ENERGY RESOURCES CONSERVATION AND DEVELOPMENT COMMISSION OF THE STATE OF CALIFORNIA

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In the Matter of:

Proposed Adoption of Regulations Establishing a Greenhouse Gases Emission Performance Standard For Baseload Generation of Local Publicly Owned Electric Utilities.

Docket 06-OIR-1
(October 30, 2006)

CALIFORNIA MUNICIPAL UTILITIES ASSOCIATION COMMENTS REGARDING IMPLEMENTATION OF SB 1368 AND ENFORCEMENT ISSUES

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C. Susie Berlin
Barry F. McCarthy
McCarthy & Berlin, LLP
100 Park Center Plaza, Suite 501
San Jose, CA 95120
Telephone: 408-288-2080
Facsimile: 408-288-2080
Email: sberlin@mccarthylaw.com

Attorneys for the Northern California Power Agency, on behalf of the California Municipal Utilities Association

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Pursuant to the direction provided by Commissioner Byron at the December 8, 2006 *Electricity Committee Workshop on Greenhouse Gases Emission Performance Standard for Implementing Senate Bill 1368*, the California Municipal Utilities Association (CMUA) offers these comments on implementation of Senate Bill (SB) 1368 related to enforcement issues, and provides responses to the questions raised by the California Energy Commission (CEC or Energy Commission) in the *Staff Issue Identification Paper: Implementation of SB1368 Emissions Performance Standard, issued November 27, 2006* (Staff Issues Paper).

I. INTRODUCTION

SB 1368 authorizes the Energy Commission to adopt regulations to enforce the greenhouse gases (GHG) emissions performance standard (EPS) authorized in SB 1368, with respect to local publicly owned electric utilities (POUs). SB 1368 added §§ 8341(c)(1) and 8341 (e)(1) to the Public Utilities code.

Pub. Util. Code § 8341(c)(1) provides that "the Energy Commission shall adopt regulations for the enforcement of this chapter with respect to local publicly owned electric utilities." Pub. Util. code § 8341(e)(1) states, "[e]nforcement of the [EPS] shall begin immediately upon the establishment of the standard."

These comments (1) address the CEC's legal scope of authority with regard to enforcement regulations; (2) discuss proposed enforcement provisions consistent with this enforcement authority and the intent of SB1368; (3) discuss the transparency of the POU contract approval t for long-term financial commitments; and (4) respond to enforcement issues raised in the Staff Issues Paper.

II. THE ENERGY COMMISSION'S ENFORCEMENT POWERS ARE LIMITED BY LAW

The Energy Commission's enforcement powers are limited to those granted in the Administrative Procedure Act (APA), Public Resources Code sections 25000, *et seq*. (Warren-Alquist Act), and SB 1368. "Administrative agencies have only those powers conferred on them, either expressly or impliedly, by the Constitution or by statute, and administrative actions exceeding those powers are void."[1]

The APA (Cal. Gov. Code § 11340 et seq.) sets forth administrative procedures to be followed by certain state agencies in California, and rulemaking actions taken by the CEC are subject to its provisions.[2] The APA broadly defines covered 'regulations' as "every rule, regulation, order, or standard of general application or the amendment, supplement, or revision of any rule, regulation, order, or standard adopted by any state agency to implement, interpret, or make specific the law enforced or administered by it, or to govern its procedure."[3] The APA further defines a state agency's authority as the provision of law which permits or obligates the agency to adopt, amend, or repeal a regulation.[4] The regulations to be promulgated by the CEC pursuant to § 8341(c)(1) are clearly within these definitions.

A state agency's authority to adopt regulations is limited by two factors: (1) the statutory authority which created the agency; and (2) the statutory authority that enables the agency to adopt regulations pursuant to statutes the agency is charged with

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[1] Terhane v. Superior Court 76 Cal.Rptr.2d 841, 872-873 (1998).

[2] Cal. Pub. Res. Code § 25213.

[3] Cal. Gov. Code § 11342.600

[4] Cal. Gov. Code § 11349.

administering.[5] Therefore, regulations promulgated by the Energy Commission are valid if they are within the scope of the legislation that created the state agency (Warren-Alquist Act) and within the scope of authority conferred by the legislation charging the agency with a duty, in this case, SB 1368.

