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)

RESPONSE OF PACIFIC GAS AND ELECTRIC COMPANY TO APPLICATIONS FOR REHEARING

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I. INTRODUCTION

The Applications for Rehearing of Commission Decision ("D.") 12-12-030, concerning PG&E's Pipeline Safety Enhancement Plan ("PSEP"), should be denied. Pacific Gas and Electric Company ("PG&E") responds to the rehearing applications of the Division of Ratepayer Advocates ("DRA"), The Utility Reform Network ("TURN"), the City of San Bruno, and the City and County of San Francisco ("CCSF") concerning the Commission's: (1) decision not to adjust PG&E's Return on Equity for PSEP investments; (2) construction of Public Utilities Code Sections 451 and 463; and (3) evaluation of the PSEP under the "preponderance of the evidence" standard. In addition, PG&E responds to several factual issues raised in the parties' applications that do not give rise to the type of "error" that would merit rehearing.[1]

II. THE APPLICATIONS FOR REHEARING DO NOT DEMONSTRATE LEGAL ERROR IN DECISION 12-12-030

A. The Commission's Decision Not To Adjust PG&E's Return on Equity Does Not Constitute Legal Error

The City of San Bruno argues that: (1) the revisions to the Proposed Decision ("PD")

[1] The CAlifornians for Renewable Energy ("CARE") also filed an Application for Rehearing that simply repeats unsupported allegations previously made by CARE, including in a recent complaint filed with the Federal Energy Regulatory Commission (Docket No. RP13-436-000), which PG&E moved to dismiss. CARE's Application for Rehearing fails to state a legally cognizable argument on rehearing, and should be ignored.

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concerning PG&E's Return on Equity ("ROE") for PSEP capital investments constituted an "alternate" decision for which insufficient notice was given; and (2) the decision to allow PG&E to earn its authorized ROE on PSEP investments is not supported by record evidence.[2] This argument conflicts with the statutory and regulatory scheme governing Commission decisions.

1. The Revisions Made To The Decision Did Not Transform It Into An Alternate Decision

The City of San Bruno claims that the changes made to the PD by the assigned Administrative Law Judge ("ALJ") prior to the Commission meeting transformed the decision into an "alternate." However, Rule 14.1(d) provides: "'Alternate' means a substantive revision by a Commissioner to a recommended decision *not proposed by that Commissioner. . .*"[3] Here, the assigned ALJ revised the PD in response to comments. Therefore, the revised draft decision was not an alternate.[4] In a similar case, applicants for rehearing argued that a revised draft decision should have been considered an alternate because it changed the draft decision's recommendation on a major issue, and that therefore the Commission should have served the revised draft decision and provided an opportunity to comment.[5] The Commission held that these arguments were "without merit":

> In this instance, a Commissioner did not revise the proposed decision. Rather, the ALJ revised the proposed decision in response to comments. . . Thus, the revised Draft Decision was not an alternate and a further round of comments was not required.[6]

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[2] CCSF makes similar arguments. CCSF Application ("App.") For Rehearing, pp. 16-22.

[3] CCSF collaterally attacks Rule 14.1(d), claiming that it is not faithful to the statutory language of Public Utilities Code Section 311. CCSF App. for Rehearing, p. 18. That is an argument more appropriately addressed in a proceeding to amend the Rules of Practice and Procedure.

[4] *Re Implementation of the Suspension of Direct Access*, Order Denying Rehearing of Decision 06-07-030, 2007 WL 142864, at *6 (Jan. 11, 2007).

[5] *Id.*

[6] *Id.* at *6; *see also id.*, footnote 7 ("Applicants are in effect arguing that an ALJ cannot be persuaded to change the proposed decision in response to comments. If that is true, then there would be no reason for public review and comment"); *see also Monasky v. Citizens Communications*, D.99-08-029 (1999) ("because these changes were made by the assigned

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City of San Bruno relies primarily on Public Utilities Code Section 311(e). Section 311(e) concerns only decisions that are properly deemed "alternate" decisions. Here, the changes by the assigned ALJ to the PD do not constitute an "alternate" under Rule 14.1(d). In fact, Public Utilities Code Section 311(d), which applies to the PD issued by the assigned ALJ in this case, makes clear that: "The commission may, in issuing its decision, adopt, modify, or set aside the proposed decision or any part of the decision."

