sale of LCFS credits in an effort to maximize the value of LCFS credits for utility ratepayers.

5. The Commission should not adopt any specific limitations on the volume of LCFS credits that must be sold within a given timeframe and the timing of

LCFS credit sales. SCE's proposal that a utility sell no more than the LCFS credits that have been provided at any point in time by ARB has merit. Utilities should consider this limit when developing proposed upfront standards for the sale of LCFS credits.

6. It is appropriate to grant utilities the authority to sell LCFS credits through competitive solicitations or via bilateral transactions presented by a broker registered with the Commodity Futures Trading Commission. To provide sufficient ratepayer protection, direct bilateral sales of LCFS credits should not be authorized at this time. Utilities should be allowed to propose alternate methods for the sale of LCFS credits, with appropriate justification.

7. It is prudent to require the utilities to propose credit and collateral provisions for the sale of LCFS credits.

8. It is appropriate to require electric and natural gas utilities that participate in the LCFS program to file ALs proposing upfront standards and plans for the sale of LCFS credits in accordance with the parameters adopted in this decision. Because this decision adopts broad parameters for the sale of LCFS credits, it is appropriate for the utilities to file ALs under the Tier 2 categorization.

9. Electric and natural gas utilities that sell LCFS credits in a given year should be required to report to their Procurement Review Groups, if applicable, and to the Commission information pertaining to their LCFS credit sale activity. Information provided to the Commission should include, at a minimum, demonstration that the utilities have adhered to the upfront standards approved in their Tier 2 AL filings, information about the number of LCFS credit sales, the means by which LCFS credits were sold, the volume of LCFS credits sold, the revenue generated by each sale, and administrative costs. Energy Division should, at its election, be authorized to develop a reporting template to be used



by the utilities and/or change the information to be reported in order to ensure sufficient monitoring of LCFS credit sales.

10. It is reasonable for the utilities to recover costs associated with administering LCFS credit sales from LCFS credit revenues; however, administrative costs should be kept sufficiently low so as not to materially impact the amount of LCFS revenues returned to utility customers upon adoption of a LCFS revenue distribution methodology by this Commission. In order to evaluate administrative costs, the utilities should be required to include in their Tier 2 AL filings estimated annual administrative costs and estimated LCFS credit sale revenues for 2014 and 2015. Utilities should also be required to report actual administrative costs in their annual LCFS reports filed with the Commission.

11. The Commission should approve the establishment of balancing accounts to track LCFS revenues for electric and natural gas utilities that sell LCFS credits. The utilities should be required to include information necessary to the establishment of balancing accounts to track LCFS revenue in the Tier 2 ALs required by this decision.

## **O R D E R**

**IT IS ORDERED** that:

1. Electric and natural gas investor-owned utilities that voluntarily participate in the Low-Carbon Fuel Standard (LCFS) regulation are authorized to sell LCFS credits according to the parameters and restrictions set forth in Appendix A to this decision, set pursuant to Public Utilities Code Section 853(b). LCFS credit sales may begin upon approval of the advice letters set forth in Ordering Paragraphs 2 and 3.

2. Electric and natural gas investor-owned utilities that wish to sell Low-Carbon Fuel Standard (LCFS) credits, and are already participating in the LCFS regulation, must file a Tier 2 Advice Letter no later than 60 days of issuance of this decision adopting policies for the rerun of Low-Carbon Fuel Standard revenue to customers.

3. Electric and natural gas investor-owned utilities that wish to sell Low-Carbon Fuel Standard (LCFS) credits, but that are not currently participating in the LCFS regulation, must file and receive approval of a Tier 2 Advice Letter (AL) filed in accordance with the adopted parameters set forth in Appendix A and the AL filing requirements set forth in Appendix B to this decision prior to commencement of the sale of LCFS Credits.

4. Electric and natural gas investor-owned utilities selling Low-Carbon Fuel Standard credits must report sales to their Procurement Review Groups, if applicable, as soon after the transaction as practicable.

5. Electric and natural gas investor-owned utilities that sell Low-Carbon Fuel Standard (LCFS) Credits must file a report with the Director of the California Public Utilities Commission's (Commission's) Energy Division by January 31 of each year addressing LCFS sales for the previous calendar year and other information as set forth in Appendix C to this decision. The Commission's Energy Division may, at its election, develop a reporting template to be used by the utilities and may also modify the reporting requirements set forth in Appendix C in order to ensure the most efficient and effective monitoring of the sale of LCFS credits.

