

Memorandum

To: ISO Board of Governors
From: Karen Edson, Vice President of External Affairs
Date: February 3, 2009
Re: *Status of State and Federal Legislative Matters*

This memorandum does not require Board action.

State Affairs

Budget and State of the State Address:

On January 15, Governor Schwarzenegger delivered a brief thirteen minute State of the State address that focused almost solely on the budget crisis with a deficit that now stands at \$42 billion. He did not discuss specific policy issues or tout accomplishments as is traditionally done in the State of the State address. Instead he communicated how dire the situation is, urged the Legislature to pass a budget and warned that California faces insolvency within weeks if an agreement is not reached.

As an incentive to pass budgets on time, which has been accomplished four times in the last 20 years, Governor Schwarzenegger suggested that he and all legislators should lose their per diem expenses and salary for each day the budget is late.

Republicans remain steadfast in their desire for a permanent cap on state spending. They also advocate rolling back environmental protections and labor regulations as a means to benefit the economy and help pull the state out of its current crisis. Their opposition to tax increases, however, seems to be softening a bit given the enormity of the deficit. Groups like the California Chamber of Commerce and Legislators such as Assembly Republican Leader Mike Villines have stated that if tax hikes become a reality, they must be broad in nature as opposed to disproportionately affecting a specific industry. This is a departure from their earlier refusal even to consider tax increases.

Newly Introduced Legislation:

So far we have identified 16 energy-related bills, including legislation by both the Assembly and the Senate that would change California's renewable portfolio standards (RPS). It is also worth noting that the Senate Pro Tem Darrell Steinberg has committed to getting a 33 percent renewable portfolio standard bill to the Governor's desk by April 2009.

Among the 16 bills that are of particular interest to the California Independent System Operator Corporation (the ISO) are:

AB 44 (Blakeslee) Energy Storage Facilities.

Existing law authorizes the California Public Utilities Commission (CPUC) to approve an increase of one-half of 1 percent to 1 percent in the rate of return otherwise allowed an electrical corporation for investment by the corporation in generation facilities using renewable resources. This bill would authorize the commission, after a hearing, to approve a similar increase in the rate of return for investment by an electrical corporation in energy storage facilities that meet specified requirements.

AB 45 (Blakeslee) Distributed Generation: small wind energy systems.

The RPS requires each retail seller to increase its total procurement of eligible renewable energy resources by at least an additional 1 percent of retail sales per year so that 20 percent of its retail sales are procured from eligible renewable energy resources no later than December 31, 2010. This bill would state the intent of the Legislature to encourage local agencies to support the state's ambitious renewable energy procurement requirements by developing and adopting ordinances that facilitate the installation of distributed generation small wind energy systems.

AB 46 (Krekorian) Energy: renewable energy resources: generation and transmission.

This bill amends California's RPS to require 35 percent by December 31, 2020 with a goal of 50 percent by December 31, 2035. It establishes flexible ranking criteria for contracts, including price, time of delivery, dispatchability, and location. Preference is given to California suppliers. It requires a benchmark price to capture cost and benefits of renewable energy as well as a cost cap for total expenditures for resources above benchmark prices. This bill also establishes the Renewable Infrastructure Authority (RIA). The Chairman of the ISO Board would hold a nonvoting seat on the RIA. The RIA would: formalize the Renewable Energy Transmission Initiative process; establish renewable energy development zones; serve as lead agency for siting renewable facilities over 5MW; identify preferred transmission corridors and site, finance and contract for transmission infrastructure between RED zones and the transmission grid.

AB 51 (Blakeslee) California Public Utilities Commission: demand-side management programs.

Existing law requires the CPUC, in consultation with the State Energy Resources Conservation and Development Commission, to adopt energy conservation demand-side management and other initiatives in order to reduce the demand for electricity and reduce load during peak demand periods. This bill would express the intent of the Legislature to enact legislation that would require the CPUC to integrate the demand-side management programs within its

jurisdiction in order to enable offerings of integrated packages that will maximize savings and efficiencies of utility program overhead.

SB 14 (Simitian, Kehoe, Padilla, Steinberg) Utilities: California Public Utilities

Commission: energy: renewable energy resources: rates.

This measure addresses a broad range of issues. Among other things the measure requires investor owned and municipal utilities to achieve a 33 percent RPS by December 31, 2020, restricts direct access and adds greater flexibility on crises era provisions that prohibit electricity rate increases for residential customers that use up to 130 percent of baseline levels.

Additionally, the measure mandates that the CEC, in consultation with the ISO and the publicly owned utilities, facilitate a process for the execution of seams agreements; the development of a statewide transmission plan and the siting and approval of new transmission lines that can be jointly owned or utilized by Investor Owned Utilities (IOUs), municipal utilities, and merchant transmission companies. The measure states that through this process transmission could be jointly operated by the ISO and municipal utilities. AB 14 also requires the ISO to undertake all feasible efforts to seek the Federal Energy Regulatory Commission's (FERC) approval of tariff changes necessary to: 1) adjust its market structure to achieve 33 percent RPS in the most cost-effective manner possible, and 2) develop a statewide transmission plan in consultation with the publicly owned utilities that incorporates the publicly owned utilities transmission plans as well as potential joint privately owned and publicly owned infrastructure projects. Finally, the bill has several provisions directed at the CPUC. It requires the Governor to appoint, subject to the approval of the Senate, a president of the CPUC from among its members, repeals the requirement that the president direct CPUC staff and requires the CPUC to hold one meeting a month in Sacramento.

