



SDREO 2003 LEGISLATIVE SUMMARY REPORT TO THE REGIONAL ENERGY POLICY ADVISORY COUNCIL

April, 2003

SDREO has prioritized current energy legislation according to legislative principles that were adopted by the San Diego Association of Governments (SANDAG) and are consistent with the Regional Energy Plan. Included in this report are a number of bills that could potential impact our region. SDREO will track those that are high priority to provide the Council with accurate and updated information. The priority definitions are as follows:

Priority 1- Bills that are significant to the region, fit with the legislative principles and that SDREO is actively tracking

Priority 2- Bills that are somewhat significant to the region

Priority 3- Bills that are not significant to the region

Priority 4- Bills that could be potentially significant, but are not active

Priority 1 State Bills (in numerical order)

SB 46

Alpert and Sher: Distributed energy resources

SUMMARY

Bill would expand the distributed energy resources criteria to include electric generation technology that commenced initial operation between May 1, 2001, and June 1, 2005, except that gas-fired distributed energy resources that are not operated in a combined heat and power application must commence operation no later than September 1, 2002.

LATEST ACTION

In Senate Energy, Utilities, And Communications Committee.

SB 72

Dunn: Independent System Operator

SUMMARY

This bill would impose specific analytical and reporting requirements intended to prevent the ISO from filing tariffs unless it determines that the proposed changes will have an economic benefit for ratepayers.

BACKGROUND

AB 1890 (Brulte), Chapter 854, Statutes of 1996, required the creation of the ISO as a "separately incorporated public benefit, nonprofit corporation." When it established the ISO, the Legislature gave little explicit guidance as to its public obligations. Section 345 of the Public Utilities Code simply declares the purpose of the ISO is to "ensure efficient use and reliable operation of the transmission grid."

Because the ISO is not a governmental agency, it is not subject to general state laws governing the conduct of state and local agencies. Last year, SB 1753 (Bowen), Chapter 847, Statutes of 2002, expanded on the original charter of the ISO, requiring it to conduct its operations consistent with state laws and the public interest, and assigning it more detailed public obligations.

In response to problems identified during the energy crisis and subsequent investigations, the ISO is in the midst of a significant redesign of its grid management practices and the markets it administers. Ratepayers will bear the capital expense of this redesign, which includes significant computer and software costs, and will also be affected by any resulting increase or decrease in electricity costs. Questions have been raised about the effects of some elements of the ISO proposal on consumers. In particular, uncertainty about the costs and benefits of the ISO proposal for pricing transmission system congestion prompted Senators Bowen, Burton, Dunn and Sher to ask the ISO to suspend all tariff filings and capital expenditures relative to implementing the proposal until the ISO analyzed its costs and benefits for consumers. The ISO has complied with this request and recently commissioned a cost/benefit study. The Senators further requested any future market redesign filings and expenditures - and other ISO actions - should be predicated on a demonstrable benefit to electricity consumers.

Issues Under Debate

1. Is "economic benefit" always the appropriate standard?

Economic benefit may not be the primary purpose of an ISO tariff filing. The ISO points out that many tariff changes are needed for reliability and operational requirements, and aren't based on economics. For such changes, or even for changes which are based on economics, economic consequences may be difficult to predict accurately. The ISO is concerned this bill will invite parties to bring actions in state court to challenge its tariff filings. A federal preemption issue could arise if a court overturned a FERC-approved tariff because it violated state law.

Also, current law requires the ISO to strike some balance between reliability, economic and environmental considerations. Economics may not always be the first concern. The author and the committee may wish to consider whether the ISO should be required instead to show a more general benefit to the public.

2. Exemptions may undermine bill's effect.

While this bill is intended to ensure that ISO tariff filings have an economic benefit for ratepayers, it may not apply to many significant filings because of the bill's exemptions for FERC-required and emergency filings. For example, the current market redesign was undertaken in response to a FERC order and the ISO's December 8, 2000 filing to remove price caps was an emergency filing. The author and the committee may wish to consider requiring a vote of the ISO's governing board to invoke the emergency exemption.

LATEST ACTION

In Senate Energy, Utilities, And Communications Committee.

PROS/OPPORTUNITIES

CONS/ISSUES

REGISTERED SUPPORT

REGISTERED OPPOSITION

None received.

