Community Choice Aggregation—An Alternative Way to Providing Electricity Service By Local Government

*By Greg Stepanicich**

I. INTRODUCTION

Historically in California, a city could provide electricity to its residents by creating a municipal electricity utility that both purchased and distributed electricity to its resident customers.[1] But in the modern era, due to financial, legal and political constraints, relatively few cities provide electricity to their residents. Instead, most cities are served by private investor-owned utilities. Yet a new trend may bring California back to its municipal utility roots.

In 2002, after the electricity deregulation meltdown in California, the state legislature adopted a statute authorizing cities and counties—either individually or jointly through a joint powers authority—to conduct what is called a community choice aggregation program.[2] Under community choice aggregation, a local public agency can purchase electricity on behalf of its resident customers and the existing investor-owned utility is required to distribute this electricity from its distribution infrastructure. This program allows local government to control the pricing and carbon content of the electricity provided in its community without the capital costs of building a distribution network. At the time of the electricity deregulation crisis, the investor-owned utilities supported this legislation.

But on December 19, 2008, a joint powers authority that later became known as Marin Clean Energy ("MCE") was formed by the County of Marin and seven cities and towns within that county to take advantage of the community choice aggregation legislation. The Pacific, Gas and Electric Company ("PG&E) vigorously opposed MCE and its efforts to become the first community choice aggregation program established in California.

Today, MCE has grown to include all eleven cities and towns within the County of Marin, as well as the City of Richmond, the City of San Pablo and the County of Napa. This article uses MCE as a case study of the key legal issues and political challenges facing the use of the innovative community choice aggregation program.

II. THE ENABLING STATUTE

Public Utilities Code section 366.2, the enabling statute for community choice aggregation, provides the basic framework for establishing this program. For the remainder of this article, community choice aggregation will be referred to by its shorthand name, CCA. The local public agency conducting the CCA program is responsible for purchasing or generating electricity for its customers and the incumbent investor-owned utility is required to distribute this electricity to these customers through its existing infrastructure. Customers are charged a generation rate by the public agency and a distribution rate by the investor-owned utility.

Section 366.2 prohibits CCA programs within any area served by a local government-owned electric utility. Thus, CCA programs are limited to areas served by investor-owned utilities. A public agency seeking to serve its community through CCA must offer electricity service to all residential customers within its jurisdiction and may offer its service to commercial and industrial users as well. When a public agency establishes a CCA program, extensive notice about this program must be provided to all potential customers within its jurisdiction. This notice must explain that each customer may opt out of the CCA program and keep its electricity generation service with the incumbent investor-owned electric utility. CCA is a customer opt-out program, which means that each customer within a CCA agency's jurisdiction automatically will be enrolled unless the customer affirmatively states that it is opting out of the program.

Although the California Public Utilities Commission ("CPUC") was given the power to review and approve CCA implementation plans, CCA agencies are otherwise authorized to operate for the most part without CPUC oversight. For example, customer rates are set by the CCA agency's governing body and power purchase agreements may be entered into without CPUC approval.

III. THE LEGAL STRUCTURE FOR MARIN CLEAN ENERGY

Like many states, California law authorizes cities, counties and other public agencies to join together to establish by written agreement a joint powers authority ("JPA").[3] Under the Joint Exercise of Powers Act, the parties to a joint powers agreement can exercise those powers common to them to address a shared problem or program. Furthermore, Public Utilities Code section 366.2 expressly authorizes cities and counties in California to establish and operate a CCA program pursuant to a joint powers agreement. Under such an agreement, a separate legal entity may be established that is governed by its own legislative body.

The MCE joint powers agreement provides for MCE to be a separate legal entity governed by a board of directors consisting of one elected official appointed by the governing body of each member. MCE has the power to enter into contracts in its name, acquire and manage buildings and other facilities, including electricity generation facilities, incur debt as permitted by state law and hire staff.

IV. KEY ISSUES ADDRESSED BEFORE THE FORMATION OF MARIN CLEAN ENERGY

A. Liability and Risk Allocation Issues

Under Government Code section 6507, a joint powers agreement may provide that the debts, liabilities, and obligations of a JPA are not the debts, liabilities or obligations of the individual members of the JPA. This was a critical protection to the local entities in Marin County exploring CCA. None of the local public agencies were willing to risk exposing their general funds to the debts, liabilities and contractual obligations of a CCA program under which power purchase agreements would be entered into to purchase electricity for distribution to its customers. Creating a liability firewall was an essential part of establishing the CCA program. Without it, MCE would not have been formed.

