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BEFORE THE PUBLIC UTILITIES COMMISSION
OF THE STATE OF CALIFORNIA

Order Instituting Investigation on the Commission's Own Motion to Determine Whether Pacific Gas and Electric Company and PG&E Corporation's Organizational Culture and Governance Prioritize Safety.	Investigation 15-08-019

MOTION TO AMEND JUNE 18, 2019 ASSIGNED COMMISSIONER AND ADMINISTRATIVE LAW JUDGE'S RULING TO ALIGN IT WITH THE SCOPE OF THE PROCEEDING

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I. INTRODUCTION

The California Public Utilities Commission (Commission) initiated this proceeding in August of 2015 in the wake of the Pacific Gas and Electric Company and PG&E Corporation (jointly, PG&E) 2010 gas transmission pipeline explosion in San Bruno, California. The first phase of this proceeding served to evaluate PG&E's organizational culture, governance, policies, practices, and accountability metrics in relation to PG&E's record of operations, including its record of safety incidents. Phase one determined that since PG&E's 2010 San Bruno pipeline explosion, PG&E has repeatedly stated its intention to change its safety culture. The Commission noted that PG&E has made some fragmented progress in developing a safety culture but that PG&E's overall progress is uneven across its gas and electric lines of business, and that while there are many programs underway, they do not yet add up to a consistent, robust, and accountable corporate-wide safety program.[1]

On December 21, 2018, the Assigned Commissioner and Administrative Law Judge issued a ruling (Scoping Ruling) identifying the issues to be addressed in the next phase of this proceeding. After setting forth a lengthy but non-exhaustive list of structural, organizational, and

[1] May 8, 2017 Scoping Memo and Ruling of Assigned Commissioner at 1-2.

managerial safety issues, the Scoping Ruling specifically notes that in order to achieve its safety and performance objectives, "the proceeding will also consider all necessary measures, including, but not limited to, a reduction of PG&E's return on equity until any recommendations adopted by the Commission are implemented."[2]

On January 29, 2019, PG&E filed for Chapter 11 bankruptcy protection. On June 18, 2019, the Assigned Commissioner and Administrative Law Judge in this proceeding issued a ruling (June 18, 2019 Ruling) that "establishes a process for parties to comment on proposals that may improve the safety culture of Pacific Gas and Electric Company and PG&E Corporation (PG&E)."[3] The June 18, 2019 Ruling solicits comments on four proposals:

1) Separating PG&E into separate gas and electric utilities or selling the gas assets;
2) Establishing periodic review of PG&E's Certificate of Public Convenience and Necessity (CPCN);
3) Modifying or eliminating PG&E Corp.'s holding company structure; and
4) Linking PG&E's rate of return or return on equity to safety performance metrics.

The Public Advocates Office at the California Public Utilities Commission (Cal Advocates) applauds this step by the Assigned Commissioner and Administrative Law Judge. The ruling acknowledges that the Commission has the authority to both grant and rescind the CPCN pursuant to which a utility such as PG&E is issued a franchise to serve California customers. However, the June 18, 2019 Ruling does not go far enough. In order to achieve the best result for California's customers, all options must be on the table.

By this motion, Cal Advocates urges the Commission to take two key steps. First, the Commission should establish minimum safety and performance prerequisites for post-bankruptcy franchisees, whether or not PG&E. By establishing those prerequisites—in terms of types of companies, ownership structure, corporate governance, and performance culture, the

[2] December 21, 2018 Scoping Memo and Ruling of Assigned Commissioner at 9.

[3] Joint Assigned Commissioner's and Administrative Law Judge's Ruling on Proposal to Improve the Safety Culture of Pacific Gas and Electric Company and PG&E Corporation, issued on June 18, 2019 (June 18, 2019 Ruling) at 1.

Commission will bring consumers the value they pay for. Second, the Commission should make its interest in alternatives to PG&E clear. As discussed more fully below, the June 18, 2019 Ruling's proposals on CPCN review are more meaningful if there are other potential entities who are interested in and capable of serving California customers. Treating PG&E as the "only game in town," validates its culture of entitlement. Californians deserve better. In regulation as in life, alternatives yield strength. The Commission must make its interest in considering options to best serve California's utility consumers clear.

II. BACKGROUND

Time is of the essence. If the Commission does not act now, there are only two likely outcomes. One outcome: PG&E and its creditors will produce a plan that leaves PG&E in place, unreformed, with ratepayers paying what the creditors want. The other outcome: PG&E will sell out to an acquirer, chosen solely for how much it will pay to creditors and shareholders rather than how well it will serve PG&E's customers and protect the public. Either outcome forces the Commission into a take-it-or-leave-it choice, where it is pressured by "Wall Street" to "take it" rather than foster a third way. Either approach could win approval from a bankruptcy tribunal whose legal authority does not include considering anything about PG&E's electricity and gas performance, including the safety of its operations and honesty flaws.

These two outcomes are the natural result of PG&E, its creditors, and prospective acquirers pursuing their legitimate self-interests—but without the discipline, public mindedness, and emphasis on safety, honesty, and performance that PG&E's customers deserve and that Commission action would bring. The better approach—the only approach that considers customers' interests—is for the Commission to 1) indicate now that it will decide what minimum criteria the post-bankruptcy entity—whether PG&E or a successor—must satisfy and 2) start the process of attracting alternatives to PG&E

This motion is timely and time sensitive. PG&E has already declared itself the emergent bankruptcy entity and is negotiating deals that may not take into account customer interests. After September 26, 2019, when PG&E's exclusivity period ends,[4] any number of self-interested

[4] The exclusivity period is the period, determined by the bankruptcy court, during which PG&E has the exclusive right to present a plan. That period is currently scheduled to last until September 26, 2019. If PG&E files a plan by

creditors, acquirers, or creditor-acquirer pairs can get the bankruptcy court's permission to offer their own plans. Those plans need clear and transparent Commission guidance, based on a public record, if they are to reflect California's priorities for service that is safe, affordable, reliable, and consistent with the state's environmental goals.

