BEFORE THE PUBLIC UTILITIES COMMISSION
OF THE STATE OF CALIFORNIA

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Order Instituting Investigation on the Commission's Own Motion into the Operations and Practices of Pacific Gas and Electric Company to Determine Violations of Public Utilities Code Section 451, General Order 112, and Other Applicable Standards, Laws, Rules and Regulations in Connection with the San Bruno Explosion and Fire on September 9, 2010.	I.12-01-007 (Filed January 12, 2012) (Not Consolidated)
Order Instituting Investigation on the Commission's Own Motion into the Operations and Practices of Pacific Gas and Electric Company with Respect to Facilities Records for its Natural Gas Transmission System Pipelines.	I.11-02-016 (Filed February 24, 2011) (Not Consolidated)
Order Instituting Investigation on the Commission's Own Motion into the Operations and Practices of Pacific Gas and Electric Company's Natural Gas Transmission Pipeline System in Locations with Higher Population Density.	I.11-11-009 (Filed November 10, 2011) (Not Consolidated)

REPLY BRIEF
OF THE CONSUMER PROTECTION AND SAFETY DIVISION
ON FINES AND REMEDIES

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As the Director of the Commission's Safety and Enforcement Division, which for purposes of this case is identified by its former name, the Consumer Protection and Safety Division ("CPSD"), I hereby submit this Reply Brief on Fines and Remedies. In this brief, I reply primarily in opposition to the opening brief on fines and remedies submitted by the Respondent, Pacific Gas and Electric Company ("PG&E"). I also provide a comparison of the penalty proposals submitted by the four intervenor parties, namely, the City of San Bruno ("San Bruno)", the Commission's Division of Ratepayer Advocates ("DRA"), the City and County of San Francisco ("San Francisco"), and The Utility Reform Network ("TURN").

I. REPLY TO PG&E

A. I Strongly Dispute PG&E's Contention that CPSD's Penalty Proposal is "Excessive" or Otherwise Unlawful

In a brief filed on May 24, 2013, PG&E challenged as "excessive" my recommendation that the Company be required to fund out of shareholder monies a total of $2.25 billion in remedial actions to make its gas system safe. In its brief, PG&E also described at length various measures the Company, under its new management, has taken since the tragic explosion of Line 132 on September 9, 2010.

While it is true that PG&E, under firm direction by this Commission, has made a strong and commendable effort since San Bruno to make its system safer, two points must be emphasized in response. First, none of this can excuse the decades of violations of fundamental safety rules and principles that led up to the tragedy at San Bruno, for which PG&E has yet to acknowledge. Second, despite the changes PG&E has made under its new management, these are only the beginning of what needs to be done in order to make the PG&E gas system safe. Based on my own evaluation, I estimate that PG&E will need to spend as much as $3 billion to $4 billion, in total, to bring this massive gas system into a state where we can say it is safe.

My proposal is that PG&E be required by this Commission to absorb, as a shareholder expense – *not to be recovered through the rates paid by its gas or electric customers* – a total of $2.25 billion in safety investments on its gas system.

If adopted by the Commission, this would be by far the largest penalty ever imposed on a public utility in the history of the United States. This is indeed a very large penalty, but contrary to PG&E's arguments it is certainly *not* excessive in light the record of PG&E's wrongdoing in this case, compounded by PG&E's lack of genuine remorse.

But, large as it is, this penalty of $2.25 billion in shareholder-funded investment in the gas system will not be enough to make the entire system safe. As I already have stated above, the total price tag for this effort is in the range of $3 billion to $4 billion.

Where will this extra money come from? That will be for the Commission to decide in future rate cases, as the dollars are expended.

My proposed penalty of $2.25 billion is informed in substantial part by the Overland Report (Joint-51), which demonstrates that PG&E could absorb a penalty of this magnitude without jeopardizing the safety of its operations and its financial viability. (*See* CPSD Opening Brief, pp. 52-54.)

I view this as the maximum financial penalty this Commission reasonably can impose on PG&E. I also feel quite strongly that the penalty should be in the form of shareholder-funded safety investments in the PG&E gas system. The alternative of imposing a traditional "fine" on PG&E, payable to the State General Fund, would not do anything to advance safety on the system. I believe the Commission owes it to the victims of the San Bruno tragedy to do something very significant, not only to sanction PG&E for past misconduct and neglect, but also to advance public safety. These are the reasons why I propose a $2.25 billion penalty, in the form of shareholder-funded investments in safety improvements on PG&E's gas system.

Again, I emphasize, $2.25 billion will not get the job done. It represents only about half of the investment needed in order to make the PG&E gas system truly safe. But I do not believe the Commission should attempt to impose a higher penalty amount, in light of the Overland Report and its suggestion that a penalty higher than $2.25 billion would actually *jeopardize*, rather than *improve*, public safety.

The Commission should not be persuaded by PG&E's rhetorical arguments that this penalty, if adopted, would be "excessive" under governing law, or constitute a violation of the federal or state constitutions. These are not legitimate arguments against the penalty I have recommended in this case.