The Warren-Alquist Act: Pursuant to the APA, in order to ascertain the scope of authority of a state agency, it is necessary to review the authority granted in the enabling legislation. Pub. Res. Code sections 25000, et seq., the Warren-Alquist State Energy Resources Conservation and Development Act, established the Energy Commission. This enabling legislation also set forth specific powers of the CEC. Specifically, § 25213 provides that "[t]he commission shall adopt rules and regulations, as necessary, to carry out the provisions of this division [Energy Conservation and Development] in conformity with the provisions of the [APA]." Unless an action is specifically authorized under SB1368, the CEC's enforcement authority is limited by the provisions of the Warren-Alquist Act.

Senate Bill 1368: Here, the second source of the Energy Commission's enforcement authority is the legislation charging the Energy Commission with administering the law, SB 1368. SB 1368 adds Pub. Util. Code § 8341(c)(1), which provides that *"the Energy Commission shall adopt regulations for the enforcement of [the EPS] with respect to local publicly owned electric utilities."* SB 1368 also provides that "[e]nforcement of the [EPS] shall begin immediately upon the establishment of the standard." Pub. Util. Code § 8341(e)(1). Nothing else in SB 1368 authorizes enforcement action, or authorizes the imposition of monetary fines or penalties on POUs.

The Legislature, in SB 1368, did not authorize any specific enforcement mechanisms, despite its clear ability to do so. For example, in Pub. Res. Code § 25321, the legislature expressly granted the Energy Commission enforcement authority with respect to the data collection requirements for the Integrated Energy Policy Report. In that

[5] See Cal. Gov. Code § 11342.1: "[E]ach regulation adopted, to be effective, shall be within the scope of authority conferred and in accordance with standards prescribed by other provisions of law," and § 11342.2: "Whenever by the express or implied terms of any statute a state agency has authority to adopt regulations to implement, interpret, make specific or otherwise carry out the provisions of the statute, no regulation adopted is valid or effective unless consistent and not in conflict with the statute and reasonably necessary to effectuate the purpose of the statute."

legislation, the CEC is specifically authorized to use "enforcement measures," including monetary penalties.

In this case, the Energy Commission has no authorization to impose a penalty of any sort on the POUs. SB 1368 is completely devoid of any express authorization to impose financial penalties of any kind. Neither can the statute be interpreted to implicitly allow for the imposition of a financial penalty, as that would violate Govt. Code § 11145, which prohibit the CEC from adopting or enforcing "any rule or regulation a violation of which can result in the imposition of a fine . . . unless a statute specifically authorizes the imposition of such fine . . . for a violation of the rule or regulation."

III. CEC ENFORCEMENT PROVISIONS SHOULD BE SOLELY INJUNCTIVE IN NATURE

A. CEC Enforcement Should be Limited to Injunctive Relief.

While SB 1368 does charge the Energy Commission with enforcing certain provisions, it does not expressly provide the Energy Commission with the authority to impose any kind of financial or other penalty on the POU. Accordingly, regulations should be carefully drafted in order to insure that they are not punitive in nature, thereby exceeding the CEC's authority. Therefore, the POUs recommend that all CEC enforcement actions be injunctive, following closely the type of proceedings generally available to parties seeking to challenge actions taken by governmental entities. As discussed more fully below, POUs and their governing bodies remain subject to enforcement compliance mechanisms resulting from their actions as governmental agencies.

As a practical matter, it is imperative to keep in mind that POUs are all subject to oversight by their individual governing bodies. These governing bodies are comprised of either elected or appointed officials. Simply put, each POU is governed by its own version of a public utilities commission, and therefore, is subject to close and ongoing regulation. These elected, locally accountable regulatory authorities are charged with overseeing POU activities and, as public agencies, are subject to stringent rules and requirements, including insuring that their actions are not contrary to the law. As a rule, POU action to enter into a long-term financial commitment for baseload generation of the type contemplated in SB 1368 will be approved by the local regulatory authority during a public meeting, and only

after a public review process. This is, *by law*, a transparent process. Furthermore, any information that might not be immediately publicly available is generally available through the Public Records Act.[6]

Since local regulatory authorities are government bodies, any SB 1368 enforcement actions should be modeled after existing California laws applicable to cities, counties and other public agencies, rather than any enforcement mechanisms that may be used by the California Public Utilities Commission (CPUC) for the oversight of investor owned utilities. For instance, because POUs are already governed by PUC-equivalent bodies, adding CPUC enforcement mechanisms to the mix would result in duplicative and unduly burdensome enforcement in the POU context. Notably, SB 1368 carefully distinguishes between investor owned utilities – which must follow rules promulgated by the CPUC – and POUs. For example, in the Legislative Counsel's Digest of SB 1368, the legislature specifically notes that SB 1368 "would prohibit the [CPUC] from approving any long-term financial commitment by an electrical corporation unless any baseload generation supplied under the long-term financial commitment complies with the [standard]." There is no similar direction with regard to the CEC. That is because the CPUC is *already* required to approve investor owned utility long-term financial commitments, whereas the CEC does not have such a charge with respect to POUs. This distinction is vital because it serves to emphasize the fact that the Legislature acknowledged the special characteristics of POUs as locally accountable governmental entities.