SB 17 (Padilla) Electricity: smart grid systems.

This bill would require the CPUC, by July 1, 2010, and in consultation with the State Energy Resources Conservation and Development Commission (Energy Commission) and the ISO, to determine the requirements for a smart grid deployment plan consistent with the policies set forth in the bill and federal law. The bill would require each electrical corporation, by July 1, 2011, to develop and submit a smart grid deployment plan to the commission for approval and would allow the commission to authorize an electrical corporation to recover reasonable costs of deploying smart grid technologies and services from ratepayers.

SB 42 (Corbett) Coastal resources: seawater intake.

This bill would prohibit a state agency from authorizing, approving, or certifying a new power plant or industrial facility that uses an open ocean intake, a new open ocean intake, or the expansion of an existing open ocean intake. The bill also would, on and after January 1, 2015, prohibit a power plant from using once-through cooling.

Governor Schwarzenegger's Proposed Energy Reorganization Plan:

During the week of January 12, Governor Schwarzenegger's office released a proposal for reorganizing California's energy related activities. It is unclear if the Governor will move this plan forward through legislation or a Governor's Reorganization Plan. According to a summary provided by the Governor's Office, the aim of the reorganization is to consolidate the State's

authority for energy policy and related functions. Specifically, the proposal will create the California Department of Energy (CDOE) with a cabinet-level Secretary of Energy. The Energy Secretary will also serve as the Governor's Principal Advisor on energy matters, as well as the Chairperson of the newly configured Energy Commission, itself, (which would continue its current licensing and regulatory responsibilities with support from CDOE staff). The energy related functions such as transmission siting, building efficiency and appliance standards will be housed in the CDOE.

According to a summary released by the Governor's office, the proposal will streamline the siting of vital electric generation infrastructure necessary to meet the State's RPS goals, and will create within the CDOE a one-stop licensing process for renewable power plants 50 megawatts and greater, which will apply to all renewable technologies and transmission line projects.

Within the CDOE would be a newly configured California Energy Commission (CEC), chaired by the CDOE Secretary. Four other Commission members would be appointed by the governor and subject to Senate confirmation. In addition, three ex officio members would serve on the Commission, including the Chief Operating Officer of the ISO.

A newly created Office of Energy Market Oversight would assume the responsibilities of the EOB and be tasked with overseeing the ISO by acting as the appeal body for ISO board members regarding certain ISO board decisions and by approving any amendment to ISO bylaws following adoption by the ISO board.

Additionally, the CDOE would conduct market monitoring and oversight functions in conjunction with the ISO.

Committee Membership:

Senate Energy, Utilities and Communication Committee: Senator Alex Padilla, Chair; Senator John Benoit, Vice Chair; Senators Ron Calderon; Joe Simitian; Alan Lowenthal; Christine Kehoe; Rod Wright; Ellen Corbett; Dave Cox; and Tony Strickland. There are 7 Democrats and 3 Republicans on the Committee.

Senate Rules Committee: Senator Steinberg, Chair; Senator Sam Aanestad, Vice Chair; Senators Gil Cedillo; Bob Dutton; Jenny Oropeza. There are 3 Democrats and 2 Republicans on the Committee

Assembly Utilities and Commerce Committee: Assemblyman Felipe Fuentes, Chair; Assemblyman Michael Duvall, Vice Chair and no other Committee Members have been named.

Federal Affairs

The New Administration:

President Barak Obama's inaugural speech cited the building of electric grids and harnessing the power of renewable energy as important parts of the "work to be done" to create new jobs and

lay a foundation for national growth. His choices for the Administration's energy and environment team include veteran policymakers and administrators that combine strong scientific credentials with a demonstrated commitment to moving the President's agenda forward.

When President Obama announced his choices for top energy and environmental posts in his Administration, he stated: "Consistently, California has hit the bar and then the rest of the country has followed." He selected Steven Chu, Director of the Lawrence Berkeley National Laboratory, to be Secretary of Energy and Los Angeles Deputy Mayor Nancy Sutley to head the White House Council on Environmental Quality. Carol Browner, a Californian who was President Clinton's EPA Administrator, will assume the newly-created position of Assistant to the President for Energy and Climate Change. Obama has also named Phil Shiliro, a long-time aide to Congressman Henry Waxman and former American Wind Energy Association staffer, as the White House liaison to Congress.