This type of Commission guidance will not interfere with the bankruptcy proceeding. While the bankruptcy court and the Commission drive in different lanes they can drive toward a common destination: a post-bankruptcy utility that provides customers with gas and electric service that is safe, affordable, reliable, and consistent with the state's environmental goals. Nothing in either bankruptcy law or public utility law puts that destination beyond our reach. No one should misunderstand, or mischaracterize this Motion as an attempt to use state law to avoid the realities of bankruptcy law. Whatever transaction is finally approved by the bankruptcy court, the associated debt will travel to whatever company or companies, PG&E or a non-PG&E entity, will serve California's customers. Because the Commission, and only the Commission, can grant to a company the right to serve California's customers, the Commission will assist, not impede, the bankruptcy process by declaring upfront the requirements that whatever franchisees emerges from bankruptcy must meet.

Ratepayers need utility investors as much as utility investors need ratepayers. This Motion signals no intent to penalize or discourage investors. Rather, it seeks to do what bankruptcy law and utility law both need to do: Give California customers the best possible performance, and provide the best performers, the compensation they deserve.

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that date, they have an additional 60-day exclusivity period to attempt to seek confirmation of that plan, unless extended for cause by the bankruptcy court. However, at any time, a party can file a motion asking for termination of exclusivity such as the recent motion filed by the Ad Hoc Committee of Senior Unsecured Noteholders. That Motion appends as an exhibit a detailed term sheet for a proposed plan of reorganization from parties other than PG&E. *See Motion of the Ad Hoc Committee of Senior Unsecured Noteholders to Terminate the Debtors' Exclusive Periods Pursuant to Section 1121(d)(1) of the Bankruptcy Code,* filed June 25, 2019 in Bankr. Case No. 19-30088 (DM) [DE# 2741], In re PG&E Corporation and Pacific Gas and Electric Company, Bankr. N.D.Cal. San Francisco Division.

III. DISCUSSION

A. The CPCN: A privilege conditioned on performance

The franchise granted by a CPCN is a government-granted privilege: the privilege to provide, free from competition, a service essential to life, at prices that provide shareholders a fair opportunity to earn a fair return on prudent, used-and-useful investments. This privilege comes with a catch. The utility must satisfy the regulator's standards for performance—at "lowest feasible cost,"[5] using "all available cost savings opportunities."[6] The utility must pursue its public duties free of conflicting private interests.

The franchise's marriage of privilege and duty transcends any particular utility. The incumbent is but a temporary grantee; its position depends on performance. That performance has many elements: rates, reliability, quality, safety (for workers, residents, customers, and contractors), innovation, customer responsiveness, legal compliance, respect for the regulatory process, accountability, acceptance of responsibility, and honesty.

B. PG&E's Performance - Unsafe and Dishonest

Over this past decade, PG&E has failed to provide safe and reliable service. Not only has it caused death and destruction; it has dealt with the Commission dishonestly. Consider the following non exhaustive list of PG&E's actions:[7]

> ***The San Bruno Explosion (2010):*** Eight deaths, 58 injuries, 38 homes and structures destroyed. PG&E was convicted of multiple federal crimes, including willfully failing to address known recordkeeping deficiencies, and willfully failing to identify and address threats to its pipelines. PG&E also was penalized for violating state regulations. Still on probation for its federal crimes, PG&E's recent wildfire behavior is under investigation by a federal judge.

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[5] *Potomac Electric Power Co. v. Public Service Commission*, 661 A.2d 131, 137 (D.C. 1995).

[6] *Midwestern Gas Transmission Co. v. East. Tenn. Natural Gas Co.*, 36 FPC 61, 28 (1966), *aff'd sub nom. Midwestern Gas Transmission Co. v. Federal Power Commission*, 388 F.2d 444 (7th Cir. 1968).

[7] This list does not include, for example, the ongoing Order Instituting Investigation (18-12-007) into PG&E's locate and mark practices, which may identify safety problems such as if there were dig-ins associated with late marked facilities.

The Kern Power Plant Demolition (2012-2013): One death, five injuries, $5.5 million in penalties. PG&E must carry out a company-wide Corrective Action plan that included a Contractor Safety Program and an Enterprise Causal Evaluation Standard.[8]

Gas Distribution Problems (2010-2014): For multiple separate safety incidents, the Commission penalized PG&E over $36 million. The specific failures included failure to maintain proper records, failure to take corrective actions, and not being responsive to local officials.[9]

The Butte Fire (2015): Two deaths, one injury, 549 homes and 372 other structures destroyed, 70,868 acres burned. The Commission's Safety and Enforcement Division (SED) fined PG&E $8 million for failing to maintain its 12 kilovolt (kV) overhead conductors safely and properly.[10]

The Atlas Fire (2017): Six deaths, 783 homes or other structures destroyed, 51,624 acres burned. Alleging violations of state law, the California Department of Forestry and Fire Protection (CAL FIRE) has referred its investigation to the District Attorney's office.[11, 12]

The Central LNU Complex Fires (2017):[13] Three deaths, 1,355 homes or structures destroyed, 56,556 acres burned. CAL FIRE referred four of its fire investigations (Norrbom, Partrick, Pythian, and Adobe) to the appropriate local District Attorneys' offices for review "due to evidence of alleged violations of state law."[14] CAL

[8] D.15-07-014.

[9] D.16-08-020 at 2-4, 10, 51, 59-61.

[10] D.16-09-055.

[11] *See* <https://calfire.ca.gov/communications/downloads/newsreleases/2018/2017_WildfireSiege_Cause.pdf>.