In California, only one published appellate court decision, *Tucker Land Company v. State of California,*[4] has addressed the liability of the members of a JPA. The *Tucker* decision involved a real estate deal gone bad in which the defendant Mountains Recreation and Conservation Authority ("Mountains Conservation Authority") was held liable for over $6 million in damages awarded in a prior lawsuit to the Tucker Land Company ("Tucker"). In the subsequent action, Tucker sought a declaration that the constituent members of the Mountains Conservation Authority were jointly and individually liable for this obligation.

The Court of Appeal in *Tucker* rejected this argument, relying upon Government Code section 6507 and language in the Mountains Conservation Authority's joint powers agreement insulating the members from the authority's debts, liabilities and obligations. Further, the court rejected the argument that the members of the Mountains Conservation Authority should be liable for its obligations on an alter ego (piercing the corporate veil) theory. In rejecting this argument, the *Tucker* court noted that the Mountains Conservation Authority had followed the organizational formalities of establishing and operating a JPA and that Tucker presumably was aware of the provisions of its formation agreement. However, in *dicta,* the court noted that this liability firewall only applied to contractual liabilities and not tort liabilities.

Due to the risk of potential tort liability arising from MCE's operations, two safeguards were implemented by MCE. First, MCE's joint powers agreement provides that the MCE will defend, hold harmless and indemnify its members from the negligent acts or omissions or willful conduct of MCE. Second, this indemnity is supported by insurance policies held by MCE naming the members as additional insureds.

In addition, MCE has implemented a third layer of liability protection. All contracts entered into by MCE require the party contracting with MCE to agree that its only legal recourse is against MCE and that the contracting party would have no legal rights or remedies against the individual members. This contractual provision substantially reduces the risk of an alter ego liability claim being brought against members of MCE in a future dispute.

These multiple layers of liability protection provided sufficient assurances to Marin County and the participating cities and towns to enter into a joint powers agreement and participate in a CCA program.

B. Governance

Another key organizational issue for MCE was the establishment of a voting system for MCE's board of directors that protected the interests of both large and small members. When MCE was first formed, its membership was limited to Marin County and the cities and towns within it, which ranged in size from approximately 2,000 to 50,000 residents. Thus, the electrical load of each member would vary greatly. The bigger members wanted a voting system that accounted for their larger electrical loads while the smaller cities wanted to insure that board decisions were not dominated by the larger members, leaving the smaller members with effectively no voice.

The solution to this potential problem was a two-tiered voting system. For a matter to be approved, it must receive both a majority vote of the members and a majority vote of the electrical load. Exceptions are provided for a limited number of matters requiring a two-thirds vote such as amending the joint powers agreement or terminating a member for materially violating the provisions of the joint powers agreement.

MCE needed to be established before a power purchase agreement could be negotiated and executed. However, the members were reluctant to commit to the CCA program until they knew whether a viable, financially sound power purchase agreement could be entered into with a reliable energy provider. To address this concern, a provision was added to the joint powers agreement requiring MCE to provide a copy of the initial power purchase agreement at least 90 days prior to consideration of the agreement by MCE's board of directors and each member was given the right to withdraw from MCE without any cost upon 30 days prior written notice to MCE and its members.

C. The CEQA Challenge

Prior to adoption of its first power purchase agreement ("PPA") with Shell Energy of North America ("SENA") in 2010, PG&E contended that MCE needed to prepare an environmental impact report under the California Environmental Quality Act ("CEQA"). [5] PG&E argued that the contract with SENA would result in the creation of more greenhouse gas emissions than the status quo of electricity service provided only by PG&E. Attorneys for the International Brotherhood of Electrical Workers Local 1245 have continued to make this argument with respect to new local public agencies considering whether to join MCE as a member.

The SENA contract required that at least 25% of the delivered electricity be from renewable energy sources. This standard exceeded the renewable energy sources purchased by PG&E. The contract also provided a 100% renewable energy option for customers. Further, a provision was added to the contract that required the carbon content of the electricity provided by SENA to be equal to or less than the carbon content of the electricity supplied by PG&E. Another important factor was that the electricity service provided by MCE did not involve the construction of any new facilities.