In addition to these California picks, Obama selected Lisa Jackson, the former chief of the New Jersey Department of Environmental Protection, to head EPA; Congressional Budget Office Director Peter Orszag, an expert on cap-and-trade policies, to head the Office of Management and Budget; and Colorado Senator Ken Salazar to head the Department of the Interior. The designees have already gone before Senate committees prior to full Senate votes on their nominations, which are expected to be non-controversial. The position of Commerce Secretary, which is expected to be a key part of the energy/environment team, remains unfilled at this writing. Obama has stated that he will appoint most of his cabinet secretaries to a National Energy Council to focus on transition to a low-carbon economy and that he will also create an interagency Energy Innovation Council to develop energy research and development priorities.

It should also be noted that President Obama has tapped a number of Californians for other prominent positions in his Administration, including Congresswoman Hilda Solis to be Secretary of Labor, Leon Panetta as Director of the CIA, and Christine Romer to head the Council of Economic Advisors.

The 111th Congress:

Democrats hold a 256 to 178 majority in the House and appear to have an edge of 59 to 41 in the Senate, including two Independents. Senate membership is still unsettled pending results in Minnesota. In addition, three Democratic Senators have resigned to join the new Administration (Biden, Clinton and Salazar).

As in the Administration, much of the energy-environment action on the Hill will be dominated by Californians, with Senator Barbara Boxer chairing the Senate Environment and Public Works Committee, Congressman Henry Waxman chairing the House Energy and Commerce Committee, and House Speaker Nancy Pelosi leading the charge. All three are strong advocates of clean air protections, conservation and energy efficiency and all have supported actions by California and other states to impose greenhouse gas controls on vehicles, mandate renewable portfolio standards and enact economy-wide global climate legislation.

Economic Recovery:

House Democratic leaders began unveiling their \$825 billion economic recovery package in mid-January with draft legislation from key committees. The plan includes \$550 billion in spending proposals and \$275 billion in tax breaks, but no earmarks.

On the appropriations side, roughly 10 percent of the funding in the plan is focused specifically on energy projects, including the following funding areas:

- \$11 billion for research and development, pilot projects and federal matching funds for the Smart Grid Investment Program to modernize the electric grid for improved efficiency, security and reliability and to construct new power lines for renewable energy resources;
- \$8 billion for loans for renewable power generation and transmission projects;
- \$9.4 billion for energy efficiency projects for state and local governments and low-income housing retrofits;
- \$2 billion for energy efficiency and renewable energy research aimed at reducing carbon emissions and cutting utility bills, with funds to be awarded competitively to university, companies and national laboratories;
- \$2 billion for an Advanced Battery Loan Guarantee and Grants Program to support U.S. manufacturers of advanced vehicle batteries and battery systems;
- \$1.5 billion in energy efficiency grants and loans for school districts, higher education institutions, local governments, and municipal utilities;
- \$500 million for energy efficiency projects in manufacturing sector;
- \$200 million for grants to encourage new electric transportation technologies;
- \$300 million for high-efficiency appliance rebates;
- \$2.4 billion for carbon capture and sequestration.

The tax package includes long-term extension of renewable energy production tax credits, a temporary program to allow an investment tax credit in lieu of the production tax credit, Clean Renewable Energy Bonds, and tax incentives for energy efficiency and conservation.

Global Climate:

President Obama has called for a mandatory, economy-wide cap-and-trade program to cut greenhouse gases 80 percent by 2050. The federal agency with authority for implementing the policy is still to be determined. Obama has indicated that he might use the EPA and the Clean Air Act as the main federal tools for greenhouse gas control through issuance of an endangerment finding by the Administration declaring greenhouse gas emissions a threat to public health or welfare, which would clear the way for expanded regulations on power plants, automobiles and other major sources of emissions.

Along the same lines, Senator Boxer has promised that her new cap-and-trade bill will be much more streamlined than the lengthy climate bill she introduced with Senators Joe Lieberman and John Warner in 2008. Many observers believe that AB 32 might serve as a legislative model,

directing the Administration and EPA to set up a cap-and-trade program and taking the most contentious and complex decisions – including allocations of hundreds of billions of dollars in emission credits – out of the hands of Congress.

Transmission:

There is strong acknowledgement in Washington that expanding renewable energy production will depend on expansion of the transmission infrastructure, including the possibility of giving FERC additional authority for siting and expediting permits for transmission lines. A number of coalitions that include environmental organizations, labor, business interests, and industry associations are working on legislative proposals. Proponents are expected to include such a transmission component in an omnibus energy bill that will be taken up later in the year.

Renewable Portfolio Standards:

Both House and Senate leaders have voiced support for a federal mandate to generate up to 25 percent of the nation's electricity from renewable resources within the next two decades, a goal that President Obama has also endorsed. This is also expected to be part of the omnibus energy bill.

Federal Energy Regulatory Commission:

FERC is widely expected to gain stature as a federal agency in the coming year, with potential jurisdictional growth to include transmission siting, permitting, and cost allocation, and perhaps even a role in the oversight of greenhouse gas allowances. President Obama is expected to name a new chair for the agency to replace outgoing chairman Joseph Kelliher within the next several weeks. State/Federal jurisdictional issues, Smart Grid standards, transmission planning, and Demand Response are some of the big issues that the Commission will likely be looking at in 2009.