[12] On June 27, 2019, the Commission opened I. 19-06-015, the Order Institution Investigation on the Commission's Own Motion into the Maintenance, Operations, and Practices of Pacific Gas and Electric Company (U39E) with Respect to its Electric Facilities; and Order to Show Cause Why the Commission Should not Impose Penalties and/or Other Remedies for the Role PG&E's Electrical Facilities had in Igniting Fires in its Service Territory in 2017. *See* <http://docs.cpuc.ca.gov/PublishedDocs/Published/G000/M303/K773/303773212.PDF>

[13] *Id.*

[14] *Id.*

FIRE did not refer the Nuns fire investigation to the local District Attorney's office.

***The Camp Fire (2018*)**: 85 deaths, 18,804 homes or other structures destroyed, 153,336 acres burned. CAL FIRE forwarded its investigative report to the Butte County District Attorney's Office.[15]

In addition to safety, there is honesty and the public trust. PG&E has committed a series of secular sins against transparency and truth. Specifically, it has been shown, and PG&E has admitted, that it engaged in:

Obstructing Investigations: After the San Bruno disaster, PG&E attempted to mislead investigators from the National Transportation Safety Board, leading to PG&E's conviction, in addition to its substantive violations, for "intentionally and corruptly tr[ying] to influence, obstruct, or impede the Board's investigation.[16]

Falsifying Evidence: The Commission has gathered evidence of PG&E routinely (thousands of times) falsifying records on locate-and-mark practices.[17]

Lobbying in Secret: PG&E has long tried to influence Commission decisions secretly—and illegally. Due to PG&E's 2007 violations of *ex parte* communications rules,[18] the Commission in 2008 required PG&E to "develop written best practices to document, control, and report on *ex parte* contacts."[19] In 2015, the Commission identified improper *ex parte* communications as early as June 19, 2009, disappointingly soon after the Commission had directed PG&E to develop written best practices on *ex parte* contacts.[20] These contacts continued over at least a five year period from mid-2009 through mid-2014.

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15 *See* <http://calfire.ca.gov/communications/downloads/newsreleases/2019/CampFire_Cause.pdf>

16 See <https://www.justice.gov/usao-ndca/pr/pge-ordered-develop-compliance-and-ethics-program-part-its-sentence-engaging-criminal>.

17 Order Instituting Investigation (I.) 18-12-007.

18 The *ex parte* communications rules determine if and how parties (such as PG&E or Cal Advocates) can communicate with decision-makers at the Commission during a formal proceeding. Decision makers include the Commissioners, their advisors, and the Administrative Law Judges. The purpose of these rules is to prevent secret communications that can affect case outcomes.

19 I. 15-11-015, Finding of Fact #1, p. 38.

20 I. 15-11-015, p. 3.

> PG&E's presidents, a senior vice president, two vice presidents, and at least one consultant were either violators or benefited from the violations.[21]

These facts form the foundation of the Commission's Safety Culture and Governance investigation.

Californians deserve a utility that serves competently, lawfully, and honestly. Convicted of breaking laws and obstructing justice, found at fault for death and destruction across its service territory, and now under investigation for false filings and improper communications with regulators, PG&E has not been that utility.

C. PG&E's Culture of Entitlement

Investigations, penalties, convictions, fines, and probations have not worked.[22] Executive shuffling hasn't worked.[23] Reorganizations haven't worked.[24] Replacing and overpaying board members[25] won't work. PG&E is a reactor not a creator. "Driven by immediate needs," it reacts to its failures instead of creating a "comprehensive enterprise-wide approach."[26] PG&E's problems are— "not just one-off situations or bad luck," but problems that are "deeper and more systemic"—problems that remain unsolved.[27] PG&E's problems come from its culture. Because its misbehaviors go beyond safety, its safety culture problem is but a symptom of a broader culture problem. PG&E has a culture of entitlement.

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[21] I. 15-11-015, Phase 2 Joint Evidentiary Record, dated May 15, 2019, pp. I-1 to I-2.

[22] Scoping Order at 5-6 (stating that "imposing penalties on PG&E did not seem to change the situation").

[23] Since 2010, PG&E has replaced four presidents (Darbee, Johns, Stavroplous, Williams); three senior vice presidents (Botorff, Soto, Hogan); and five vice presidents (Cherry, Horner, Franke, Dasso, Lemier).

[24] August 22, 2018 PG&E Announces Interim Organization Structure While Conducting COO Search <http://investor.pgecorp.com/news-events/press-releases/press-release-details/2018/PGE-Announces-Interim-Organization-Structure-While-Conducting-COO-Search/default.aspx>.

[25] In 2018, the average compensation for PG&E's board members was $257,000 per year for part-time work. PG&E Corp, *Joint Notice of 2019 Annual Meetings, Proxy Statement* at 46 (June 21, 2019).

[26] Scoping Order at 6, quoting Northstar Report at I-1.

[27] Scoping Order at 5.

A culture of entitlement cannot be solved with investigations, penalties, convictions, fines, probations, personnel changes, or press releases. These actions miss the main cause of PG&Es' entitlement culture - our policy on franchises. The utilities assume their monopoly franchises exempt them from competition in perpetuity. As decades go by, costs rise, performance slips, patterns of rule violations and lax compliance emerge and a culture of entitlement is established. The utility expects to remain the monopoly franchisee indefinitely, no matter how many felonies it commits, how many rules it breaks, or how unsafe its practices. No amount of investigations, penalties, convictions, probations, personnel changes and board replacements can fix a company with a culture of entitlement. Instead of punishing behaviors that derive from entitlement, we must change the expectations that cause the entitlement. Instead of punishing the results of failure, we must create the conditions for success.

In a competitive market, a company with PG&E's record would be long gone, left behind by workers, investors, and customers, all seeking safer, more honest places to work, invest, and buy. Treating PG&E as our only option and its CPCN granted franchise as its permanent right, validates PG&E's culture of entitlement. The Commission must make its willingness to consider alternatives clear and public.

