

**BEFORE THE PUBLIC UTILITIES COMMISSION
OF THE STATE OF CALIFORNIA**

Order Instituting Rulemaking on the
Commission's Own Motion to Adopt New
Safety and Reliability Regulations for Natural
Gas Transmission and Distribution Pipelines
and Related Ratemaking Mechanisms.

Rulemaking 11-02-019
(Filed February 24, 2011)

**TURN RESPONSE TO MOTION OF PG&E FOR APPROVAL OF
STIPULATION REGARDING THE ORDER TO SHOW CAUSE**



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I. INTRODUCTION AND SUMMARY OF RECOMMENDATIONS

Pursuant to Rule 11.1(e) and to the schedule memorialized in the Assigned Commissioner's Ruling of March 30, 2011, the Utility Reform Network (TURN) files this response to the "Motion of Pacific Gas and Electric Company for Approval of Stipulation Re Order To Show Cause" ("PG&E Motion"), filed on March 30, 2011.

PG&E and the Consumer Protection and Safety Division (CPSD) have entered into a Stipulation which purports to resolve all the allegations raised in the Order to Show Cause without any finding of guilt or innocence on the part of PG&E. The Stipulation itself was filed by PG&E on March 24, 2011.

TURN supports an expeditious resolution of the contempt claim so as to allow PG&E and other parties to focus on compiling the required records to complete the validation of pipeline maximum allowable operating pressures (MAOP), as well as to complete the pipeline testing and repair as promised by PG&E. However, TURN suggests that the Commission should adopt the Stipulation *if and only if* PG&E and CPSD agree to the following two modifications, which do not impose any new commitments on PG&E:

- The penalty for an unexcused failure to comply with the forward-looking compliance plan should be \$30 million, not just another \$3 million;
- The compliance plan should include a specific deadline for completing the testing and/or repair of 152 miles of pipeline, as committed to by PG&E in their own separate compliance plan submitted on March 21.

II. BACKGROUND

On January 13, 2011 the Commission issued Resolution L-410, which directed PG&E 1) to search for designated records for certain pipelines without a maximum allowable operating pressure (MAOP) established by hydrostatic testing, and 2) to use these records to determine a valid maximum allowable operating pressure. The original deadline for this task was February 1, 2011, but the Commission granted PG&E's request for an extension until March 15, 2011.

On March 15, 2011 PG&E submitted a "Report on Records and Maximum Allowable Operating Pressure Validation." In its filing PG&E described the extensive record search it had conducted to date. In the section entitled "PG&E's Phased MAOP Validation Approach," PG&E then described how it planned to complete the Phase 2 MAOP validation effort that will verify "that the documents identified in Phase 1 support the MAOP of each HCA segment" by the "end of 2011."¹

¹ PG&E March 15 Report, p. 12.
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In response to a March 16th letter from CPUC Executive Director Paul Clanon to PG&E President Chris Johns and the issuance of a draft Order to Show Cause, PG&E filed a Supplement on March 21.² In this Supplement PG&E more fully explained its record search and detailed its plan for validating valid the MAOP based on the records and documents resulting from its document search.

Neither the March 21 Report nor the March 21 Supplement provided any validation of the MAOP of those pipelines that had not been hydrostatically tested. The issues in dispute with respect to the Order to Show Cause phase of this proceeding are well identified in the Order to Show Cause itself.³ The primary issue raised in the Order to Show Cause is whether PG&E should be found to be in contempt of a Commission order and penalized for failing to comply with Resolution L-410.

On March 24, 2011 PG&E filed a “Stipulation Re Order to Show Cause” signed by PG&E and CPSD. The main elements of the Stipulation are:

- PG&E agrees to pay a \$3 million penalty;
- PG&E will develop an MAOP validation methodology in consultation with CPUC staff;

² “Request for Approval of Compliance Plan and Supplement to Report of PG&E on Records and Maximum Allowable Operating Pressure Validation,” March 21, 2011. (“PG&E Supplement”).

³ D.11-03-047, March 24, 2011. The Order to Show Cause reiterates the directives contained in Resolution L-410 and explains how PG&E’s March 15 submission failed to meet the Commission’s orders. Due to time constraints, TURN does not repeat all the details in the Order to Show Cause.

