BEFORE THE PUBLIC UTILITIES COMMISSION

OF THE STATE OF CALIFORNIA

Application of Pacific Gas and Electric Company for Authority, Among Other Things, to Increase Rates and Charges for Electric and Gas Service Effective on January 1, 2011.	Application 09-12-020 (Filed December 21, 2009)
Order Instituting Investigation on the Commission's Own Motion into the Rates, Operations, Practices, Service and Facilities of Pacific Gas and Electric Company.	Investigation 10-07-027 (Filed July 29, 2010)

LATE-FILED NOTICE OF EX PARTE COMMUNICATION

Pursuant to Rule 8.3(a) of the Commission's Rules of Practice and Procedure, The Utility Reform Network (TURN) gives notice of the following *ex parte* communication. On December 17, 2010, at approximately 6:00 p.m., Robert Finkelstein, TURN's Legal Director, conveyed by e-mail the attached letter to Scott Murtishaw, advisor to Commission President Michael Peevey, with a copy to ALJ David Fukutome. TURN had intended to serve the letter on all parties on the service list for the proceeding on that date, but inadvertently failed to do so.

The letter addresses TURN's position that PG&E should not earn its authorized rate of return on electromechanical meters that have been replaced by SmartMeters and are therefore no longer used and useful. It specifically addresses the options for amortizing the remaining investment, explaining that the Commission has discretion to adopt a shorter period than the eighteen years proposed by PG&E, but also citing reasons supporting use of the longer period. The letter also addresses the Pacific Bell decision

that PG&E cited for the first time in its reply brief, and explains why the core principle followed in that decision is most consistent with TURN's recommendation in this proceeding.

Copies of this Notice may be obtained by contacting Larry Wong at 415-929-8876, x. 300 or adminassistant@turn.org.

December 21, 2010 Respectfully submitted,

By: ____________/S/________________

Robert Finkelstein
Legal Director

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December 17, 2010

Scott Murtishaw
California Public Utilities Commission
505 Van Ness Avenue
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Re: PG&E 2011 GRC Meter Issues – A.09-12-020

Dear Scott:

Early last week we spoke by phone about the PG&E GRC and, in particular, TURN's proposal to permit recovery of the investment in the electromechanical meters replaced by SmartMeters, but no return on that investment because it is no longer "used and useful." Some of the discussion waw related to contentions PG&E raised for the first time in its reply brief. At the time I committed to reviewing those contentions and following up with you after doing so. My apologies for the delay in getting back to you on this; as I suspect you know better than I do, it's been a busy period leading up to yesterday's final Commission meeting of 2010.

The Amortization Period

One question that came up during our discussion was TURN's use of PG&E's proposed amortization period of eighteen years, rather than a shorter period (typically 5-6 years) as the Commission has used in its decisions when it addressed prematurely retired plant in past decisions. PG&E did not challenge TURN's proposal to use the 18-year amortization period in its rebuttal testimony or its opening brief, but instead chose to challenge this element of TURN's proposal for the first time in its reply brief.

As I noted during our phone conversation, TURN does not dispute that the Commission has the discretion to adopt a shorter amortization period for recovery of the remaining investment in the retired meters. PG&E has requested a 2011 revenue requirement of approximately $64 million revenue requirement for the meters that are no longer in service (approximately $20 million for amortization and $44 million for return on the remaining investment). If that $64 million annual figure were instead devoted entirely to amortization beginning in 2011, the remaining investment of $341 million would be fully recovered in just over five years. (TURN Reply Brief, pp. 20-21)

However, TURN submits that the eighteen-year amortization period proposed by PG&E is an appropriate alternative under the circumstances present here. Given the current economic climate in PG&E's service territory, the Commission should welcome the opportunity to keep rates lower than they would be under a five-year amortization. Furthermore, maintaining PG&E's cost recovery period at eighteen years rather than some shorter period is appropriate, given the delays experienced in installing and activating meters and the resulting reduction and postponement of substantial portions of the benefits described in D.06-07-027 and D.09-03-026.

The utility would have an opportunity to seek a different amortization period in its next GRC, should it so desire.

The Pacific Bell Decision

We also discussed D.83-08-081, a decision addressing depreciation issues for Pacific Telephone and Telegraph (Pacific) from back when the phone utilities were subject to cost-of-service ratemaking. Again, PG&E did not mention this decision in its opening brief, even though the utility's reply brief describes it as "the Commission decision that is most on point." (PG&E Reply Brief, pp. 18-19.) More importantly, PG&E's reply brief misses an important distinction between the circumstances underlying the Pacific decision and the issues before the Commission in this GRC. The phone company continued to provide utility service through some of its pre-existing equipment that remained in rate base and, therefore, continued to be "used and useful." As the Commission well knows, a central premise of PG&E's SmartMeter program is that it will replace the entire population of electromechanical meters in the near future.

To understand the import of the Pacific decision, one needs to look at D.93367 (6 CPUC 2d 441), the 1981 decision in a Pacific general rate case. As the Commission explained, the regulated phone companies were facing growing competition from firms such as MCI. One element of such competition was that phone company customers could now own telephone terminal equipment, and the incumbent phone monopolies were to form "fully separated terminal equipment subsidiaries to handle the deregulated activities." (*Id.*, at 532.) These changes caused the Commission to focus on the need

> to ensure that customers of the remaining regulated portions of the phone systems are treated fairly during and after the transition, the assumption being that competition will take care of unregulated operations. Costs associated with the establishment of the fully separated operations must be borne by those operations, and terminal equipment investment and associated tax and depreciation reserves left with the still-regulated portions should reflect accurately the remaining physical plant <u>necessary to serve the regulated sector</u>, on which, of course, revenues to recover the investment with a return will be required. (*Id.*, p. 533 [emphasis added])

Pacific engaged in a "migration strategy" that sought to encourage existing utility customers "who had unmet needs for more sophisticated terminal equipment" to abandon the older terminal equipment in favor of "flagship equipment." The abandoned equipment was no longer "used and useful" (or, as the Commission described it, no longer "necessary to serve the regulated sector"). The Commission ordered further hearings to address appropriate costing procedures, and in particular the impact of the "migration strategy" marketing campaign.

In D.83-08-081, the Commission followed up on the issues first discussed in D.93367. As PG&E noted in its reply brief, only costs that were attributable to the premature retirements associated with the success of the migration strategy were removed from rate base. However, this is because the other costs were associated with the remaining physical plant that continued to serve

customers of the regulated utility. Here, of course, PG&E's SmartMeter program is premised on prematurely retiring its entire investment in electromechanical meters, such that none of those meters will be "necessary to serve" or, to put it another way, "used and useful."

In short, D.83-08-081 and its predecessor D.93367, while interesting to read for the insight in the history of telephone regulation, do not represent any erosion of the Commission's treatment of "used and useful" plant. On the contrary, the Commission removed from rate base the costs associated with plant that was no longer used and useful, while the costs associated with plant that continued to provide service to customers of the regulated utility remained in rate base. TURN submits this is entirely consistent with the treatment that we are seeking here for the investment in the retired and removed electromechanical meters.

Please let me know if you have any questions about this letter or wish to discuss these matters further.

Yours truly,

/s/

Bob Finkelstein
Legal Director

cc: ALJ David Fukutome
Service List for A.09-12-020