D. Bankruptcy's outcomes: Four possible paths

A bankruptcy proceeding typically produces a plan of reorganization. Per the bankruptcy court's ruling, through September 26 of this year the exclusive proposer of a plan is PG&E. Beginning September 27, others permitted by the court may submit a plan.[28] At some point, a plan will gain sufficient support among creditors to receive the court's tentative approval. Where the bankrupt company is a utility, the court may grant final approval only if the plan's rate path has received Commission approval.[29]

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[28] *See* "Order Pursuant to 11 U.S.C. § 1121(d) Extending Exclusive Periods." Bankruptcy Case No. 19-30088, Docket Entry 2226 (May 23, 2019).

[29] *See* 11 U.S.C. § 1129(a)(6).

1. Path 1: PG&E emerges as franchisee, unconditionally

During or after the present period of exclusivity, PG&E could reach agreements with its creditors, present to the Court a plan with a rate path, get the bankruptcy court's conditional approval of the plan (other than the rate path), get the Commission to approve that rate path, then get the bankruptcy court's final approval. There would be no necessary change in PG&E's operational performance. Commission investigations into gas safety, wildfire performance, honesty in reporting, and other matters would continue as before.

2. Path 2: PG&E emerges as franchisee, subject to Commission probation

This path is like Path 1, but with a key difference: The Commission would require, as a condition of approving the rate path, PG&E's compliance with specific performance metrics (such as for safety and honesty), the breach of which would cause the Commission to consider penalties including revocation of PG&E's franchise—subject to the Commission selecting one or more replacement franchisees competitively.

3. Path 3: One or more non-PG&E franchisees replaces PG&E, in whole or in part

A plan may include the sale of all or a portion of PG&E. If the Commission establishes minimum prerequisites for all potential post-bankruptcy franchisees (as recommended under Action #1 above), then whatever bidder(s) emerge(s) with the bankruptcy court's approval will necessarily satisfy those prerequisites, because the bankruptcy court will not likely approve an acquirer that the Commission would reject. Only the Commission, not the bankruptcy court, can award franchises or approve transfer of control of a California utility's assets or control.

4. Path 4: PG&E emerges from bankruptcy with a temporary franchise, with PG&E to be replaced as franchisee after a defined period

This path is like Path 3, but separates the bankruptcy decision-making from the franchise decision-making. That way, the State can take the time it needs to (1) determine minimum franchise prerequisites (including defining the different services that will be subject to the franchise), and (2) run the competition to select new franchisees. The time period necessary might not mesh well with the bankruptcy court's wish to complete its work expeditiously. But for PG&E to keep its franchise by default—merely because the Commission has insufficient time to complete its own work—would ill serve the public. At the same time, PG&E's creditors deserve to know PG&E's future. So the Commission could declare, after making the necessary legal findings, that (a) PG&E's role as franchisee will end no later than, say, two years after it emerges from bankruptcy; and (b) the Commission during that two-year period will select one or more replacements for all or part of PG&E's utility activities. The Commission would issue its decision about PG&E in time for participants in the bankruptcy process to take it into account. PG&E then would emerge from bankruptcy with a franchise that everyone understood to be temporary. Participants who wanted a chance to acquire or replace PG&E would make their bids before the Commission rather than before the bankruptcy court.

We do not yet recommend any of these paths; we describe them here to emphasize the Commission's options. As the Governor's Strike Force emphasized, all options must be on the table.[30] And while bankruptcy does have some potentially preemptive effects, those effects do not reach the options discussed here. For an explanation, see the Appendix I: "Bankruptcy Law Does not Preempt the Commission's Decisions on Franchisee Qualifications."

E. Necessary Actions

Action 1 - Establish performance prerequisites for post-bankruptcy franchisees, including PG&E

The franchise created by a CPCN is a privilege granted by the government, not an asset owned by the utility.[31] As this Commission stated, in opening this investigation into PG&E's culture:

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[30] Governor Newsom's Strike Force, Wildfires and Climate Change: California's Energy Future, Executive Summary at 4.

[31] *See New Orleans Gas Co. v. Louisiana. Light Co.*, 115 U.S. 650, 669 (1885) (franchise "belong[s] to the government, to be granted, for the accomplishment of public objects, to whomsoever, and upon what terms it pleases"); *Bank of Augusta v. Earle*, 38 U.S. (13 Pet.) 519, 595 (1839) (franchises are "special privileges conferred by government upon individuals, and which do not belong to the citizens of the country generally of common right").

> The Commission, invested by the California Constitution and the Public Utilities Code with police power to regulate public utilities, among other actions sets rates, authorizes capital investments and operating budgets, and awards franchises to companies such as PG&E. A 'franchise to operate a public utility … is a special privilege which … may be granted or withheld at the pleasure of the State.' Holding that franchise, PG&E must 'comply with the comprehensive regulation of its rates, services, and facilities as specified in the Public Utilities Code.' And the Commission must actively, not passively, supervise and regulate public utilities.[32]

This authority underlies the June 18, 2019 Ruling's consideration of a periodic review of a utility's CPCN as a means to provide "additional incentive for the utility to do a good job."[33] In California, a utility receives its franchise "in return for" its performance.[34] The franchise thus is conditioned on meeting the Commission's, customers' and the public's expectations.[35] While the June 18, 2019 Ruling's questions about a periodic review of a utility's CPCN are consistent with the authority identified above, the Ruling does nothing to identify potential replacements for PG&E, without which a CPCN review will be limited at best. The Commission must take full advantage of its authority to issue and rescind franchises in order to address PG&E's culture of entitlement.

