**BEFORE THE PUBLIC UTILITIES COMMISSION**

**OF THE STATE OF CALIFORNIA**

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| 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) |

# NOTICE OF EX PARTE COMMUNICATION

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December 18, 2012

Pursuant to Rule 8.4 of the Commission's Rules of Practice and Procedure, The Utility Reform Network (TURN) gives notice of the following ex parte communication.

On December 13, 2012, Thomas Long, TURN's Legal Director, met with Commissioner Sandoval's Energy Advisor, Colette Kersten. The meeting took place at the Commission's office in San Francisco from approximately 3:00 p.m. to 3:30 p.m. The communication consisted of an oral presentation accompanied by a written handout, a copy of which is attached.

In the meeting, Mr. Long discussed the points in TURN's handout regarding the proposed decision (PD) on the Phase 1 Pipeline Safety Enhancement Plan (PSEP) proposed by Pacific Gas & Electric Company (PG&E), namely: (1) the PD erroneously requires ratepayers to pay for pipeline replacement costs that result from PG&E's failure to maintain the required records to document safe operating pressure; (2) the PD's approved scope of Phase 1 is excessive and needs to be corrected to remove projects that PG&E will not perform in Phase 1; (3) the PD provides ratepayer funding for replacement projects under Decision Tree Box M2 that PG&E's expert witnesses admit are unnecessary, as supported by the document attached to the handout; (4) the five-year ROE reduction is entirely justified and, in fact, should be longer to avoid rewarding PG&E for its mismanagement of its pipeline system and to avoid giving PG&E an incentive to undertake unnecessary pipeline replacement projects; (5) the PD properly denies contingency costs; and (6) the PD's denial of recovery for 2012 costs is compelled by the rule against retroactive ratemaking and the implicit denial of PG&E's request for a memorandum account was a sound exercise of the Commission's discretion, which the

Commission has previously exercised to the benefit of utilities and the detriment of consumers.

December 18, 2012

Respectfully submitted,

_____/s/_____
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# ATTACHMENT

TURN
THE UTILITY REFORM NETWORK
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Ex Parte Meeting
R.11-02-019: PG&E PSEP Proposed Decision
December 2012

**Background to PG&E's Pipeline Safety Enhancement Plan (PSEP)**

- San Bruno 9/9/10 explosion: 8 dead, 58 injured, 38 homes destroyed, another 70 homes damaged

- Key NTSB Accident Report findings (pp. 107-110, 116-118):
  - PG&E had inaccurate pipeline records
  - PG&E exercised inadequate quality control
  - PG&E's Integrity Management Program was deficient and ineffective
  - The multiple and recurring deficiencies in PG&E operational practices indicate a systemic problem; this was an "organizational accident" (pp. 117-118)
  - "The NTSB is concerned that the PG&E GIS still has a large percentage of assumed, unknown, or erroneous information for Line 132 and likely its other transmission pipelines as well." (p. 110)

- Key Independent Review Panel Report findings (pp. 7-13, 16-18, 48-54):
  - PG&E's top management was focused on financial performance and corporate image and insufficiently attentive to public safety.
  - PG&E had erroneous pipeline records because of the lack of: robust data and document management systems, and processes to capture emerging information about the system.
  - PG&E's record-keeping problems hindered PG&E's ability to identify threats and to assess the risks posed by those threats.

- Decision 11-06-017
  - MAOP validation project was set in motion by NTSB's "justifiable alarm" at PG&E's inaccurate pipeline records (p. 17)
  - Curing PG&E's unreliable pipeline records was the "obvious goal" of the NTSB's recommendation to obtain traceable, verifiable and complete records and with reliably accurate data, create a dependable MAOP (p. 17)

**Ratepayers Should Not Pay for PG&E's Failure to Maintain the Required Records to Document Safe Operating Pressure**

- The PD correctly finds that for any pipe segments installed from 1955 to the present, applicable industry standards (1955-1960) and regulations (GO 112, 1961-1970 and 49 C.F.R. Part 192, 1970 to present) required PG&E to retain records of a post-installation pressure test for the life of the segment.
- The PD correctly disallows recovery of the expenses of re-testing post-1955 pipe segments for which PG&E failed to retain the required pressure test records
- However, the PD erroneously allows PG&E nearly full recovery of the (extremely expensive -- 9 times the cost of pressure testing) costs to replace post-1955 pipe segments, even though:
    - The only reason these pipe segments are being replaced now is because PG&E "imprudently" (putting it mildly) failed to retain the required pressure test records
    - Similar pipe segments for which PG&E retained the required records may not need to be replaced for decades
    - Post-1955 pipe is relatively new and modern pipe in PG&E's system – roughly half of PG&E's pipe was installed prior to 1955
    - PU Code Sections 451 and 463 and CPUC precedent are clear that ratepayers should not be responsible for paying costs that result from a utility's imprudence
- The PD should be revised to disallow the full $240 million of cost to replace post-1955 pipeline (instead of the minimal $16 million disallowance in the PD), which would still allow PG&E full recovery for the cost to replace pre-1955 pipeline