SUMMARY

This bill would require any person that imports electrical energy into the state, or causes electricity to be imported into the state, to pay up to a \$0.001 per kilowatt-hour air contaminant emission mitigation fee for that electricity. This bill would impose the fee only if the electricity is produced by an electrical generating facility that is owned by a person domiciled in the United States, located within an air basin shared by a district and Mexico, and located in Mexico within 100 kilometers of the United States Border. Additionally, the fee would only apply if the state board determines that the electrical generating facility was not constructed using the best available control technology (BACT) for air contaminants. This bill would establish the Imported Electricity Air Pollution Mitigation sub account in the Air Pollution Control Fund and require the air contaminant emission mitigation fees to be deposited in that sub account and revenues would be distributed to each district in the state that the board determines directly impacted by air contaminant emissions.

SB 289 (Murray: Solar on New Residential Construction)**SUMMARY**

Bill would require builders of single-family homes to offer purchasers the option of including a solar energy system on the residence. It would also require an undetermined percentage of single-family residences constructed on or after January 1, 2006, to be constructed with a solar energy system that produces at least 2 kilowatts of electrical power to the residence.

BACKGROUND

The debate around solar energy systems revolves around the issue of cost effectiveness. Systems are relatively expensive. The costs of installing a solar energy system on a new home currently costs between \$12,000 to \$20,000 per home. Supporters believe that existing market trends and the economies of scale created by this bill will drop the price to at least \$8,800 by 2006. Based on this cost and their estimates of energy savings the sponsors argue that consumers will face an added cost of only \$8 per month.

Other persons in the energy field believe that solar energy systems are still not cost-effective unless heavily subsidized. A CBIA advocate provided information on his personal home showing that the costs of financing a \$20,000 system would have exceeded his entire energy bill for the first three months of this year by \$220. These costs are potentially offset by rebates through the state's Renewable Buydown Program. However, the Buydown Program is already oversubscribed and is subject to reauthorization in 2006.

LATEST ACTION

Passed out of the Senate Housing Committee by a slim margin, and the Committee Chair spoke of the importance of including solar thermal in the bill.

PROS/OPPORTUNITIES

According to the REIS, increased use of renewables and in particular, solar, is an important component of achieving a balanced supply of electricity for the San Diego region. As a result of the high retail electricity prices, consumer interest in residential solar systems has increased dramatically. Currently, five new home builders offer solar systems in new homes in San Diego.

The industry has recognized that in general, incorporating solar systems during new construction is most cost effective, since retrofit of systems later is more costly.

CONS/ISSUES

The building industry generally opposes mandates for increased use of solar due to potential increased costs of housing.

SUPPORT

City of San Diego

Environment California (sponsor), The California League of Conservation Voters (CLCV), The Planning and Conservation League, CAL SEIA

OPPOSITION

None received.

SB 684 (Alpert: San Diego Regional Energy Authority)

SUMMARY

Bill would have formed the San Diego Regional Energy Authority.

LATEST ACTION

Bill reassigned to unrelated issue. City of San Diego may reintroduce Bill next year.

SB 888 (Dunn: Repeal of Electricity Deregulation)

SUMMARY

Bill would enact the Repeal of Electricity Deregulation Act of 2003 by

- ✓ Restore and affirm the public utility's obligation to serve all of its customers and to provide adequate service at just and reasonable rates,
- ✓ Requiring the CPUC to ensure that generation assets remain dedicated for the benefit of the utility's bundled customers so as to a) eliminate opportunities for market manipulation by stopping electric plant divestiture and authorizing cost-of-service construction of new electric plants and to b) public utility wholesale electricity procurement, while providing a fair opportunity for reasonable returns on prudent investment.
- ✓ Establish standards for the recovery of costs and return on investment.
- ✓ would authorize the commission to require utilities to make investments in electric plants that are dedicated to serve customers connected to the utility's distribution system or grid, or to contract for such investment with the California Consumer Power and Conservation Financing Authority.
- ✓ Eliminates direct transactions (Direct Access), including aggregation of loads and other provisions to facilitate direct transactions, between an electric service provider and retail end-use customers of an utility, on a prospective basis.
- ✓ Require all metering of customer usage of electricity and customer billing to be performed by the utility in that metering customer usage of electricity is an integral part of the electricity distribution system, and is the responsibility of the utility.
- ✓ Prohibits residential and small commercial customers being required to take service under a time-differentiated rate without prior consent.
- ✓ Eliminates the Power Exchange
- ✓ Deletes provisions relative to the ISO participation in FERC activities.
- ✓ Requires the Legislature to approve the entry of the ISO into a multistate or regional transmission organization, and would repeal that provision regarding the adoption of

standards for transmission facilities by the ISO.