If the Commission wishes to provide "additional incentive for the utility to do a good job,"[36] it must disabuse PG&E of the notion that it is entitled to continue to operate as a franchise under its CPCN in perpetuity. For the Commission to break the culture of

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[32] "Order Instituting Investigation on the Commission's Own Motion to Determine Whether Pacific Gas and Electric Company and PG&E Corporation's Organizational Culture and Governance Prioritize Safety," Investigation 15-08-019, 2015 Cal. PUC LEXIS 539 at § 3.4 (citations omitted).

[33] June 18, 2019 Ruling at 3.

[34] "In return for safe and reliable natural gas service, the Commission provides a relatively exclusive *franchise*, recovery of all just and reasonable costs to serve customers, and a very low-risk and ample rate of return." "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," 2012 Cal. PUC LEXIS 39.

[35] *Id.* at § 3.5 ("This investigation should begin with what the Commission, customers, and the public should expect from PG&E when the State awarded PG&E its franchise and approved PG&E's rates.").

[36] June 18, 2019 Ruling at 3.

entitlement, it must also consider alternatives to PG&E by defining the performance customers deserve, then finding the best performers. In the current context, the Commission must establish priorities that any post-bankruptcy franchisee must satisfy. Then to make those priorities realities, it must seek non-PG&E alternatives whose reorganization plans will align with those priorities. Amending the June 18, 2019 Ruling to solicit comments that will assist the Commission in establishing criteria that any post-bankruptcy franchisee must satisfy will give PG&E and other potential franchisees fair notice of what the Commission requires. As discussed below, these criteria include services and quality, and company characteristics (i.e. ownership structure, corporate governance, attitude toward quality, and attitude toward regulation and regulators).

1. Services and quality

Energy service today takes multiple forms: generation, procurement, transmission, distribution, demand aggregation, distributed energy resources, conservation services, microgrids, storage, electric vehicle infrastructure. An investor-owned utility is either the primary operator or provider of these services or has some role in administrating programs that provide these services. As such, it is important that the utility's work to provide these services includes ensuring safety, reducing emissions, lowering costs, and maintaining reliability. What are a utility's standards of performance in the provision of these services?

2. Company characteristics

A provider's characteristics affect its performance. And those characteristics can complicate, or simplify, regulators' efforts to induce performance. So we must ask: What kind of companies will best provide the necessary services, cost-effectively and safely? The relevant company characteristics fall into four main categories.

- ***Ownership Structure*** - The Scoping Order refers to "publicly owned utility, cooperative, community choice aggregation or other models."[37] There are, of course, more categories and multiple variations within those categories: government ownership (municipal, regional, state); private ownership (non-profit, for-profit, and semi-profit); publicly traded and privately traded; holding company-owned and retail shareholder-owned.

[37] "Assigned Commissioner's Scoping Memo and Ruling," I. 15-08-019 at 12 (Dec. 21, 2018).

Different business forms bring different strengths and weaknesses. All must satisfy these minimums: (i) no conflict between earning profit and pursuing the public interest in safety and cost, (ii) commitment to transparency, (iii) commitment to the state's clean energy goals, and (iv) respect for workers and their unions.

- ***Corporate Governance*** - Governance affects accountability; accountability affects performance. Who controls which decisions? Who is accountable to whom, for what types of performance? How does the company pay its people? Do compensation methods create conflicts between profit and performance, between executives' interest and customers' interest? Do the boardroom and the workforce reflect the communities the company serves?
- ***Attitude Toward Quality*** - Does the company aspire to excellence or does it rest on its government-protected laurels? Does it look ahead for hazards to prevent and create plans to prevent them—or does it wait for disasters to happen, then seek full credit for its response and full payment for its costs?
- ***Attitude Toward Regulation and Regulators*** - Each company views regulation self-interestedly. Everyone wants regulation when it protects; but not when it constrains. Does the company respect the regulatory process—especially its key features of transparency, facts, logic, and law—or does the company rely on non-factual forms of persuasion, and use non-transparent paths to persuade?

Why do these company characteristics matter? A prospective franchisee's business mix will determine whether it has internal conflicts between the utility's public service obligation and its holding company's private business priorities. Companies that mix utility and non-utility businesses have an internal conflict over scarce capital. Companies that compensate their executives based on share price or earnings have an internal conflict between shareholder interest and ratepayer interest. Companies with internal conflicts require more regulatory effort than companies without those conflicts. And regulatory efforts do not always succeed.[38]

[38] *See, e.g.*, this Commission's Decision No. 91-05-028, supra at 277 ((“[I]f Edison's past violations of the regulatory compacts set forth in our … decision [authorizing SCE's holding company] are any indication of what will transpire in the future, it will be increasingly difficult to ensure that inappropriate costs are not passed on to ratepayers. . . . Edison has attempted to use [that decision] to shield its activities rather than open the Commission's access to expeditious and thorough review. Such contentiousness produces increased burdens on the Commission. . . .”).

Action 2 - Foster the development of non-PG&E alternatives whose reorganization plans align with Commission priorities

As noted above, if we treat PG&E as our only alternative and treat its CPCN granted franchise as its permanent right, we validate PG&E's culture of entitlement. Californians deserve better. The Commission must make its willingness to consider alternatives clear and foster the development of non-PG&E alternatives if it intends to improve utility safety and service.

3. Finding the candidates, causing them to compete

Since 1985, dozens of electric utilities have been acquired, most at substantial premiums.[39] From this simple fact, we know that owning a utility, or controlling a utility monopoly franchise is desirable. If California opens its doors to prospective franchisees, the competition for the customers' favor will be vigorous.[40]

How do businesses find employees and manufacturers find suppliers? They search for the best, then choose the best. Rather than awarding a franchisee non-competitively or threatening to review a CPCN in the absence of any viable alternatives, California's decision-makers should do what everyone else does: Create a competition—here, a competition for the privilege of being a monopoly. "[T]he public has an obvious interest in competition, 'even

[39] For a list of those acquisitions through 2017, and an analysis of their regulatory approvals, *see* Scott Hempling, :Inconsistent with the Public Interest: FERC's Three Decades of Deference to Electricity Consolidation," *Energy Law Journal* (Fall 2018), available at <https://www.eba-net.org/assets/1/6/15-233-312-Hempling_[FINAL]1. pling_%5bFINAL%5d1.pdf>.