- PGE will complete the records search and MAOP validation for 705 miles of specified pipeline at identified deadlines, with final completion of MAOP validation by August 31, 2011;
- If PG&E fails to meet any deadlines in the Work Plan due to an “unexcused failure” it will pay a portion of an additional \$3 million as determined by the Commission.

III. THE QUESTION OF PGE’S COMPLIANCE IS NOT RESOLVED IN THE STIPULATION, AND THE STIPULATION SHOULD BE EVALUATED BASED ON ITS EFFICACY IN ENSURING FUTURE COMPLIANCE

The Stipulation resolves the Order to Show Cause by penalizing PG&E three million dollars and by establishing a Compliance Plan that includes a schedule for completing the document search and MAOP validation. The Stipulation does not determine whether PG&E was or was not in contempt of the Commission’s order and explicitly states that it does not “constitute an admission by PG&E” of any violation. PG&E agrees to pay a penalty of \$6 million, although \$3 million is “suspended” pending completion of the proposed Compliance Plan.

TURN completely agrees that we should focus our efforts on ensuring public safety, not in litigating the question of “who said what when”? However, PG&E itself raises the issue of compliance to assert that the \$6 million dollar penalty is reasonable and in the public interest. In its Motion for Approval of the Stipulation PG&E asserts that CPSD agrees that the March 21 Supplement brought PG&E into compliance with Commission Orders. This preposterous

claim must first be soundly rejected before we can analyze the efficacy of the Stipulation.

PG&E contends that a total penalty of \$6 million total is reasonable because it “is nearly as much as CPSD could have obtained if it litigated the OSC and won.”⁴ PG&E alleges that CPSD “appears to acknowledge that the Supplement brought PG&E into compliance,” based on the fact that Julie Halligan, the Deputy Director for CPSD, stated that the fine was calculated by multiplying a potential statutory penalty of \$1 million per day by six days.⁵ PG&E thus concludes that its March 21 Supplement fulfilled the requirements of Resolution L-410, so that PG&E was not in compliance only for the six days between March 15 and March 21.

PG&E’s assertions concerning CPSD’s position on compliance completely misrepresent Ms. Halligan’s actual testimony and the plain text of the Stipulation. In explaining the calculation of the penalty Ms. Halligan did not say anything about PG&E being in compliance or not on March 21.⁶ During subsequent testimony Ms. Halligan specifically agreed that PG&E “did not comply with the Commission’s resolution,”⁷ and then explained that the Stipulation is actually designed to get PG&E into compliance:

Q Am I correct that the Stipulation addresses the completion of the January 3rd NTSB urgent recommendations that were also reflected in a January 3rd letter from the Executive Director?

⁴ Motion of PG&E for Approval of Stipulation, p. 8.

⁵ Motion of PG&E for Approval of Stipulation, p. 6.

⁶ RT 169-170.

⁷ RT 178, Halligan/CPSD, in response to question from ALJ Bushey.

A It doesn't complete the entire set of NTSB recommendations. There was – the Compliance Plan refers to the first two recommendations, not the third. **So the Stipulation is designed to get at their search for the records, and they're using the records discovered during that search to validate the MAOP for these lines.** That's what the Stipulation is intended to get PG&E to accomplish quicker than they would otherwise have.⁸

Moreover, the very first sentence of the Stipulation explains that the fundamental purpose of the Compliance Plan submitted with the Stipulation is to create a schedule for PG&E to provide the requested documents and perform the MAOP validation as directed in Resolution L-410:

In order to protect public safety and expedite PG&E's compliance with the National Transportation Safety Board's urgent safety recommendations as required by Commission Resolution L-410, PG&E and Commission Staff developed a Compliance Plan appended hereto as Attachment 1.⁹

The Commission's original Order to Show Cause extensively documents the inadequacy of the March 15 Report. The March 21 Supplement added no new data. It simply explained in detail PG&E's records search and ongoing validation process. Neither the March 15 Report nor the March 21 Supplement even remotely fulfills the plain language directives of Resolution L-410.

As explained by PG&E's most senior witness, Tom Bottorff, PG&E believed that the literal requirements of Resolution L-410 were modified by two subsequent letters from PG&E to the Commission and by communications

⁸ RT 175, Halligan/CPSD (emphasis added).

