BEFORE THE PUBLIC UTILITIES COMMISSION
OF THE STATE OF CALIFORNIA

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Application of Pacific Gas and Electric Company for a Two-Year Extension of the ClimateSmart TM Program and Tariff Option. (U 39 M)	Application 09-05-016 (Filed May 18, 2009)

OPENING COMMENTS OF PACIFIC GAS AND ELECTRIC COMPANY ON PROPOSED DECISION GRANTING DAY-TO-DAY EXTENSION OF CLIMATE SMART PROGRAM

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Dated: November 10, 2009

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I. INTRODUCTION

Pursuant to Rule 14.3 of the Commission's Rules of Practice and Procedure, Pacific Gas and Electric Company (PG&E) provides its opening comments on the Proposed Decision (PD) granting PG&E a day-to-day extension of its ClimateSmart™ Program and tariff option, pending a decision by the Commission on the merits in this proceeding, expected during the first quarter of 2010.

PG&E supports and appreciates the PD's day-to-day extension of the program pending a merits decision in this proceeding. This extension will ensure that there is no disruption in the Program and services provided to 30,000 PG&E customers who are enrolled in the Program. PG&E also appreciates the constructive support and cooperation provided by TURN and DRA for the day-to-day extension, even while those parties and PG&E may not be in complete agreement on the merits of PG&E's application to extend the Program for two years.

PG&E requests one change to the PD in order to avoid an unintended disruption in the ClimateSmart™ Program during the day-to-day extension period: PG&E requests that the temporary restriction on marketing expenses and cap on administrative expenses in the PD be deleted, because they would unnecessarily restrict PG&E's ability to administer the Program, negotiate and procure greenhouse gas emissions offsets, and educate and enroll new customers on a day-to-day basis during this period. Alternatively, if the Commission believes a cap on costs is essential during this interim period, PG&E recommends a cap that is based on the minimum level of expenses PG&E expects to incur to keep the Program running at an adequate level of service during the three-month period.

PG&E describes this requested change to the PD in more detail in the next section.

II. THE RESTRICTION ON MARKETING EXPENSES AND CAP ON ADMINISTRATIVE EXPENSES IS UNNECESSARY, BECAUSE PG&E IS ALREADY INCENTED TO MINIMIZE SUCH COSTS IN ORDER TO COMPLY WITH THE PERFORMANCE GUARANTEE

The PD would prohibit PG&E from spending any ratepayer funds on marketing for the Program during the day-to-day extension, and would cap PG&E's administrative expenses at $20,000 per month. PG&E believes these restrictions are unnecessary and unreasonable, because PG&E shareholders are already at risk for obtaining insufficient revenues from customers to meet the 1.5 million ton performance guarantee at the end of the Program, and thus already under a powerful incentive to minimize costs during the day-to-day extension that do not add revenues at least equal to the costs.

The arithmetic of this is very simple. If PG&E has only $4 million in unspent funds available at the end of 2009 for the costs of the Program, and needs to obtain an additional $5 million in new customer revenues under the Program in order to procure an additional 500,000 tons of emissions reduction projects @ $9.71 per short ton, then every dollar that PG&E spends for the Program that does not result in at least a dollar or more of new revenue, is a dollar of loss that shareholders will incur at the end of the Program.[1/]

1/ These numbers are illustrative but pretty close to actual projections. See slide 17 of PG&E's presentation at October 22, 2009, workshop in this proceeding.

Thus, during the day-to-day extension period, PG&E is under a strong incentive to maximize customer revenues net of expenses, and thus minimize cost-ineffective expenses, both marketing and administration. Thus, it is unnecessary for the Commission to cap or restrict PG&E's expenses during this period, particularly in light of the fact that PG&E is not requesting additional ratepayer funding or relaxation of the performance guarantee on the merits in this application.

III. IF THE COMMISSION DETERMINES THAT A CAP ON ADMINISTRATIVE AND MARKETING EXPENSES IS ESSENTIAL DURING THE DAY-TO-DAY EXTENSION PERIOD, THE CAP SHOULD ALLOW COSTS THAT ARE NECESSARY TO PERFORM KEY PROGRAM COMPLIANCE ACTIVITIES AND MAINTAIN PG&E'S GREENHOUSE GAS REDUCTION PROJECTS

If the Commission determines that a cap on PG&E's administrative and marketing expenses is essential during this interim period, PG&E requests that the cap be set at the level necessary to allow PG&E to continue to perform key compliance activities and to maintain its ongoing greenhouse gas reduction projects.