Accordingly, it is appropriate for any enforcement mechanism to follow the traditional local government model and provide for injunctive relief, not penalties. Specifically, if a POU is found not in compliance with SB 1368, any CEC enforcement procedure against the POU should be modeled after a traditional writ of mandate. A writ of mandate is an action compelling a government body to perform its legal duty, and may be issued to compel a governmental agency to perform an act which the law specifically enjoins as a duty resulting from an office.[7] A writ of mandate may issue if the following requirements are met: (1) lack of plain, speedy and adequate remedy in the usual course of law; and (2) a clear beneficial right of the petitioner to performance of that duty.[8]

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[6] Cal. Govt. Code § 6250 *et seq.*

[7] Cal. Code Civ. Proc. § 1085

[8] Cal. Code Civ. Proc. § 1086

If, for example, a POU has a contract that does not comply with SB 1368, the Energy Commission or any interested party may file a writ of mandate to compel compliance with the standard. The writ requires the petitioner (*e.g.*, the Energy Commission) to show that it: (1) has a beneficial interest; (2) that the POU has the ability to perform that duty; (3) that the POU failed to perform its duty or abused it discretion; and (4) that the Energy Commission has no other plain, speedy and adequate remedy. The Legislature has already determined that such enforcement actions are appropriate for enforcing public agency compliance; the CEC should follow that model here. However, as more fully set forth below, it is important to note that this is not the only enforcement mechanism to which the POU is subject.

B. POUs Are Subject To Stringent Compliance And Enforcement Mechanisms.

POUs are subject to enforcement mechanisms to insure compliance with the law – including SB 1368 – even though the CEC has limited enforcement powers over the POUs. POUs are subject to strict and stringent enforcement mechanisms as it pertains to contract compliance. As noted above, POUs are governmental agencies subject to regulation by their local regulatory authorities. As a practical matter, any long-term financial commitment – especially for a new ownership investment – will go through a transparent public process. Each transaction will be thoroughly vetted by the POU's staff before being presented to the local regulatory authority for approval. Part of the "packet" of information presented to the governing board would include background information on the proposed investment or project, including why the project is necessary, and that it is in compliance with all relevant laws. This latter attestation is especially important where the financial commitment will entail third party financing (in the case of POUs, this would likely mean the issuance of bonds). The local governing body would have to approve the disclosure statements for the issuance of bonds, which disclosure would include a warranty of compliance with all applicable laws –including SB 1368. Such financing would also be subject to federal securities laws, which include severe penalties for violations.

Furthermore, even in the absence of a CEC enforcement action, contracts

entered into that do not comply with the law (any law, and not just SB 1368), would be voidable. The governing bodies of POUs are public officials directly answerable to their local constituency. These governing bodies will exercise due diligence to ensure they do not burden the POU with a contract that may not be lawful.

IV. RESPONSES TO STAFF ISSUES PAPER QUESTIONS REGARDING ENFORCEMENT

Set forth below are the questions raised in Chapter 6 of the Staff Issues Paper and responses to those questions based on the legal discussion set forth above.

Question 6.1: *Is there agreement that an enforcement mechanism should be identified in the regulations?*

SB 1368 specifically provides that the Energy Commission should adopt regulations regarding the enforcement of the statute. Accordingly, there is no reason why an enforcement mechanism should not be identified in the regulation, and every reason to include a clearly defined mechanism up front. However, as noted above, such a regulation cannot include fines or penalties. Rather, any such regulation should be similar in scope to the types of mechanisms already established for enforcement of governmental entity compliance, after an opportunity to cure.