- ✓ Establishes a Ratepayer Refund Account for each utility, into which would be paid any funds recovered by utilities resulting from litigation or agreement relative to the charging of excessive costs for wholesale electricity by electrical generators. All funds would be held in trust on behalf of ratepayers.
- ✓ Establish a comprehensive integrated resource planning process under regulation, in order to ensure resource adequacy, including investing in cost-effective energy efficiency and conservation programs, and increasing the proportion of electricity provided from cost-effective renewable resources.
- ✓ Simplify corporate ownership of utilities by requiring transparent forms of corporate ownership of public utilities, by improving accountability for holding company requirements in state law and by seeking enforcement of the Public Utilities Holding Company Act of 1935.
- ✓ Provide for fair cost allocation among customers in just and reasonable rates fixed through open public processes, not discriminatory retail choice or direct access transactions.

LATEST ACTION

Set, first scheduled hearing on April 21, 2003 at the SEN ENERGY, UTILITIES, AND COMMUNICATIONS canceled at the request of author.

PROS/OPPORTUNITIES

Would restore needed regulation to an industry that is not ready for free market forces.

CONS/ISSUES

May limit non-utility involvement in investment in generation.

May limit the potential for municipalities to take advantage of community aggregation as provided for by AB 117.

Utilities have warned that "cautioned that the swing back to regulation has its limits. Investor-owned utilities "have dismantled their generation, design and construction capabilities. When we rebuild, we're not going to rebuild the way we did in the past" (Greg Rueger, senior vice president of generation for Pacific Gas & Electric).

SUPPORT

OPPOSITION

Independent Energy Producers

AB 428

Richman: Utilities: core and bundled customers

SUMMARY

This bill repeals the suspension of the right of retail end use customers to acquire direct access service. The bill would require the commission, on or before January 1, 2006, to adopt guidelines for the appropriate composition of a core portfolio of electricity supplies to be established by each utility to meet the needs of the utility's bundled core customers and provide an adequate reserve capacity. Commencing January 1, 2006, an electric corporation would have no obligation to serve a noncore customer except by contract for a term of no less than 3 years and on terms approved by the commission that reimburse the utility for all costs of providing electrical service. Commencing on that date, noncore customers would be served by direct transactions or by contract with a utility. The bill would require the commission to adopt rules allowing residential bundled core customers to elect to be served by direct transactions in a manner that fully accounts for their cost of service by the utility and payments for a proportionate share of system costs, bond payments, and public benefits charges. The bill would require the commission to

adopt corresponding rules for nonresidential bundled core customers on or before January 1, 2012.

SB 429 (Morrow: Priority of capital requirements of holding companies of utilities)**SUMMARY**

This bill requires the capital requirements of the electric or gas corporation, as determined by the CPUC, to be given first priority for any holding company approved to have a controlling interest in an electric or gas corporation and requires the CPUC - when it determines capital is required to meet the electric or gas corporation's obligation to serve - to order the holding company to infuse sufficient capital of any type it deems necessary into the utility. The bill would codify current regulatory provisions of CPUC decisions.

BACKGROUND¹

Since the mid-1980's, California's investor-owned energy utilities (IOUs) have sought to form holding companies for purposes of diversification. The holding companies become the sole owner of the utilities and often times use utility profits to fund other ventures. In its simplest form, for example, Pacific Gas & Electric (PG&E) Corporation is a holding company with two separate divisions, PG&E Company and PG&E National Energy Group. Investors can only buy stock in PG&E Corporation. The CPUC has to approve all holding company requests before such a company can be created. The first to apply was the San Diego Gas and Electric Company (SDG&E) in 1985. SDG&E was concerned its monopoly position was eroding, and, consequently, it feared the company was losing its traditional status as a safe investment. To maintain its ability to attract investors, SDG&E believed it needed to seek new lines of business outside of its utility operations. Forming a holding company would facilitate the integration of non-utility ventures into the corporation by providing improved access to financing and establishing a clear separation between utility and non-utility operations. The company argued this wouldn't adversely effect the public interest because it would have no effect upon its utility operations or service to customers.