A. Essential Program Administration, Compliance and Marketing Expenses

During the day to day extension period, basic Program administration activities include functions such as enrollment of customers, responding to customer inquiries, and operational aspects of the Program such as billing, accounting, and reporting. In addition, there are particular requirements that are unique to the first quarter of the year: the preparation of the prior year's annual report for the CPUC, an annual report for Program customers, and the charity tax letters which are sent to all ClimateSmart™ Program customers to inform them of their tax-deductible contributions during the prior year.

The Program administration budget is largely a labor budget; however the annual reports and charity tax letter preparation and mailing have material costs as well. The program administrative support will be reduced to 90% of one full-time employee's

(FTE) time to manage the Program, as well as minimal support from various internal departments such as finance, accounting, information technology, and customer care organizations.

Altogether, funding to support the administration of the Program during this day to day extension will require **$35,500 per month**. In addition, the cost to produce and distribute the CPUC annual report, the customer annual report, and the charity tax letters is a one-time cost of **$36,000. The total expenses that PG&E requests for these activities during the three-month period is $142,500, or $47,500 per month**.

PG&E also requests limited and minimal marketing-related funds during this period solely to maintain the Program's customer communication and enrollment infrastructure. This is necessary to maintain existing infrastructure including the ClimateSmart™ Program's website, quarterly e-newsletter, social media, and collateral/merchandising for our existing customers. To stop these activities even temporarily would create a significant communication void and lead to customer confusion for existing enrolled customers as well as new customers seeking information about the Program. For example, customers regularly use the website to enroll, obtain updates on the projects in which their money is being invested, calculate their carbon footprint, and find out information about what they can do to reduce their carbon footprint. In a similar manner, social media and the *Carbon Neutral News*, the Program's quarterly e-newsletter sent to all existing customers, provide a high degree of transparency into the Program and into the projects in which the funds are invested. Finally, in order to fulfill PG&E's commitment to provide collateral and merchandising materials to its existing customers, some budget for these items must be provided.

It should be noted in regards to the online and social media specifically, that shutting down and later re-launching this infrastructure if the Commission subsequently grants PG&E's requested two-year extension would require more funds than would be required to do basic maintenance of the site. Shutting down these operations and then later restarting them at potentially a higher cost would be an inefficient use of ratepayer funds. As the day to day extension occurs during a period when customers are most likely to seek information given the substantial required customer communications in the first quarter, it is fundamental that the communication infrastructure be available to provide needed transparency, and to inform customers as to the impact that their contributions have made to the environment and the future direction of the Program.

Maintaining this marketing-related communication infrastructure will require minimal funds totaling $18,600 for the three-month period, or $6,200 per month.

The total request for essential administration, compliance and marketing-related activities would be $161,100 for the three month period, or $53,700 per month.

B. Essential Greenhouse Gas Reduction Project Costs

PG&E anticipates spending $38,000 per month (1.4 FTE) in the interim period on its GHG emission reduction procurement and management activities, specifically for labor costs, legal counsel, and costs of administering the ClimateSmart™ Charity. As described more fully below, this maintenance level of funding during the interim period is necessary for PG&E to fulfill its commitment to be in contract for 1.5 million short tons of emission reductions, manage existing contracts to ensure that PG&E's ClimateSmart™ customers receive the purchased tons, and maintain its other essential commitments to the procurement process such as the administration of the Charity and engagement with the ClimateSmart™ Program's External Advisory Group.

1. Contracting for Emission Reductions – 75% (1.1 FTE)

PG&E has now entered into contracts to purchase GHG emission reductions from six different projects. These contracts represent the largest investments in verifiable GHG emission reductions in California following the stringent verification protocols of the Climate Action Reserve. To date, PG&E's ClimateSmart Program has contracted for 1,168,338 short tons of emission reductions. However, to meet our performance obligation to be in contract for 1.5 million short tons, the ClimateSmart™ Program still needs to contract for another 331,662 short tons.