Issue 6.2: Prior Review of Contracts

Under a scenario where POUs obtain approval of their contracts before they are entered into, one option for enforcement (where a contract is deemed non-compliant) would be for the Energy Commission to instruct the POU that they are not allowed to enter into that contract. This determination could be made using the existing Complaints and Investigations process outlined in the California Code of Regulations, title 20, section 1230 et seq., or could be made under a new tailor-made process for SB 1368 compliance determinations.

Question 6.2(a): *Are there any other options for enforcement under this scenario?*

As discussed above, the CEC lacks the authority to impose penalties on the POUs. Regardless, POUs are subject to enforcement and compliance in other venues, including at the local level.

Title 20, section 1230 et seq. should not be utilized for SB 1368 enforcement. The provisions of Title 20, section 1230 et seq. have broad applicability, but clearly

contemplate investigation and enforcement of provisions pertaining to power plant siting and site certification, which specifically allow for the imposition of civil penalties. These provisions are clearly distinguishable from the regulations regarding enforcement under SB 1368, and SB 1368 does not authorize the CEC to use them for SB 1368 enforcement.

Due to the unique nature of SB 1368, and the fact that the CEC is charged with promulgating enforcement regulations that are separate and distinct for POUs than for other load serving entities, any complaint and investigation process should be specifically tailored to the POUs, and should include, when applicable, an opportunity to cure.

Furthermore, SB 1368 addresses *entering into* long-term financial commitments for baseload generation, and does not contemplate ongoing performance monitoring of such commitments, and accordingly, the investigation process outlined in Title 20 would be inapplicable.

> *Another option would be to use an Order to Show Cause to require a POU to appear before the Energy Commission and explain why an enforcement action should not be taken. If the POU persisted despite an Energy Commission determination of noncompliance, then one enforcement option would be for the Energy Commission to seek judicial enforcement; most likely in the form of a permanent injunction.*
>
> ***Question 6.2(b):*** *Are there any other options for enforcement under this scenario?*

Before fully developing something similar to an Order to Show Cause (OSC) process, the "enforcement action" contemplated for the POU must be fully defined, including provisions for an opportunity to cure. Something similar to an OSC may be appropriate, in that it would provide for an opportunity to be heard, but the form of the OSC should allow for a "paper process" whereby the Energy Commission sets forth its allegations, including the grounds upon which it bases its belief that the POU is not in compliance with the statue and a procedure for a written response to the same.

> ***Issue 6.3: Prior Review of "New Ownership Investments"***
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> *Under a scenario that has the POUs obtaining prior approval for new ownership investments in baseload generation, one enforcement option would be for the Energy Commission to declare the proposed investment noncompliant (in the manners discussed above), and instruct the POU that they are prohibited under SB 1368 from making that investment. If the POU persisted, one option for further enforcement would be for the Energy Commission to seek judicial enforcement.*

Question 6.3: *Are there any other options for enforcement under this scenario?*

The CEC should not involve itself in pre-approval of POU contracts or ownership investments. The POU governing bodies, and not CEC staff, have the technical and legal expertise to determine whether long-term financial commitments are compliant with SB 1368. The governing bodies of POUs are also directly answerable to their local constituents for their actions; this creates a further incentive to comply with all applicable laws. POUs are not without considerable mechanisms that would encourage, or if necessary, compel compliance, not the least of which is the threat of significant financial penalties associated with long-term investment financings for contracts that are not in compliance with *all* relevant laws and regulations, not just SB 1368. The "fear" that once such an agreement is entered into California ratepayers are exposed to too great a risk is simply unfounded.

Issues 6.4-6.6 Review of Executed Contracts

Enforcement becomes more complicated if Energy Commission compliance review occurs after contracts have already been executed. Enforcement to deter or correct noncompliance under such a scenario may work best by employing two different measures: a penalty measure and a corrective measure. A penalty measure might reduce the likelihood that a POU would risk entering into a noncompliant contract if the penalty was of sufficient weight to act as a deterrent. It is unclear what form this penalty could take. Monetary penalties have not been specifically provided for under SB 1368 and there does not appear to be independent authority under the Warren-Alquist Act to put them in place for this purpose. One possibility would be to require any POU determined to have entered into a noncompliant contract to thereafter undergo prior review of all contracts.

Questions 6.4: *Are penalties the right approach? If so, what types of penalties would be appropriate?*

The CEC is prohibited by law from imposing financial penalties of any kind. SB 1368 does not authorize penalty measures and therefore, they should not be employed.