6. Electric and natural gas investor-owned utilities may recover costs associated with administering the sale of Low-Carbon Fuel Standard (LCFS) credits from revenues received from the sale of LCFS credits upon approval of

2014 and 2015 administrative cost forecasts included in the utilities' Tier 2 Advice Letter filings.

7. Electric and natural gas investor-owned utilities selling Low-Carbon Fuel Standard (LCFS) credits are authorized to establish balancing accounts to track LCFS credit revenue. Information necessary to approve these balancing accounts must be included in the advice letters ordered in Ordering Paragraphs 2 and 3.

8. Rulemaking 11-03-012 remains open.

This order is effective today.

Dated May 15, 2014, at San Francisco, California.

MICHAEL R. PEEVEY  
President  
MICHEL PETER FLORIO  
CATHERINE J.K. SANDOVAL  
CARLA J. PETERMAN  
MICHAEL PICKER  
Commissioners

## Appendix A: Parameters and Restrictions on the Sale of Low-Carbon Fuel Standard Credits

1. There are no restrictions on the volume of Low-Carbon Fuel Standard (LCFS) credits that must be sold within a given timeframe or the timing of LCFS credit sales. A utility may sell no more than the LCFS credits that have been provided at any point in time by ARB per LCFS regulations. There are no restrictions on the length of LCFS credit sale transactions.
2. Utilities may sell Low-Carbon Fuel Standard (LCFS) credits through competitive solicitations (requests for proposals) or via bilateral transactions presented by a broker registered with the Commodity Futures Trading Commission. The Commission may approve other LCFS credit sale methods in the utilities' Tier 2 Advice Letter filings.
3. No specific credit and collateral provisions are adopted. The Commission finds interesting Southern California Edison's proposal to use the same credit and collateral requirements in its current Assembly Bill 57 Bundled Procurement Plans for other authorized emissions products has merit and utilities should consider use of these provisions.
4. Utilities must receive approval of Tier 2 Advice Letters detailing their proposed upfront standards and plans for the sale of Low-Carbon Fuel Standard (LCFS) credits prior to commencement of LCFS credit sales in the marketplace.

(END OF APPENDIX A)

## Appendix B: Tier 2 Advice Letter Filing Requirements

Tier 2 Advice Letters filed with the Commission addressing utility upfront standards and plans for the sale of Low-Carbon Fuel Standard credits must include, at a minimum:

1. A description of the proposed limits on the volume of Low-Carbon Fuel Standard (LCFS) credits to be sold at any given time, the planned timing of LCFS credit sales, and any proposed limitations on the transactional length of LCFS credit sales.
2. A description of the process for selecting brokers.
3. Proposed credit and collateral requirements.
4. Necessary information relevant to the establishment of Low-Carbon Fuel Standard revenue balancing accounts.

In addition, utilities may propose and justify other means of selling Low-Carbon Fuel Standard credits, including organized exchanges and auctions, if such mechanisms become operational.

(END OF APPENDIX B)

# Appendix C: Low-Carbon Fuel Standard Reporting Requirements

1. Utilities with Procurement Review Groups must report sales of Low-Carbon Fuel Standard credits to their Procurement Review Group at least quarterly.
2. Utilities without Procurement Review groups must report sales of LCFS credits to the Commission's Energy Division, and the Office of Ratepayer Advocates.
3. Utilities must also file a confidential report with the Energy Division Director by April 30 of each year containing information about LCFS credit sales for the prior year, concurrent to the Annual LCFS Compliance Report that regulated parties must submit to the Air Resources Board.
4. Low-Carbon Fuel Standard (LCFS) annual reports must demonstrate that the standards approved in the utilities' Tier 2 Advice Letters were applied appropriately, and reports must detail the number of sales, the means by which the credits were sold, the volume of credits sold, the revenue generated by each sale, and administrative costs. Once the Commission adopts an LCFS revenue distribution scheme, utilities must also report the amount of revenue disbursed to customers and the means by which the revenue was distributed.

(END OF APPENDIX C)