CCSF's reliance on *The Utility Reform Network v. Public Utilities Commission*[7] is similarly misplaced. In that case, the Commission initially denied PG&E's application for approval of an agreement to construct a new electric generating facility. PG&E subsequently filed a petition for modification, requesting approval of the same project, with a later in-service date. The Commission denied PG&E's petition but, on its own motion, deemed the petition an application for approval and granted it.[8] The Court of Appeals found that the legal error stemmed not from either the Proposed Decision or the Alternate Decision, but from a "Revised Alternate," which denied the petition for modification, but deemed it an application and granted it.[9] Neither the comments nor the proposed decisions contemplated treating the petition as an application without the procedures that apply in such proceedings.[10] It was the Commission's *sua sponte* expansion of the scope of the proceeding that was found to constitute error.

Even if the revisions to the PD did fall under the definition of "Alternate" in Rule 14.1(d), the ALJ's revision concerning ROE was suggested in prior comments. The issue of whether the Commission should adjust PG&E's ROE for PSEP investments, and if so what the adjustment should be, was discussed extensively in: (1) testimony from various parties, including

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administrative law judge, they do not make the Commission's final Decision an 'alternate' to the Proposed Decision.")

[7] 2012 WL 1059368 (Cal. App. 1 Dist.) (March 16, 2012) (Not Officially Published).

[8] *Id.* at *1.

[9] *Id.* at *11.

[10] *Id.* at *12.

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expert rebuttal testimony of PG&E;[11] (2) post-hearing briefing;[12] and (3) comments on the PD.[13] Therefore, "the issue has been fully briefed and the Commissioners were fully aware of all arguments," and the Commission was not obligated to give parties an opportunity to comment on the December 19, 2012 revised draft decision.[14]

The City of San Bruno also claims that the agenda was legally insufficient because it did not contain notice of the revision concerning ROE.[15] Under Rule 15.2, the Commission must issue an agenda listing the items to be transacted at the Commission meeting. In this case, the agenda for the December 20, 2012 Commission meeting was timely issued, and included the ALJ's proposed decision in this case. The revision to the PD removing the ROE reduction was not made until December 19, 2012, so it could not have been included on the agenda. This does not run afoul of Commission rules; there is no prohibition on changes to a draft decision after the agenda is issued. In fact, the Commission can "adopt, modify, or set aside the proposed decision or any part of the decision."[16] Furthermore, the Commission is under no obligation to serve a revised draft decision, but can post on its website and place on the "Escutia Table" revisions to a draft decision any time prior to the Commission meeting.[17]

2. The Commission's Decision Concerning The ROE For PSEP Investments Was Supported By Substantial Record Evidence

The City of San Bruno claims that the Commission's decision not to reduce PG&E's ROE for PSEP investments lacks substantial evidence in the record. Not so. ROE was a pivotal

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[11] Exhibit ("Ex.") 21, PG&E Rebuttal, Chapter 2, *Principles To Align Safety and Regulatory Ratemaking Policy.*

[12] *See*, *e.g.*, PG&E Opening Brief, pp. 82-85; PG&E Reply Brief, pp. 32-37.

[13] *See, e.g.*, PG&E Opening Comments, pp. 14-16. Other parties, including Southern California Edison ("SCE"), also addressed the ROE issue.

[14] 2007 WL 142864, at *7.

[15] City of San Bruno App. for Rehearing, pp. 10-11.

[16] Public Utilities Code Section 311(d).

[17] 2007 WL 142864, at *7.

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issue in the PSEP proceedings. Several parties proposed to reduce the return for capital expenditures made under PSEP. PG&E's rebuttal witness on ROE, Susan Tierney, analyzed the parties' proposals under five ratemaking principles and concluded that the proposed ROE adjustments would undermine the Commission's goal of improving the safety of the natural gas transmission pipeline system, and adversely affect the utility's incentives to undertake PSEP investment.[18] Ms. Tierney also testified regarding the importance of providing an appropriate rate of return so that PG&E can raise the financing necessary to implement the aggressive schedule and extensive scope of the PSEP at reasonable cost.[19] SCE also testified that reducing PG&E's rate of return would make it more difficult for PG&E to access capital markets to finance the needed pipeline enhancements, because "[n]o rational investor will invest capital in a company where he or she is required to earn a reduced return compared to other similar investments where a full-risk adjusted return is available to be earned."[20] The Commission relied on this record evidence and found compelling "PG&E's argument that drastically reducing return on equity harms the ratepayers in the long run by increasing borrowing costs and potentially diminishing the financial health of the utility."[21] The City of San Bruno's claim that the Commission's decision was not based on substantial record evidence is without merit.[22]

B. The Commission Correctly Determined That Public Utilities Code Sections 451 And 463 Do Not Mandate Wholesale Cost Disallowance

DRA alleges that the Commission committed legal error by not construing sections 451 and 463 of the Public Utilities Code to require disallowance of *all* PSEP costs due to PG&E's

[18] *See* PG&E's Opening Brief, pp. 82-85.