B. PG&E Continues to Manifest a Conspicuous and Disturbing Lack of Remorse for Its Many Failures Leading Up To The Tragedy At San Bruno

PG&E's brief on penalties displays a chilling lack of remorse for the many failures that led up to the tragedy in San Bruno. I believe the lack of remorse by PG&E in its brief only

serves to reinforce the need for the Commission to impose the very substantial $2.25 billion penalty I have proposed.

PG&E's lack of remorse is particularly evident in the section of its brief entitled "Severity of the Offense." Although PG&E commences that section of the brief with a statement of "regret" for the incident in San Bruno, the gist of PG&E's argument is "don't blame us." PG&E attempts to refute the record evidence in this case showing its culpability in installing patently defective pipe in the Crestmoor neighborhood in 1956, in the midst of what was then being developed as a residential neighborhood. This early lapse then was compounded by PG&E's failure over the ensuing years to inspect the pipe or even to keep adequate records.

PG&E's statements of "regret" ring hollow in the face of this continuing lack of any sincere remorse whatsoever for the Company's past shortcomings. If there was ever any doubt about the need for a very large penalty in this case, any such doubt is removed by the unrepentant tone of PG&E's brief. It is time to throw the book at PG&E.

II. PENALTY PROPOSALS

A. CPSD's Penalty Proposal

As stated in CPSD's opening brief on fines and remedies, we urge the Commission to use its equitable powers to order PG&E to take the steps needed to ensure its system is safe without unduly burdening the ratepayers. CPSD continues to recommend PG&E be penalized $2.25 billion for all three San Bruno-related OIIs at shareholder expense. The Commission should order PG&E to spend the entirety of this penalty on safety improvements for its gas transmission and distribution systems to prevent such disastrous events from recurring.

CPSD supports a flexible apportionment of the penalty, so long as funds are used exclusively to improve the safety of PG&E's gas transmission or distribution systems. As indicated in CPSD's opening brief, these funds may be used on Phase I and Phase II of the Pipeline Safety Enhancement Plan ("PSEP"). For the purposes of clarity, the funds also may be used to carry out the shareholder-funded safety improvements required by this Commission's decision concerning PG&E's Gas Accord V Settlement (Decision 11-04-031). The penalty funds may be used to develop safety management systems. It is also CPSD's intent that this money be available to remediate any gas pipeline right-of-way encroachments (without prejudice to CPSD's right to pursue future enforcement actions against PG&E for any such encroachments). These examples of expenditures are illustrative but not exhaustive. Any bona

fide safety enhancement to PG&E's gas transmission or distribution system made at shareholder expense may be eligible to satisfy the $2.25 billion penalty.

Oversight is required to ensure that PG&E spends the penalty funds appropriately. The Commission should order all expenses be subject to third-party auditing. To ensure the integrity of the audits, CPSD will select the auditors and oversee the auditing process. Any costs incurred by CPSD for the auditing should be reimbursed by PG&E as a shareholder expense, as part of the $2.25 billion penalty.

In the interest of predictability throughout the auditing process, the Commission should admonish PG&E as to certain ineligible expenditures. Any payments made to compensate victims or the City of San Bruno cannot be used to satisfy the penalty. Any administrative costs associated with the San Bruno incident, including those associated with implementing the Commission's decisions, likewise should be excluded. Any expenses related to customer notification will not be considered eligible, nor will PG&E's legal fees. Likewise, other expenses previously approved for rate recovery are not eligible to satisfy the penalty. While this list is not exhaustive, it provides PG&E sufficient guidance to determine what expenditures will be deemed eligible.

B. Comparison of CPSD's Penalty Proposal with the Penalty Proposals Submitted by the Intervenor Parties

Table 1, below, summarizes the penalty proposals submitted by CPSD and the intervenors in these proceedings. Each proposal also contains remedies not included in the table. These remedies are specific recommendations for improving PG&E's natural gas system in addition to the penalties.

Most of the proposals plead for a set of penalties totaling approximately $2.25 billion. However, both the City of San Bruno's proposal and DRA's proposal may exceed that amount. The City of San Bruno has specified a fine of $1.25 billion, payable to the State General Fund, and requested the PSEP costs be incurred by shareholders without assessing a total dollar amount for the PSEP costs. Under the City of San Bruno's proposal, the unknown PSEP cost could elevate the total penalty above the estimated $2.25 billion that CPSD believes PG&E is capable of absorbing without jeopardizing safe operations. The DRA has specified a fine of $550 million, payable to the State General Fund, and estimates the cost of PSEP Phase I to be

$1.989 billion ($800 million of which has already been disallowed in Decision 12-12-030) for a total of $2.539 billion. CPSD is concerned with the safety implications of hampering PG&E's financial integrity, and therefore we stand by our proposal that the maximum penalty in this case be set at $2.25 billion.

While the proposals of the other intervenor parties seek a penalty of approximately the same magnitude CPSD has recommended, the structure of CPSD's proposal ensures each dollar is spent improving the safety of PG&E's gas system. It is for this reason that I urge the Commission to adopt CPSD's proposed penalty.