**The PD Would Erroneously Increase Rates to Pay for Work that PG&E Will Not Do in Phase 1**

- It is undisputed that the scope of pipeline testing and replacement work will be reduced (i.e., fewer segments will need to be tested or replaced) when the PSEP database is updated with current data.
    - The PD is based on out-of-date January 2011 data. PG&E admits that, since then, it has located significant numbers of pressure test records, obviating the need to test or replace those segments.
    - Using updated data would reduce the mileage of segments to be tested or replaced by 15% or more, resulting in a reduction in replacement costs of approximately $132 million.
- The PD correctly finds that non-contiguous Class 2 (low population density) segments should not be addressed in Phase 1, but does not remove those segments from the scope of the Phase 1 PSEP on which rate recovery is based
    - TURN estimates that making this correction would remove 36 replacement miles and 141 testing miles from the scope of Phase 1, thereby reducing Phase 1 costs by $233 million.
- These corrections are not disallowances. They are necessary reductions to cost recovery for work that will not be performed.

**The PD Would Erroneously Allow Rate Recovery for Pipeline Replacement Projects that PG&E Admits Are Unnecessary**

- Don't let PG&E make lemonade from lemons at ratepayer expense: The CPUC needs to prevent PG&E from acting on its incentive to inflate its rate base and boost its profits by including unnecessary pipeline replacement projects in the PSEP
- The PD erroneously finds that all segments identified for replacement via Box M2 have "suspect" welds, even though PG&E admits that their plan identified more replacement miles from Decision Tree Box M2 than are necessary:
    - PG&E's own expert in PG&E's own testimony: not all pre-1970, non-DSAW, non-seamless pipe is "problem pipe" (See Attachment.)
    - PG&E's witness Hogenson admitted that whether to test or replace will require a case-by-case analysis and that not all of the pipe identified in Box M2 will need to be replaced
- The PD should be modified to require PG&E to demonstrate in writing the need to replace a pipe segment before proceeding with replacement projects

**The 5-Year ROE Reduction Is Entirely Justified and, In Fact, Too Mild**

- There is a long line of CPUC decisions that reduce a utility's ROE in response to inattentive or inefficient utility management. E.g.:
    - PG&E, D.91107, 2 CPUC 2d 596, 728 (1979): "Poor performance" in promoting development of cogeneration
    - Southern California Edison, D.82-12-055, 10 CPUC 2d 155, 258 (1982): SCE's "continuing pattern of disregard for the Commission's avoided cost policy"
    - California Water Service Co., D.04-07-033: Company's "failure to coordinate its acquisition activities with its . . . regulatory obligations"
    - Southern California Water Co., D.06-11-020: "Management's inattention to efficiency improvements and cost cutting"; "poor planning and budgeting" for a key project; "mishandling" of an important contract
- The PD's ROE reduction is not a penalty for violations but rather a response to the NTSB and IRP findings that PG&E's management was ineffective and insufficiently focused on safety, as well as the additional evidence in the record that PG&E deferred necessary improvements to its system
    - PG&E management's dangerous disregard for pipeline safety justifies an ROE reduction for much longer than 5 years.
- The ROE reduction would apply only to a small and targeted subset of PG&E's overall rate base and thus would have only a minimal impact on PG&E's overall return
- The ROE reduction somewhat reduces PG&E's incentive to inflate its rate base by undertaking unnecessary pipeline replacement projects
- If the Commission is (unnecessarily in TURN's view) concerned about a multi-year impact, at a minimum, the decision should order an equivalent ($130 million) one-time capital disallowance

**The PD Properly Denies Contingency Costs**

- The PD reasonably concludes that PG&E's high-end cost estimates for pressure testing and replacement should be sufficient to cover PG&E's reasonable costs.
- The PD reasonably concludes that PG&E should be required to exert firm control over its PSEP costs
- The Commission should reject PG&E's request for "back-door" recovery of contingency costs by allowing cost recovery for projects that will not be performed in Phase 1 (see previous heading)