Formation of the holding company was hotly debated at the CPUC. The entity now known as the Office of Ratepayer Advocates (ORA) argued a holding company was not necessary for SDG&E to diversify, that it could jeopardize future CPUC oversight, that it would complicate proper regulatory oversight, and that a holding company would provide no benefits to ratepayers. Utility Consumer Action Network (UCAN), a San Diego-based consumer group, argued a holding company would divert company resources and management from SDG&E's utility operations, which would inevitably create conflicts of interest between the needs of the utility and its corporate siblings. In the end, the CPUC agreed to permit the formation of the holding company, subject to numerous conditions (see D.86-03-090). Those conditions included a financial requirement - which is at the heart of this bill - known as the "first priority" condition:

"The capital requirements of the utility, as determined to be necessary to meet its obligation to serve, shall be given first priority by the Board of Directors of the holding company and SDG&E."

This condition, and others, reflect concern by the CPUC that diversification through a holding company could have adverse consequences to utility ratepayers, so the conditions were designed to ensure the financial health of the utility remains paramount. SDG&E agreed to this condition, though it ultimately suspended its pursuit of a holding company because of disagreements over other conditions the CPUC sought to attach to the request.

¹ <http://www.assembly.ca.gov/acs/acsframeset2text.htm>

The CPUC's SDG&E holding company decision was the basis for later holding company decisions for all three major IOUs. Each of these decisions contain many conditions virtually identical to those found in the original SDG&E decision discussed above, including the first priority condition. The CPUC's concerns about the financial health of the utility in a holding company structure has been consistent, as has the holding company's acceptance of these conditions.

In late 2000 and early 2001, California's energy crisis was in full flower. Wholesale electric costs were skyrocketing, causing the utilities severe financial difficulties as they labored to cover these costs after agreeing to a retail rate freeze as a part of California's deregulation statutes. IOUs weren't able to buy power, causing the state to step in first with a \$400 million emergency appropriation to cover less than two weeks worth of power purchases, then later with a directive to require the Department of Water Resources to temporarily assume power buying responsibilities on behalf of California's electricity customers. The CPUC raised electric rates by over 40% to help cover the ongoing cost of power. PG&E filed for Chapter 11 bankruptcy protection, while SCE threatened a bankruptcy filing and pursued a negotiated financial settlement both legislatively and at the CPUC, where they were eventually successful.

While the financial position of the utilities became precarious, the utility holding companies managed to stay out of harms way. Both PG&E Corporation and Edison International, the holding companies for PG&E and SCE, used a technique known as "ring fencing" to shield the holding company assets, making them unavailable to help the utility. In April 2001, the CPUC initiated an investigation into whether PG&E Corporation, Sempra Energy, and Edison International complied with the conditions contained in the decisions which allowed their creation, including the first priority condition.

The holding companies have objected to the CPUC's investigation, arguing the CPUC has no jurisdiction over the holding companies because the holding companies aren't public utilities. They also contend the term "capital" means equity capital, not operating capital, which is what the IOUs needed during the energy crisis. While the holding companies failed to inject additional operating funds into their utilities during the energy crisis, there was no failure to provide adequate equity capital. Hence, the holding companies argue they weren't in violation of the first priority condition, according to the holding companies.

In January 2002, the CPUC found there was no basis for limiting the meaning of capital to equity capital in any of the holding company decisions. The holding companies challenged this decision to the Appellate Court in December 2002, but hearings the issue have yet to be held.

Questions Before The Court

Is A Utility Holding Company A Public Utility?

The holding companies argue they are not public utilities. Therefore, they believe the holding company decision is a contract between them and the CPUC, and is therefore only enforceable through a court. While this question will be resolved by the court, the Public Utilities Code seems clear. PU Code Section 216 defines a "public utility" as any "electrical corporation." PU Code Section 218 defines an "electrical corporation" as an corporation owning or controlling any electric plant for compensation. Because the utility holding companies own 100% of the stock of their underlying electric utilities - and therefore own and control the electrical corporation which owns the electric plant - it's difficult to see how holding companies couldn't be defined as public utilities.