⁹ Stipulation Re Order to Show Cause, March 24, 2011, ¶ 1 (emphasis added).

between PG&E and Commission staff. PG&E asserts that through these additional communications PG&E and Staff agreed that PG&E would not have to *actually complete the MAOP validation* by March 15.¹⁰

And what we said again in the January and February letters is that we can get the pressure testing done. We will have that for you on March 15th. Those letters were clear that on March 15th we would provide to you the results of the pressure tests. What would take longer what we said was to ultimately complete the validation of the MAOPs. That was always the message from early on and continues to be the message we describe here today.¹¹

Based on the content of these subsequent communications, PG&E contends that its Report and Supplement were by themselves compliant with the Commission's directives.

Indeed, PG&E made clear that *if* the Commission did not adopt the Stipulation, PG&E would introduce these other communications as evidence for the fact that the requirements of Resolution L-410 had been modified, so that PG&E did not fail to comply with a Commission order.¹² PG&E's counsel suggested that it would be a large distraction of time and resources to litigate the meaning of these subsequent communications.

As a preliminary matter, TURN finds PG&E's contentions dubious, at least based on the language of the actual letters sent by PG&E to Paul Clanon on

¹⁰ RT 152-155, Tom Bottorff in response to ALJ Bushey.

¹¹ RT 153-154, Bottorff/PG&E.

¹² RT 182, Statement of Attorney Malkin.

January 7 and February 1.¹³ In the first letter PG&E explicitly promises that “we will deliver the results of our pressure testing verification work to you on March 15, 2011.” In the second letter PG&E states that it “is aggressively and diligently working to meet the expectations of the Commission to perform our records review and verification work by March 15, 2011” and then reiterates that “PG&E is dedicated to taking all steps to ensure the safety and integrity of our gas pipeline systems, including the monumental effort of verifying the underlying records of over 1,800 miles of pipeline by March 15th.”

There is absolutely no mention in these letters that PG&E may need additional time to perform the records search and the verification process. One might argue from a legalistic sense that PG&E had not promised to “complete” the verification work in these letters. But that is irrelevant. Given the Commission’s order it was up to PG&E to request another extension if it could not complete the verification work. We do not have any information concerning any additional “oral communications” between PG&E and Commission staff.

Nevertheless, TURN agrees that we should focus our efforts on ensuring public safety, not in litigating the question of “who said what when”? However, we emphasize that precisely because we do not know at this point whether those subsequent communications actually changed the Commission’s intent in the Ordering Paragraphs of Resolution L-410, we cannot conclude that PG&E’s submissions of March 15 or 21 did or did not comply with the Commission’s

¹³ These letters were Attachments A and B to the PG&E Motion.
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orders. As a matter of law it cannot be concluded that six million dollars represents that maximum penalty that CPSD “could have obtained” if it litigated the Order to Show Cause.

If PG&E did not prevail in its position that its March 15 Report and/or March 21 Supplement complied with Commission directives, the maximum penalty could be one million dollars *still continuing until PG&E completes its MAOP validation process.*

Rather than litigating what happened in the past, the Commission should evaluate the Stipulation for its efficacy in motivating PG&E to validate the pipeline MAOPs and to test or repair its pipelines as promised in its filings. In that light, TURN suggests that the Commission adopt the Stipulation only with two changes. We suggest that these changes should not unduly burden the parties, as they do not actually impose any *new obligations* not already committed to by PG&E.

IV. THE STIPULATION SHOULD BE MODIFIED TO ENSURE COMPLIANCE AND PROMOTE PUBLIC SAFETY WITHOUT ANY NEW COMMITMENTS BY PG&E

A. THE PENALTY FOR FUTURE NON-COMPLIANCE MUST BE INCREASED

The Stipulation states that PG&E will “pay a penalty of \$6 million,” but half of that amount is “suspended” pending completion of the Compliance Plan.