[40] Another example comes from South Carolina, where a special legislative committee in late 2018 issued a request for expressions of interest and indicative offers to acquire the state-owned utility, Santee Cooper. According to the committee's then-consultant ICF, which ran the process, the request attracted 15 "strong and diverse" proposals: seven full purchase proposals and eight others: long-term asset management agreements, long-term power supply arrangements, and partial acquisitions. *See* ICF's evaluation of February 2019, available at <https://governor.sc.gov/sites/default/files/Documents/newsroom/ICF%20Evaluation%20of%20EOI%20Responses%20for%20Santee%20Cooper.pdf>.

In May 2019, the South Carolina Legislature enacted legislation directing the state's Department of Administration to conduct a full-fledged competition for acquirers and managers of Santee Cooper, as well as an evaluation of the utility's standalone plans.

though that competition be an elimination bout.'"[41] Using competition to find the best performers, and having replacements ready to replace those performers, is challenging but it is the path to real performance. Granting someone a permanent monopoly, then fining, penalizing, and "incentivizing" them to improve, or juggling board membership and serially replacing executives, does not work.

The following is an illustrative six-step process to create competition for new franchisees.

> ***Step 1. Issue Order starting the process:*** The Commission issues an Order announcing it will hold a competitive process for choosing one or more franchisees to serve in PG&E's territory. The Order should describe the end goal: to have Californians served by the most cost-effective, customer-responsive, safe, environmentally responsible, innovative and reliable provider or providers. The Order also should describe the steps that will follow and pose a series of questions that invite creative ideas from stakeholders and prospective bidders.
>
> ***Step 2. Spread the word:*** The Commission, likely through an agent, creates interest in the marketplace by spreading the word about the Commissions goals, and informally contacting entities that might have an interest in serving. This outreach serves multiple purposes: stimulating interest, identifying new firms or organizations, and identifying any concerns about regulatory uncertainties that might discourage bidders from competing. Some prospective competitors might want to buy the entire company, others only some of the assets; some might want to serve the entire service territory; others only parts. Some might want to provide only monopoly services; others might want to provide both monopoly and competitive services.
>
> ***Step 3. Hold a technical workshop:*** The Commission would hold one or more technical workshops. Using materials from stakeholder submissions and intelligence gathered through the market conversations, the Commission staff would have a dialogue with stakeholders (about what services they want from a franchisee) and prospective bidders (about what clarity they need on regulatory policy). At the technical workshop, people could ask questions of PG&E as well as Commission staff.
>
> ***Step 4. Establish threshold criteria:*** The Commission would establish threshold criteria for eligibility to compete. Examples of requirements for eligibility (illustrative only):
>
> a. The company has a minimum number of years of experience providing safe, affordable, reliable energy utility services consistent with the state's environmental goals in rural and urban areas.

[41] *Hecht v. Pro-Football, Inc.*, 570 F.2d 982, 991 (D.C. Cir. 1977).

b. Demonstrated ability in meeting or exceeding the minimum federal, state, and local safety requirements.

c. The company has a demonstrated commitment and ability to carry out the state's clean energy goals.

d. The company has a demonstrated commitment to integrity, transparency, and honesty in its relations with the public, regulators and other stakeholders.

e. The company has a demonstrated respect for workers and their unions.

f. If the competitor is part of a holding company system, that holding company system is not complex, overly leveraged, or invested in businesses whose risks or strategies conflict with a utility's obligation to serve.

g. The company satisfies Commission criteria designed to reduce the risk of horizontal or vertical market power.

h. The company has the financial capability both to execute the purchase (paying the shareholders and paying off or taking on the debt) and to operate successfully.

Step 5. Issue formal requests for proposals: The Commission would design a formal Request for Proposals for the particular services that franchisees would provide. Competitors including PG&E could offer the entire package or a subset (although the Commission will likely want to place appropriate limits on what types of geographic areas would be carved out to avoid cherry-picking).

Step 6. Choose the franchisees: The Commission then would apply its evaluative criteria and choose the winning franchisees. Evaluative criteria could include: experience, record of customer responsiveness, record of regulatory relationships, operational record, employee relations, ethical character, creativity in developing resource plans, likely rate path, price offered, non-quantifiable benefits offered.

4. Avoiding negative outcomes

While we seek positive outcomes, we must avoid potential negative outcomes or gaming. While three such potential outcomes come to mind, more may arise in response to questions posed herein.

a. Cherry-picking: PG&E's service territory covers diverse geographic areas and diverse members of the population. Despite this diversity, all customers within a rate class face the same electric and gas rates, just as all individuals face the same tax rates. The Commission must discourage proposals that cherry-pick lower-cost and lower-risk subregions, leaving the higher cost and higher risk ones behind. A utility's obligation to serve—the very foundation of an exclusive franchise—exists to prevent precisely this type of redlining. The Commission must make clear that the franchisee is a privilege that includes this obligation; it is not some acquisition opportunity to be carved, shaped and resold for maximum profit. That is not to say that PG&E's entire, vast service territory must remain whole, especially if the Commission were to find that economies of scale no longer favored (if they ever did) a region this large. A useful principle: Ensure that if portions of the current service territory are sold to different acquirers, no customer is made worse off.