In approving the SENA contract, the MCE board of directors determined that the action was not subject to CEQA and was otherwise exempt from further environmental review. Specifically, the board determined that the approval of the SENA contract and the commencement of the CCA program was not a "project" for purposes of CEQA, as the contract and the resulting purchase of electricity for sale to customers was not the type of activity that could cause either a direct physical change in the environment or a reasonably foreseeable indirect physical change in the environment. In this regard, the MCE board considered that the CPUC had a history of treating PPAs, including those entered into by PG&E, as actions that were not subject to CEQA review. Like the SENA contract, those PPAs did not involve the construction of new facilities, but instead the buying and selling of electricity from existing facilities. The MCE board determined that the action before it was similar and essentially a financial transactions that did not require the construction of new facilities. The MCE board further determined that such purchases of electricity on the open market from separately permitted facilities was therefore not a "project" for purposes of CEQA and was otherwise an activity that posed no possibility of having a significant effect on the environment under Section 15061(b)(3) of the CEQA Guidelines.

The MCE board also determined that the approval of the SENA contract and the commencement of the CCA program was categorically exempt under Section 15308 of the CEQA Guidelines. This section provides what is known as a Class 8 categorical exemption and states:

> [A] Class 8 [exemption] consists of actions taken by regulatory agencies, as authorized by state or local ordinance, to assure the maintenance, restoration, enhancement, or protection of the environment where the regulatory process involves procedures for protection of the environment. Construction activities and relaxation of standards allowing environmental degradation are not included in this exemption.

The MCE board determined that the commencement of the CCA program by MCE was a regulatory activity for the protection of the environment. The regulatory activity was the establishment of specific criteria by the MCE Board for the purchase and sale of electricity that would result in the increased use of renewable energy and the reduction of greenhouse gas emissions.

On the administrative level, PG&E challenged these CEQA determinations. In part, PG&E argued that MCE was not a regulatory agency for purposes of the Class 8 categorical exemption. This argument was without merit as MCE is a joint powers authority made up of cities and counties and has the same broad police powers as its members, including the power to enter into contracts with regulatory components. Ultimately, no CEQA challenge was filed in court by any party during the 35 day statute of limitations period after MCE filed its notice of exemption.

D. Political Maneuvers

Two extensive political maneuvers also have been launched against the establishment of CCA programs in California. As MCE began to implement its CCA program, a ballot measure heavily supported by PG&E was placed on the June 2010 statewide primary election ballot. Proposition 16 would have required a two-thirds local voter approval before a local government could establish a CCA program, use public funding to implement a plan to become a CCA provider, or expand CCA electricity service to new territory or customers. The voters rejected Proposition 16, despite over $46 million being spent in support of this proposition, with most funding coming from PG&E.

In 2014, another legislative attack on CCA programs was mounted through the introduction of AB 2145. Initially this bill would have required CCA programs to be conducted as an opt-in rather than an opt-out program. In other words, a CCA could not enroll customers into its program unless the customer specifically elected to join the program. This change in the law would have made CCA programs very difficult, if not impossible, to implement. However, based on widespread and growing opposition to the bill, it was amended to delete the opt-in requirement with a requirement that a CCA could serve no more than three contiguous counties. State law normally does not place independent territorial limits on JPA's within the state, as the territory of a JPA is determined by the jurisdictional boundaries of the government agencies that make up the JPA. This was an unprecedented limitation aimed at the success of MCE's program that was gaining interest from a number of local agencies in the San Francisco Bay Area. This bill died in the State Senate at the end of the legislative term.

V. LOOKING FORWARD

Since the formation of MCE, another JPA called Sonoma Clean Power out of Sonoma County became the second CCA in California with electricity service starting in 2014. Alameda County currently is studying the establishment of a CCA program as well. Other cities and counties throughout California also are either studying or expressing an interest in pursuing community choice aggregation in their communities. CCA provides a vehicle for cities and counties to increase the consumption of renewable energy and promote a variety of energy efficiency programs that do not rely on profit-based decisions made by investor owned utilities. In the end, consumers are given greater choice in the electricity they purchase.

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Endnotes

1 *See* Municipal Utility District Act, Cal. Pub. Utilities Code §§ 11501 *et seq.*

2 Cal. Pub. Utilities Code § 366.2.

3 Cal. Gov. Code §§ 6500 *et seq.*

4 *Tucker Land Company v. State of California* (2001) 94 Cal.App.4th 1191.

5 Public Resources Code §§ 21000 *et seq.*

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