[19] *Id.*, p. 83.

[20] Ex. 130, Rebuttal Testimony of Paul Hunt, p. 5.

[21] D.12-12-030, p. 105.

[22] The City of San Bruno requests oral argument. PG&E opposes this request, on the grounds that the City of San Bruno has not met the heightened standards for oral argument set forth in Rule 16.3(a).

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alleged prior "errors" and "omissions."[23] TURN takes a more circumscribed tack, and argues that the Commission's decision to disallow rate recovery of equivalent hydrotesting costs for the replacement of pipelines installed after 1955 violates Sections 451 and 463.[24]

The Commission rightly rejected DRA's argument that Sections 451 and 463 compel disallowance of all PSEP costs. Section 451 required the Commission to evaluate whether PG&E's cost estimates for PSEP and the resulting rates were just and reasonable. PG&E provided hundreds of pages of testimony and workpapers detailing its cost forecast and describing its ratemaking proposal. The Commission fully discharged its legal obligations under Section 451 by reviewing all evidence and determining a just and reasonable rate.

DRA and TURN misconstrue the applicable requirements under Public Utilities Code Section 463(a). This statute requires that for large capital projects totaling $50 million or more the CPUC shall disallow any costs resulting from "unreasonable error or omission relating to the planning, construction or operation" of the plant. DRA's assertion that Section 463 allows the Commission to conduct a historical review of alleged "errors" and "omissions" over a multi-decade period to deny cost recovery for forecasted projects is not supported by the plain language of the statute. "Error" and "omission" are defined as specifically related to construction and development of the plant in question. "Error" is defined as "any action or direction which causes an avoidable (i) increase in the time required to bring the plant to full commercial operation, (ii) change in the number or types of personnel or firms required to bring the plant to full commercial operation, (iii) increase in the number of worker hours required to complete any portion of the plant construction project, or (iv) change of equipment, configuration, design, schedule, or program." The definition of "omission" also concerns solely the particular plant in question. The prudence review required is thus limited to the "development, construction and operation" of the capital assets themselves if there has been a

[23] DRA App. for Rehearing, pp. 4-10.

[24] TURN App. for Rehearing, pp. 11-15.

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significant cost overrun or significant delay due to errors or omissions in project management. Section 463.5(a) clarifies that Section 463 "does not require the commission to undertake a reasonableness review of recorded costs to determine the reasonableness" of plant that may exceed $50 million if the CPUC has adopted "an estimate of the reasonable costs in any proceeding."[25]

Therefore, it was not legal error for the Commission to conclude that, "[t]he public utility code standards for rate recovery, i.e., just and reasonable, and the disallowance concept reflected in § 463 do not combine to provide an analytical basis for disallowing reasonable costs on the basis that the utility should have made the expenditures at an earlier date."[26] The Commission found "no case law or statute supporting the assertion" that PG&E's alleged past errors and omissions "render the currently proposed expenditures unreasonable."[27]

Nor do Sections 451 and 463 compel disallowance of all capital costs to replace transmission pipeline installed after 1955 for the life of those assets, as TURN contends. The Commission concluded, based on its finding that "from 1956 on, PG&E's practice was to comply with then-applicable industry standards for pre-service pressure testing, and that retaining records of such testing was part of the industry standard,"[28] that shareholders will be allocated the costs of retesting pipeline installed between 1956 and 1961.[29] However, the record evidence also demonstrated that, "[c]ertain pipeline segments, for reasons unrelated to PG&E's

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[25] The Commission correctly distinguished D.94-03-048, 53 CPUC 2d 451, in which the Commission disallowed rate recovery for costs stemming from an accident at the Mohave power Plant, on the grounds that the utility request in that case was for rate recovery of expenses stemming from the accident at the plant in question. D.12-12-030, p. 54, footnote 43. The Commission did not undertake a review in that case of any errors or omissions *generally* to determine whether cost recovery for expenses relating to the accident should be permitted.

[26] D.12-12-030, p. 54.

[27] *Id.*

[28] *Id.*, p. 59.

[29] *Id.*, p. 61.

poor document management, require replacement, rather than just re-testing,"[30] and that "ratepayers should not receive a new pipeline at no cost."[31] This finding was supported by the record evidence, and does not constitute legal error.