TURN suggests that it is useful to separately evaluate the reasonableness of the

\$3 million payment for the already incurred violation versus the \$3 million potential penalty for possible future violations.¹⁴

The Commission has held that a penalty should be an “effective deterrent,” and has considered the severity of the offense and the conduct of the utility as factors to weigh in setting the penalty.¹⁵ In weighing the severity of the offense, the Commission has looked at actual or potential physical harm, economic harm, or harm to the regulatory process. In analyzing the conduct of the utility, the Commission has evaluated both the intention and actions of the utility as well as the size of the penalty as a deterrent in light of the financial resources of the utility.¹⁶

This case presents a somewhat unusual situation. The utility’s actions did not directly harm customers to date. However, in failing to provide the information and analyses ordered by the Commission, PG&E has delayed action on matters that are vital to ensuring physical public safety. The relationship between proper documentation and MAOP calculation and pipeline safety has been explained and emphasized in the reports and pronouncements of the National Transportation Safety Board, resulting in a public speech by NTSB

¹⁴ The Stipulation makes the future payment conditional, stating that “Upon any unexcused failure of PG&E to meet a milestone set forth in the Compliance Plan, PG&E will pay such portion of the remaining \$3 million as the Commission may find to be appropriate”

¹⁵ See, D.98-12-075, 84 CPUC 2d 155, 182.

¹⁶ See, for example, ; D.07-09-041, *mimeo.* p. 35-42 (Section VII).

Chairperson Deborah Hersman highlighting the failure of PG&E's record-keeping.¹⁷

The conduct of the utility is difficult to evaluate. As explained in the Order to Show Cause, PG&E apparently willfully misinterpreted the clear directives of the NTSB and the Commission, which requested validation of the MAOP through certain documents. This was not provided by PG&E. The extent of any willful violation is undoubtedly the topic of the defense already raised by PG&E.

In any case, TURN does not object to the \$3 million penalty for prior non-compliance. We are willing to accept at face value the magnitude of the task as documented by PG&E and accept the fact that additional time may be required to accomplish the MAOP validation task. We accept this with some reservations, given that there are significant unanswered questions concerning the reasons why PG&E has apparently relied on erroneous "Pipeline Survey Sheets" for inputting pipeline segment data into its computerized geographic information system database.¹⁸

However, we believe that the Stipulation should include much greater fines in the event of an "unexcused failure" to meet future deadlines in the compliance plan. There is no valid rationale for penalizing PG&E additionally only three million dollars if it fails to meet a six-month extension.

¹⁷ See, generally, Section 3 of the Order to Show Cause for a summary of NTSB statements and recommendations.

¹⁸ RT 52-53, K. Johnson/PG&E.

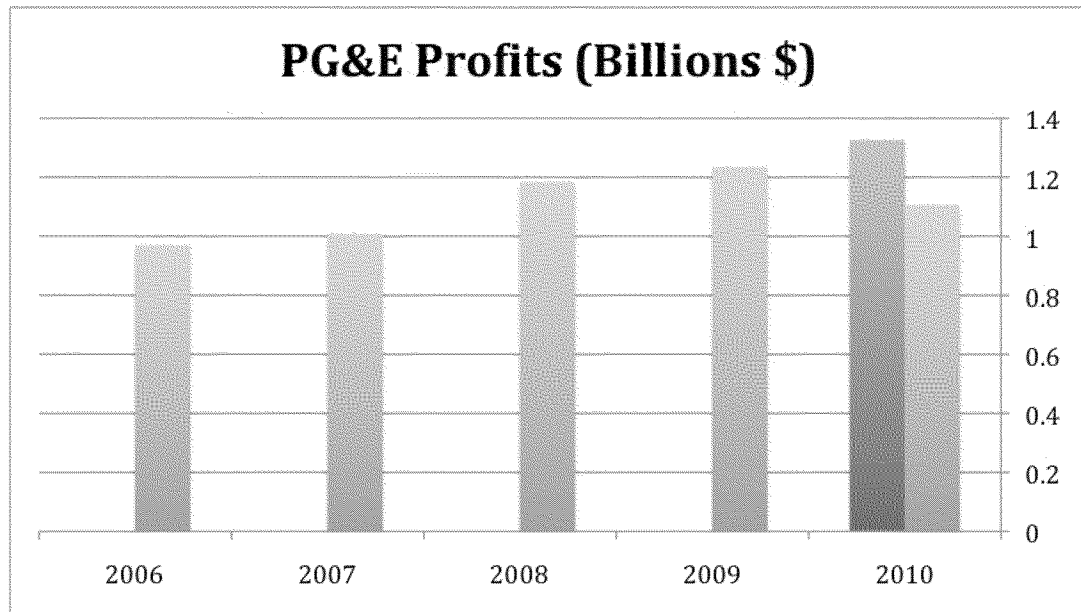
As a starting point, TURN notes that assuming a potential penalty of one million dollars per day, the maximum penalty for non-compliance from March 15 through August 31 would be over \$150 million. The Stipulation provides flexibility for the Executive Director to reprioritize the work plan or to modify the proposed schedule in case additional field work is needed. (p. 3, Work Plan footnote 3). The proposed work plan now calls for completion of the records search for various pipeline segments on June 10, July 10 and August 10; and for completion of MAOP validation for those segments by June 30, July 31 and August 31. In essence, the Stipulation provides PG&E with an additional five-and-a-half months to complete the work requested in Resolution L-410.