b. ***A bailout without accountability:*** Allowing PG&E to emerge with reduced debt but an unchanged culture of entitlement—is dangerous for California's consumers and businesses. This path presents a risk to customers: that PG&E, unguided by Commission prerequisites, will work with creditors to pour concrete around a plan that maximizes creditors' return, then pressure the Commission to raise rates to implement it. Additional pressure would come from the financial community (that is, the portion of the financial community connected to PG&E—not the portion wishing to invest in alternatives to PG&E)—all arguing the customary platitudes: PG&E is too big to fail, uncertainty raises costs for all. But because the bankruptcy court has no statutory power to improve PG&E's performance, this path has the customers protecting the creditors from their losses but getting left with an unreformed PG&E. The best protection against this path is for the Commission to start developing alternatives.

c. ***Investor expectation that PG&E's franchise will remain uncontested:*** California has never subjected its major utility franchises to competition—even after multiple occasions of franchise-breaching conduct. If the Commission says nothing now, and PG&E emerges from bankruptcy under Path 1, its investors could reasonably conclude that PG&E's future will be like its past—that it can commit any manner of crimes and violations, at no risk of losing its privileged position. While the Commission's silence would not create a constitutionally protected expectation of future franchise permanence, any later Commission effort to question PG&E's franchise would likely provoke the type of vocal outrage disappointed people use, strategically, to cause those lacking alternatives to fear developing alternatives.

F. The Consequences of Inaction: The Bankruptcy Court Displaces the Commission and Price Displaces Performance

We have explained how the Commission can establish prerequisites for post-bankruptcy franchisees, and seek non-PG&E alternatives whose reorganization plans align with Commission priorities, without impeding the bankruptcy court's jurisdiction. If the Commission fails to take those two steps? The bankruptcy process can, in practice if not in law, diminish the Commission's powers. This concern has at least three bases.

- ***The bankruptcy court has no duty to produce cost-effective utility performance.*** Bankruptcy courts focus on approving a plan that satisfies the creditors' legitimate interests while preserving, if possible, the debtor's business. The bankruptcy court has no legal power to make a utility's performance safer, to address its honesty issues, or to fix its culture of entitlement. So if PG&E and its creditors agree on a plan to sell the company, the utility will be sold to the highest bidder, not to the best performer, with the ratepayers covering the cost—unless the Commission specifies its prerequisites for PG&E's purchaser. Bankruptcy law does not preempt the Commission's state law power to approve or disapprove an acquisition of PG&E or its assets. But if the Commission does not state its requirements in advance of the Bankruptcy court's actions, it will be stuck with the bare, suboptimal choice of Yes or No to a proposal not of its own making. Or the Commission will end up negotiating in private with PG&E and its prospective acquirers, then hand intervenors in the Commission approval proceeding a single take-it-or-leave-it plan—with no opportunities for intervenors to reshape the result because the plan's sponsors will claim it rests on agreements "too fragile," too "painstakingly negotiated," to be changed.

- ***PG&E's motivations conflict with the public's interest in performance.*** In the bankruptcy proceeding, PG&E's goals are self-interested: Emerge with lighter debt and maintain control of the monopoly franchise; or, get the highest price possible for its shareholders, paid for by ratepayers. In the bankruptcy proceeding, PG&E has no obligation to improve performance or changes in its culture. So in terms of performance and culture, post-bankruptcy PG&E could be the same as pre-bankruptcy PG&E—or worse.

- ***The creditors' goals conflict with the public's interest in performance.*** The creditors' goal is to be paid. While those who continue to hold bonds will not be indifferent to the utility's future performance (since penalties and fines hurt the bottom line), their priority is payment, not performance.

These three factors all point in one direction: The bankruptcy process will emphasize payments over performance. However, readers should not take this point separate from its context. Cal Advocates respects creditors' legitimate claims. But ratepayers also have material and substantive rights—to performance commensurate with the rates they pay. The best solution—one that marries bankruptcy's priorities with the Commission's obligations—is what this Motion urges: that the Commission set standards that bring competitors who can perform with excellence and get the creditors paid. But to make this marriage work, the Commission needs to act, and act now. Relying solely on its legal ability to block a plan later based on its rate path[42] will not get California the best performance it needs. The Commission needs to make clear to the bankruptcy court that it will approve a post-bankruptcy PG&E, or new owner of PG&E, or a new successor to PG&E, or a rate path for PG&E or its successor, only if that entity, among all possible entities, best meets the Commission's criteria for performance. Only by acting now to influence to-be-filed plans or sale proposals brought in bankruptcy court, not by reacting to filed plans or sale motions, can the Commission's priorities prevail.

IV. CONCLUSION

The clock is ticking: The Commission must establish its priorities before non-PG&E acquirers appear.

The Commission must take action. It must define the features of, and expectations for, the franchisee's performance. Then to ensure that customers receive that performance the Commission must find the best performers.

These Commission actions must happen soon. On September 26, 2019, PG&E's current exclusivity period ends. Absent Commission-set prerequisites, either creditors will accept a PG&E proposal or, starting September 27, 2019 other entities will offer plans that serve their interests. Unless it declares its criteria, the Commission will be a bystander and reactor. It is only by acting now that the Commission can produce a result that satisfies creditors' legitimate needs, while also ensuring that California's ratepayers are served by the best performer.

The Public Advocates Office urges the Commission to amend its June 18, 2019 Ruling to align with the broader goals of this proceeding by adding the questions in Appendix II, which address the prerequisites necessary to ensure Californians are provided the service they deserve and to begin laying the framework for seeking alternative providers.

[42] Under 11 U.S.C. § 1129(a)(6).

Respectfully submitted,

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Appendix I

Bankruptcy Law Does not Preempt the Commission's Decisions on Franchisee Qualifications

The filing of a bankruptcy petition triggers, under Section 362 of the Bankruptcy Code, an "automatic stay." The stay prevents litigation against the debtor that attempts to enforce or collect on financial claims that pre-dated the petition.