Further, it would seem odd to statutorily permit the CPUC to authorize the creation of an entity

(such as a holding company) that it would then have absolutely no regulatory authority over. If indeed the courts find this to be the case, the author and committee may wish to consider barring the CPUC from allowing the creation of any holding companies.

Would This Constitute A Taking?

It's argued by some that this bill may be an unconstitutional "taking" by failing to provide an IOU or a holding company with an opportunity to earn a fair return on a mandated investment. That concern seems misplaced because this proposed statute is part of a larger body of statutes that collectively provide the utility with a fair opportunity to earn a return on its investment.

Are Holding Companies A Recipe For Conflicting Goals & Interests?

The energy crisis pointed out a number of inherent conflicts existing inside a holding company - 1) The need to allocate capital between the utility and its affiliates; 2) Business strategies which benefit the unregulated affiliates at the expense of the utility; 3) Diversion of management attention and resources; and, 4) Potential self-dealing, just to name a few. It's difficult to see how the existence of utility holding companies benefited utility ratepayers during the crisis or how they benefit those same ratepayers today.

RELATED LEGISLATION

SB 888 (Dunn) contains provisions that are substantially similar to this bill. However, SB 888 also contains a number of provisions and issues that aren't related to the narrow holding company subject matter addressed by this measure.

LATEST ACTION

PROS/OPPORTUNITIES

CONS/ISSUES

REGISTERED SUPPORT

None on file

REGISTERED OPPOSITION

Sempra Energy
Southern California Edison
PG&E

AB 1352: (Maddox: Municipally-owned utilities)

SUMMARY

This bill would state the intent of the Legislature to facilitate, in subsequent amendments, the most efficient operation of municipally owned utilities by restructuring the functions and duties of the various state responsible for oversight and governance of the electrical utility market.

AB 1685 (Leno: Self-generation incentive program)**Summary**

Bill requires the CPUC to administer a self generation incentive program for solar electricity generation *until January 1, 2017, in the form that exists on January 1, 2004* .

The Self-Generation Incentive Program (created by AB 970, signed by the Governor on September 6, 2000) provides \$125 million per year (\$15 million per year in San Diego) of incentive funding to renewable and non-renewable self-generation unites up to 1 MW in size (photovoltaics, wind turbines, fuel cells, microturbines, small gas turbines, and internal combustion engines to provide some or all of their electricity for onsite use). PG&E, SCE, SoCalGas, and the San Diego Regional Energy Office (serving SDG&E customers) administer the program throughout their respective service territories.

The SelfGen Incentive Program has been a critically important subsidy for the growth of solar electricity generation in California, but is set to expire at the end of 2004.

Last Activity

Heard and passed the ASSEMBLY COMMITTEE ON UTILITIES AND COMMERCE on April 21, 2003.

Committee recommendation on changing the sunset date : This bill currently requires the program to continue until January 1, 2017. The committee recommendation is to instead have this bill sunset on January 1, 2008 so that the incentive program can be reviewed at that time to determine whether it is worthwhile to continue with it or focus instead on other areas of technology.

PROS/OPPORTUNITIES

According to the REIS, clean self-generation that is incentivized by this has program is a critical component of the San Diego region's ability to meet its future electricity demand through a balanced portfolio that minimizes the risk for price volatility.

Would continue the successful SelfGen Program beyond 2004.

CONS/ISSUES**SUPPORT**

SDREO and City of San Diego Councilmembers have written letters of support.

PG&E, Shell Solar Industries, Light Energy Systems, POCO Solar Energy, Six Rivers Solar, SoCal Solar Energy, Performance Solar Inc., AMECO, EcoEnergies

OPPOSITION

SCE.

AB 1734 (Reyes: Energy Efficiency Programs)**SUMMARY**

Identifies a separate rate component to fund cost-effective energy efficiency and conservation activities. This rate component is a nonbypassable element of local distribution and collected on the basis of usage.

LATEST ACTION**PROS/OPPORTUNITIES****CONS/ISSUES**

Could eliminate third-party energy efficiency programs, which are the primary funding source of SDREO. Third-party programs are providing needed innovation and competition to IOU energy efficiency programs that are broadly supported by most parties other than the IOUs.

SUPPORT

PG&E.

OPPOSITION

CPUC on the basis that provisions calling for automatic approval of demand-side budgets “could impair the commission’s ability to fulfill its legal requirement to approve cost-effective efficiency programs.”