TURN suggests that the Commission should consider closely the second prong of the “conduct” test – the size of the penalty in light of utility resources. PG&E’s annual profits averaged \$1.1 Billion over the five years 2006-2010, and have continuously increased during this time period of financial hardship for most Americans and many companies, as illustrated in Figure 1 below.¹⁹

A one percent impact on PG&E’s bottom line is approximately eleven million. The three million dollar penalty represents less than 0.3% of PG&E’s profits.

¹⁹ PG&E can boast of joining the ranks of major financial institutions whose profits have likewise soared during this time period.

Figure 1: PG&E Utility Profits 2006-2010²⁰



TURN suggests that a more reasonable penalty for any future non-compliance would be more in the range of \$30 million, rather than the proposed \$3 million. Three million for non-compliance with an additional almost six month timeline for compliance is simply not commensurate with the task or PG&E's financial resources. Why penalize only \$3 million for a six-day failure and the same amount for a six-month failure?

²⁰ PG&E Utility Net Income for Common Stock. From 2008 and 2010 Annual Reports. Note that the decrease in 2010 already reflects San Bruno-related third-party claims costs of \$220 million, even though the utility expects "that most of the costs the utility incurs for third-party claims relating to the accident will ultimately be recovered through insurance." PG&E 2010 Annual Report, p. 2. The red bar shows 2010 net income with this \$220 million added.

In its Motion PG&E obliquely cautions that “it would not serve the public interest to impose forward-looking penalties that would incentivize PG&E to move more quickly than is prudent or possible without sacrificing the accuracy of the finished product.”²¹ As discussed above, the Stipulation explicitly allows the Executive Director to modify the schedule if more field work is needed. There is obviously a balance that needs to be struck between expeditious activity and accuracy. However, that balance is out of kilter if the penalty for failing to complete the task that PG&E promised to complete by March 15 in another six months is just three million dollars.

B. THE STIPULATION SHOULD ALSO INCLUDE WITHIN THE WORK PLAN THE PIPELINE TESTING OR REPLACEMENT THAT PG&E HAS ALREADY COMMITTED TO DOING

The Stipulation was filed three days after PG&E filed its “Request for Approval of Compliance Plan and Supplement to Report.” In that filing, PG&E explicitly committed to testing or replacing in 2011 the 152 miles of pipeline without pressure records that are similar to the San Bruno pipeline. These are the same 152 miles for which PG&E intends to complete document search and complete the MAOP validation by June 30, 2011 in the Stipulation Work Plan.

The Stipulation does not include within it PG&E’s explicit commitment. While TURN appreciates that PG&E has reiterated its promise to complete the testing or replacement in 2011, we cannot understand why this promise was not

²¹ PG&E Motion, p. 10.

memorialized in the Stipulation, to make clear that a financial penalty would apply if PG&E did not complete this work absent an excused failure.

PG&E explained at the hearings that the exact scope of work for the testing or replacement may be impacted by the results of the MAOP validation process. However, PG&E did not claim that any such changes would preclude it from completing the testing or repair of the 152 miles of pipeline in 2011. PG&E should put its money where its mouth is and include this commitment explicitly in the Stipulation. If PG&E believes that it may require any additional time for completing this work, PG&E and CPSD should come up with a realistic schedule to include in the Work Plan.

V. CONCLUSION

TURN strongly supports concluding the Order to Show Cause phase of this Rulemaking in an expeditious manner so that parties can focus on vital issues related to pipeline safety and maintenance. However, the proposed Stipulation does not provide sufficient incentive for PG&E to comply with the documents search and MAOP validation detailed in the Work Plan. The Commission should allow PG&E and CPSD to modify the Stipulation to increase the remaining fine for any future non-compliance to \$30 million and to include a deadline for PG&E to complete its proposed work on testing or replacing 152 miles of pipeline.

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