**The PD Properly Denies Recovery of Costs Barred by the Rule Against Retroactive Ratemaking**

- The Commission has considerable discretion in deciding whether or when to approve a memorandum account.
- As the PD points out, memorandum accounts are a two-way street. Utilities benefit when the Commission rejects memorandum accounts that would allow refunds of rates that TURN and DRA allege are excessive. See, e.g., D.98-07-100 (denying TURN's request for memo account to track alleged excess rates collected by SoCalGas)
- Given the complexity of the issues raised by PG&E's PSEP, the Commission has taken a reasonable amount of time to prepare a decision. PG&E's choice to incur PSEP costs prior to a decision reflects its recognition, in the wake of the San Bruno disaster, of the urgent need to make its gas transmission system safer.

Final Report No. 11-081

**Final Report**

on

# REVIEW OF PG&E'S IMPLEMENTATION PLAN DECISION PROCESS IN RESPONSE TO CPUC DECISION 11-06-017

to

**PACIFIC GAS & ELECTRIC COMPANY**

**August 19, 2011**

by

**MJ Rosenfeld, PE**

**Kiefner and Associates, Inc.**
**585 Scherers Court**
**Worthington, Ohio 43085**

0215-1101

required to undergo a hydrostatic pressure test before entering service. Pipelines installed in California after July 1, 1961 were required to undergo pressure testing under California General Order 112. Pipelines installed prior to those dates in their respective jurisdictions were not required to be pressure tested, although often they were pressure tested in accordance with company or industry consensus standards.

Also with respect to 1970, almost all manufacturing of certain "problem" pipe including those with flash-welded seams and low-frequency ERW seams (excepting the dc-ERW pipe made by Youngstown Sheet & Tube Company) had ceased by then, if not earlier. If the pipe is known to be seamless or have DSAW seams, it is not considered to be inherently susceptible to gross manufacturing defects affecting the pipe seam and the process is exited per Step 1D for evaluation in the Fabrication and Construction Threats decision process.

Certain varieties of "problem" pipe seams are defined in Steps 1E through 1G, consisting of anything that is not seamless or DSAW seam pipe. It is noted that PG&E conservatively categorizes "spiral" (helical) seam pipe (the older vintages manufactured in accordance with now-discontinued ASTM A211, not currently manufactured helical seam pipe) and flash welded pipe manufactured by the A.O. Smith Company as "problem pipe." It is my opinion that this is unnecessary for two reasons: (1) in the case of the spiral welded pipe, the angle of the seam makes it much less susceptible to the effects of hoop stress even if gross defects are present; and (2) A.O. Smith cold expanded its flash welded pipe in the manufacturing process so any seam that survived could not be severely defective. However, PG&E's choice is a conservative one. In any case, if any of the types of pipe named in Steps 1E through 1G are present, and the pipe has experienced a hydrostatic pressure test meeting the requirements of Part 192, Subpart J, then it is evaluated for the potential for flaw growth by pressure-cycle fatigue. In most cases, a test meeting the requirements of Subpart J will assure that pressure cycle fatigue is not a problem in normal natural gas service.[6,7] Nevertheless, Step M1 performs that check for Phase 1 pipe.

If a Subpart J test is not confirmed then the treatment of this threat is determined based on whether it operates at a hoop stress of greater than or less than 30% of SMYS (Step 1J). The 30% SMYS hoop stress represents an approximate threshold below which a rupture is extremely unlikely in a ductile material (based on a review of burst test data[8] and operator experience, though it is not impossible in an extremely low-toughness material). If the pipe operates at greater than 30% SMYS and is in an HCA or is in Classes 2 through 4 (Step 1K), the pressure is

[6] Kiefner, J.F., and Rosenfeld, M.J., "Effects of Pressure Cycles on Natural Gas Pipelines", Gas Research Institute Report No. GRI 04/0178, Sept. 17, 2004.
[7] Kiefner, J. F., "Evaluating the Stability of Manufacturing and Construction Defects in Natural Gas Pipelines", Report to US DOT, Office of Pipeline Safety, Contract No. DTFAAC05P02120, April 6, 2007.
[8] Kiefner, J.F., Vieth, P.H., and Roytman, I., "Continued Validation of RSTRENG", PRCI Catalog L51749, Dec. 20, 1996.