C. The Commission Evaluated The PSEP Using The Correct Burden of Proof

DRA argues that the Commission should have evaluated PG&E's proposal under the "clear and convincing evidence" standard, rather that the "preponderance of the evidence" standard.[32] The more recent authorities cited by DRA confirm that the Commission evaluates rate cases under the "preponderance of the evidence" standard. For example, the Commission evaluated SCE's 2009 GRC, and PG&E's 2011 GRC, under the preponderance of the evidence standard.[33] As the Commission noted, "[t]he preponderance of the evidence is generally the default standard in civil and administrative law cases."[34] The Commission's evaluation of the PSEP under the preponderance of the evidence standard therefore does not constitute error.

D. Disputed Factual Issues Do Not Merit Rehearing

DRA, TURN and CCSF take issue with the Commission's approval of the scope of Phase 1 of the PSEP, the prioritization of pipeline segments for testing and replacement, and certain technical aspects of PG&E's "decision trees" that are used to determine what actions will be taken (*e.g.*, pressure testing or pipe replacement) based on certain pipeline threat categories.[35]

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[30] *Id.*, p. 60.

[31] *Id.*, p. 61.

[32] DRA App. for Rehearing, p. 11.

[33] D.09-03-025, p. 8 ("the Commission has held that the standard of proof the applicant must meet is that of a preponderance of evidence, which the Commission has, at times, incorrectly referred to as 'clear and convincing' evidence"); *accord*, D.11-05-018, pp. 68-69.

[34] *In the Matter of the Application of San Diego Gas & Electric Company for a Certificate of Public Convenience and Necessity for the Sunrise Powerlink Transmission Project*, D.08-12-058, p. 19. DRA claims that the Commission adopted a preponderance of the evidence standard in *Sunrise* because it was *not* a rate case. This is misleading. There, the Commission noted that it had applied the clear and convincing evidence standard previously in rate cases, but it did not decide to use the default preponderance of the evidence standard because it was "not a rate case."

[35] D.12-12-030, p. 15. The decision trees are appended to D.12-12-030 as Attachment C.

For example, DRA and TURN claim that Box M2 of the decision tree should have been modified such that all pipelines falling into that box on the Decision Tree would not have to be replaced.[36] This claim was the subject of testimony,[37] briefing,[38] and comments on the PD,[39] and the Commission decision to adopt this aspect of PG&E's Decision Tree was based on substantial evidence.[40] Similarly, DRA's recommendation that Decision Point 2F (which queries whether a Subpart J strength test has been done) be omitted from the Fabrication and Construction Threats Decision Tree was rejected based on substantial record evidence.[41]

The same is true for CCSF's criticism of the Commission's approval of PG&E's prioritization of segments for testing and replacement. CCSF attacks approval of PG&E's prioritization of Class 2, 3 and 4 and Class 1 HCA operating at or greater than 30% Specified Minimum Yield Strength ("SMYS") over Class 2, 3 and 4 and Class 1 HCA operating between 20% and 30% SMYS.[42] The Commission's decision, however, was based on substantial evidence submitted by PG&E explaining that pipeline failures are more likely to result in a rupture than a leak when they occur on pipelines operating above 30% SMYS, while pipelines operating below 30% SMYS will typically fail as a leak before rupture.[43] The Commission's decision on PG&E's proposed scope for Phase 1 of PSEP should stand.

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[36] DRA App. for Rehearing, pp. 15-20; TURN App. for Rehearing, pp. 16-19.

[37] Ex. 145, DRA Direct (Rondinone), p. 11; Ex. 21, PG&E Rebuttal, p. 3-3, line 21—p. 3-4, line 11; Transcript ("Tr.") (Hogenson), p. 1512, line 11—p.1513, line 6.

[38] PG&E Opening Brief, pp. 7-8; PG&E Reply Brief, p. 57.

[39] TURN Comments, p. 6; PG&E Reply Comments, p. 3.

[40] D.12-12-030, Finding of Fact 25.

[41] Ex. 21, PG&E Rebuttal, p. 3-7, lines 12-27; PG&E Opening Brief, p. 10; PG&E Reply Comments, p. 3.

[42] CCSF App. for Rehearing, pp. 12-14.

[43] Ex. 21, PG&E Rebuttal, p. 3-16, line 32—p. 3-17, line 2.

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III. CONCLUSION

For the foregoing reasons, the Applications for Rehearing of Commission Decision 12-12-030 should be denied.

Respectfully Submitted,

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