Once noncompliance is detected it should be quickly corrected and the POU brought back into compliance with SB 1368 and supporting regulations. One option would be to require the POU to cancel the noncompliant contract. The POUs have stated that this may not be an easy or quick task. For due process purposes, they would possibly have to allow the contracting facility time to correct the non-conformance with the EPS. It is unclear whether this potential requirement could be removed with a contract provision allowing the POU automatic

termination if the subject facility is found not to comply with the EPS. Even if a POU could legally terminate a contract, doing so may not be practical for reliability reasons. It could take some time to find another source of electricity to replace the noncompliant source.

Question 6.5: *Are there any other approaches to quickly correct a noncompliant contract?*

SB 1368 requires that the POU be in compliance at the time the long-term financial commitment is made. It does not provide for ongoing contract monitoring. As a practical business matter, POUs will make every effort to avoid entering voidable contracts, which means they are also going to make every effort to insure that contracts may be terminated if the counterparty is not complying with the provisions SB 1368. POUs can cancel the noncompliant contracts, but must do so under the normal contracting provisions, which will likely require opportunities to cure from the counterparty. There are approaches that will allow for correction for noncompliance, should that occur; this will be addressed in contract provisions, not unlike contracts for renewable resources that require the counterparty to attest to the fact that the energy provided comes from a renewable source.

Question 6.6: *Does after-the-fact enforcement satisfy the Statute's goals of reducing California's exposure to costs associated with future regulation of greenhouse gases and "potential exposure of California consumers to future reliability problems in electricity supplies?"*

"After the fact enforcement" is a misnomer that ignores the intensive and transparent public process that is employed before a POU enters into a long-term financial commitment of the type contemplated under SB 1368. The local governing body is already engaging in a full review of the commitment and is aware of the legal ramifications (which are more severe for most financings than what the CEC is authorized to impose) before approving the transaction. An additional layer of regulatory oversight will not aid this process, nor it is necessary or even contemplated under SB 1368.

Issue 6.7: Review of Completed "Investment" Transactions

As in after-the-fact review of contracts, enforcement of the EPS after a new ownership investment has already been made can be complicated. As discussed above, instituting a penalty might be useful in deterring noncompliant investments. If such deterrence should fail, however, corrective action would be required. In order for the noncompliance to be corrected, either the facility would have to be made compliant (reduce its emissions to the standard) or the POU would have to somehow retrieve its investment. Parties have argued, however, that once an

investment is made in a noncompliant facility the damage has been done and no action could fully correct the harm caused.

Question 6.7: *Are penalties an appropriate initial enforcement mechanism? If so, what types of penalties could serve as an effective deterrent under this scenario? Is it possible to fully correct an investment in a noncompliant facility after it has been made? If so, how?*

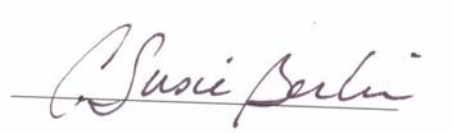
As stated above, the CEC has no authority to impose penalties. Neither SB 1368, nor the CEC's enabling legislation authorize the CEC to impose financial penalties on POUs. The CEC is further prohibited under by Govt. Code § 11145 from even adopting a regulation, a violation of which could result in the imposition of a fine. California law already provides for enforcement mechanisms for governmental entities; these mechanisms are just as applicable to long-term financial commitments for baseload generation as they are for any other investment decision made by the governing body of the local government.

V. CONCLUSION

In preparing the proposed regulations for implementation of SB 1368, specifically with regard to enforcement, CMUA respectfully requests Energy Commission Staff to incorporate the legal analysis and responses set forth herein.

Dated: December 13, 2006

Respectfully submitted,



C. Susie Berlin
McCarthy & Berlin, LLP
100 Park Center Plaza, Suite 501
San Jose, CA 95120
Telephone: 408-288-2080
Facsimile: 408-288-2080
Email: sberlin@mccarthylaw.com

Attorneys for the Northern California Power Agency, on behalf of the California Municipal Utilities Association

CERTIFICATE OF SERVICE

I certify that the following is true and correct:

On December 13, 2006, I served an electronic copy of the attached:

CALIFORNIA MUNICIPAL UTILITIES ASSOCIATION COMMENTS REGARDING IMPLEMENTATION OF SB 1368 AND ENFORCEMENT ISSUES

on all known parties to Docket No. 06-0IR-1, or their attorneys of record, that have provided copies of their e-mail addresses.

Executed this 13th day of December 2006, at San Jose, California.

Katherine McCarthy