Table 1: Penalty Proposal by Party	
Party	**Penalty Proposal**
CPSD	• $2.25 billion shareholder expense for safety improvements • No civil penalties
City of San Bruno	• PSEP I & II at shareholder expense • $1.25 billion civil penalty

City and County of San Francisco	• $2.25 billion total shareholder expense
	  o Large portion for safety improvements
	  o Remainder as a civil penalty

DRA	• Approx. $2.539 billion total
	  o PSEP I at shareholder expense ($1.989 billion total)
	  o $550 million civil penalty

TURN	• Approx. $2.25 billion total
	  o PSEP I at shareholder expense
	  o Remainder as a civil penalty (at least $670 million)

III. RESPONSE TO PG&E'S CLARIFICATION OF PROPOSED REMEDIES

A. CPSD's Detailed Reply to PG&E Concerning Remedies Is Contained in Appendix A to this Reply Brief

The extensive shortcomings in PG&E's safety systems and compliance with the law call for extensive changes to their operations. CPSD included a list of proposed remedies in its Opening Fines and Remedies Brief. PG&E responded to these remedies in PG&E's Coordinated Reply Brief, Appendix B, and the Proposed Remedies table. To ensure a clearly organized response to PG&E, CPSD created the attached table in Appendix A, by adding one column to

PG&E's Appendix B. This column is entitled "CPSD Comments re PG&E Response and Edits." Entries in this column respond to PG&E's proposed edits to CPSD's original proposed remedy.

Where CPSD's response results in modification of CPSD's original proposed remedy, the modifications are indicated (underlined text is added, strikethrough text is removed) in Column 2, entitled "Revised Party Proposal".

Appendix B to this reply brief lists CPSD's finalized proposed text from Column 2 of Appendix A. These proposed remedies are the product of extensive analysis of the shortcomings in PG&E's operations and are considered necessary by CPSD to ensure the safety of the people of California. CPSD strongly recommends the Commission adopt the recommended remedies listed in Appendix B in their entirety.

B. The Commission Should Reject PG&E's Proposal to Apply the Government Auditing Standards

PG&E proposes modifying CPSD's auditing proposal so that it is consistent with the Government Auditing Standards issued by the United States Government Accountability Office ("GAGAS"). (*See* PG&E Coordinated Reply Brief, p. 102.) For the reasons discussed below, CPSD opposes this proposed modification to CPSD's remedies proposal.

The purpose of GAGAS is to audit the government, not PG&E. By its own wording, "[t]hese standards are for use by auditors of government entities and entities that receive government awards and audit organizations performing GAGAS audits." (*See* PG&E'S Request for Official Notice, Exhibit 12, p. 5.)

Furthermore, GAGAS guidance for auditing does not contemplate recordkeeping audits. In fact, the types of GAGAS audits include financial audits and attestation engagements, neither of which is pertinent to the auditing of PG&E's safety related records. (*See* PG&E'S Request for Official Notice, Exhibit 12, pp. 14-16.) The final type of GAGAS audit is for "Performance Audits," but GAGAS lists a number of types of professional standards that mesh with it, none of which include recordkeeping standards. (*See* PG&E'S Request for Official Notice, Exhibit 12, pp. 17, 23-24.)

Fundamentally, it is within this Commission's discretion to choose whatever audits it wishes to employ. We are aware of no Commission precedent endorsing the use of GAGAS for any audits. Using a recent and pertinent example, Commission Resolution L-436 does not require using GAGAS, even though it requires disclosure of safety related auditing records.

(*See* Resolution No.: L-436, p. 1.)

In short, it is up to the Commission, in its own discretion, to determine the appropriate scope of audits. Here, GAGAS is not appropriate, given PG&E's specific auditing needs that must be carefully considered.

C. CPSD Accepts PG&E's Clarification That It Will Take Up to Three Years for PG&E to Achieve Compliance with Generally Accepted Recordkeeping Principles, Level 3, as CPSD Has Recommended

PG&E agrees to undertake to achieve Level 3 information maturity scores under the Generally Accepted Recordkeeping Principles ("GARP"), but clarifies that it will take the Company up to three years to do so. CPSD agrees with PG&E's proposed clarification and recommends that the Commission require PG&E to meet this deadline. CPSD reserves the right to audit PG&E during the intervening time, in order to ensure PG&E is on schedule to achieve this commitment. CPSD provides additional response to PG&E on this point in Appendix A.

IV. CONCLUSION

For the reasons explained here and in CPSD's prior briefs in this case, I ask that the Commission penalize PG&E a total of $2.25 billion, to be paid in the form of shareholder-funded investments to enhance the safety of the PG&E gas system. None of this $2.25 billion should be paid by PG&E's gas or electric ratepayers. All legitimate, Commission-supervised safety investments should qualify toward the penalty amount. Finally, this entire program of safety

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investments should be subject to after-the-fact audit by an independent auditing firm at PG&E's shareholder expense, to ensure that PG&E invests this money appropriately and in accordance with the Commission's directives.

Respectfully submitted,

/s/ EMORY J. HAGAN, III

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