The automatic stay does not apply, however, to "the commencement or continuation of an action or proceeding by a governmental unit . . . to enforce such governmental unit's or organization's police and regulatory power, . . ." Bankruptcy Code § 362(b)(4). Applying this language, courts have developed two tests: the pecuniary purpose test and the public policy test. The pecuniary purpose test asks whether the government action relates primarily to the protection of the government's pecuniary interest in the debtor's property or to matters of public safety or welfare. If the former, the police-and-regulatory power exception is unavailable; the automatic stay applies. But if regulatory action carries out public policy, it is exempted from the stay.

Even if the regulatory action affects the debtor economically, if its purpose is public policy the stay does not apply.[43] PG&E's last bankruptcy case illustrates the point. Before PG&E filed its bankruptcy petition, the Commission required it to transfer negative balances to a Transition Cost Balancing Account. After filing for bankruptcy, PG&E argued that the Commission's effort to enforce that decision violated the stay. Judge Montali (the bankruptcy Judge then and now) disagreed. He held the Commission's primary purpose was public policy. That the result may be a negative economic impact on PG&E, and a positive impact on PG&E's customers, does not change the fact that the Commission's ratemaking implements public policy. PG&E also argued that the Commission's decision adjudicated private rights (a sign of pecuniary

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[43] *See generally MLRD v. Continental Hagen Corp.*, 932 F.2d 828, 833 (9th Cir. 1991).

purpose, which cannot avoid the stay), by favoring consumers at PG&E's expense. The court again disagreed concluding that the Commission's action was "more legislative in character"; and, that the regulating of utilities, wrote the court, "is one of the most important of the functions traditionally associated with the police power of the states."[44]

In particular, the bankruptcy court's approval of an acquirer does not force a state to grant that acquirer control of the franchise. We know this from the Texas experience. The retail utility Oncor was owned 80 percent by Energy Future Holdings Corp ("EFHC"). EFHC went bankrupt. The federal bankruptcy court approved Oncor's acquisition by NextEra (the holding company for Florida Power & Light). But the Texas Commission rejected NextEra because NextEra wanted control of Oncor's utility cash flow to pay off NextEra's high acquisition debt. The court then approved a bid from Sempra (the holding company for San Diego Gas & Electric Company)—again subject to the Commission's approval, which was granted. Both times, no one argued preemption.[45]

Caution: *This Commission should not follow Texas's approach of waiting for the bankruptcy court outcome before disapproving the result.* Doing so makes a Commission a spectator rather than a decision maker. The Commission should make clear, now, that it will approve only the best performer, not the highest bidder.

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[44] PG&E's previous bankruptcy was addressed in *In re Pac. Gas & Elec. Co.*, 263 B.R. 306 (Bankr. N.D. Cal. 2001). The passages quoted here appear at *id.* at 318-20 (citing *Ark. Elec. Coop. Corp. v. Ark. Pub. Serv. Comm'n*, 461 U.S. 375, 377 (1983)).

[45] On Oncor, see *Joint Report and Application of Oncor Electric Delivery Company LLC and NextEra Energy*, Docket No. 46238, Tex. Pub. Util. Comm'n, (Apr. 13, 2017). On Sempra, see *Joint Report and Application of Oncor Electric Delivery Company and Sempra Energy for Regulatory Approvals*, Docket No. 47675 (Mar. 8, 2018). While bankruptcy litigants behave as if the state commission is not preempted from rejecting a bankruptcy-approved acquirer, that specific question has not been litigated. The Ninth Circuit has held that a court-approved bankruptcy reorganization plan is preemptive of state regulation "relating to financial condition" under 11 U.S.C. § 1142(a). *See Pacific Gas and Electric Co., et al. v. People of the State of California,* 350 F.3d 932, 937, 948 (9th Cir. 2003). While the appeal was pending the bankruptcy judge terminated debtor's exclusivity, the Commission filed its own competing plan, leading to the confirmation of an entirely different plan. As a result, there has been no judicial determination whether Commission regulation of corporate ownership structure is regulation "relating to financial condition."

Appendix II
Amendments to the June 18, 2019 Ruling - Additional Questions for Parties

ADD new section 2.5 to the June 18, 2019 Ruling:

2.5 Minimum requirements for Serving PG&E's Ratepayers in the Post-Bankruptcy Era

This question begins the process of developing the minimum criteria the Commission should require of a post-bankruptcy franchisee.

What are the minimum criteria the Commission should require of a post-bankruptcy franchisee, whether PG&E or another entity? Consider for example:

d. The company has a minimum number of years of experience providing safe, affordable, reliable energy utility services in rural and urban areas consistent with the state's environmental goals.

e. Demonstrated ability in meeting or exceeding the minimum federal, state, and local safety requirements.

f. The company has a demonstrated commitment and ability to carry out the state's clean energy goals.

g. The company has a demonstrated commitment to integrity, transparency, and honesty in its relations with the public, regulators and other stakeholders.

h. The company has a demonstrated respect for workers and their unions.

i. If the competitor is part of a holding company system, that holding company system is not complex, overly leveraged, or invested in businesses whose risks or strategies conflict with a utility's obligation to serve.

j. The company satisfies Commission criteria designed to reduce the risk of horizontal or vertical market power.

k. The company has the financial capability both to execute the purchase (paying the shareholders and paying off or taking on the debt) and to operate successfully.

ADD new section 2.6 to the June 18, 2019 Ruling:

2.6 Possible Requirements of Bidders and Bids

These questions help begin defining the procedure by which the Commission can attract prospective franchisees.

A. By what procedures might the Commission use to (a) collect expressions of interest, and then (b) conduct a competitive bidding process? Are there analogies from government procurement processes that would be helpful?

B. How can the Commission ensure that prospective bidders for portions of PG&E's system do not cherry-pick parts of the system, or avoid their appropriate share of costs associated with existing debt, public purpose programs, or long-term contracts?

C. How can the Commission avoid a situation in which bidders offer an acquisition premium for PG&E's stock and then seek recovery of the premium in rates?