In order to fulfill this obligation, the ClimateSmart™ Program needs to continue extensive negotiations that are underway with shortlisted bidders from the fourth request for proposals (RFP), and begin negotiations with shortlisted bidders from the recently concluded fifth RFP. Having undertaken negotiations now for nearly two and a half years, the ClimateSmart™ Program has realized efficiencies along the way which result in cost savings going forward. While every effort is taken to minimize legal costs, legal fees are also necessary in order to finalize these contracts.

As there are not enough projects in the pipeline to yield all of the remaining 331,662 tons, ClimateSmart™ Program staff will also need to launch a sixth RFP in the interim period (first quarter of 2010) in order to secure the outstanding volume of GHG emission reductions. Efforts will include conducting targeted outreach to potential bidders, hosting a bidder's information session, interviewing potential bidders, hosting a bidder workshop, and selecting shortlisted bidders.

The ClimateSmart™ Program has found that the procurement process requires a considerable lead time to move from encouraging prospective bidders to submit proposals to signing a contract. Because of the groundbreaking nature of the voluntary carbon market, a significant amount of time is required to educate counterparties on the requirements of the Climate Action Reserve, the ClimateSmart™ Program, and the basics of GHG emission reductions, such as leakage, additionality, and permanence. In addition, negotiations have been slowed by the struggles many of our counterparties face in securing financing during these difficult economic times. Postponing negotiations would put current negotiations at risk, particularly as counterparties may find other interested buyers or lose their ability to obtain financing.

Also, the ClimateSmart^{TM} Program staff's procurement expertise is hard to find and may get recruited by others should there be a lapse in procurement. If the ClimateSmart^{TM} Program's current negotiations fail because of a postponement during the interim period, finding new projects will require additional resources and will be an inefficient use of ratepayer dollars. Furthermore, the closer we get to implementation of a mandatory carbon cap-and-trade system in 2012 as required by the Global Warming Solutions Act of 2006 (commonly referred to as AB 32), the more likely counterparties are to either raise prices considerably or drop out of the voluntary market and wait to sell into the anticipated compliance market for offsets. Halting negotiations during the interim period would have a cascading effect in delaying procurement that could prevent the ClimateSmart Program from being able to secure the remaining tons at all.

2. Managing Existing Contracts for Emission Reductions – 15% (0.2 FTE)

Funds are also needed for contract management efforts during the interim period. Once contracts are signed, we must ensure that our contract partners fulfill their obligations to the ClimateSmart^{TM} Program and meet milestones in a timely manner. Most of these milestones arise in the near term after a contract is executed. For example, a project owner is required to undertake regular reporting and meetings with Program staff until its project is operational.

The ClimateSmart^{TM} Program must also ensure that construction is started on-time and that the project is progressing to operation in order to avoid delays that may cause the project to be inoperable. Often there are hurdles with the Climate Action Reserve or local permitting issues that Program staff expertise is needed to resolve.

Given Program staff's extensive knowledge of the project protocols, contacts, and experience in the voluntary carbon market generally, experts from the ClimateSmart Program are often in a better position than new project developers to help overcome the hurdles they may face from regulatory bodies. The ClimateSmart^{TM} Program has signed three new contracts in 2009; therefore, a significant portion of Program staff's time in early 2010 will be devoted to working with the ClimateSmart™ Program's new contract partners to ensure that their projects get off the ground successfully.

3. Procurement Management Activities – 10% (0.1 FTE)

Finally, the ClimateSmart™ Program has other important ongoing commitments to its customers that should be funded in the interim period as well. The procurement efforts of the ClimateSmart™ Program provide a continuing benefit to the state of California and its residents as the Program is helping to develop the infrastructure for a carbon market in the state through engaging with the Climate Action Reserve's protocol development process, developing the tools, such as a standard form contract, and "road testing" the processes of the Reserve through the registration and retirement of GHG emission reductions.

At the CPUC's request, the ClimateSmart™ Program created the ClimateSmart™ Charity, and the Program has ongoing costs associated with its administration that will remain constant during the interim period. This includes providing an annual letter to Program participants with the amount they may be able to deduct on their taxes.

The Program also regularly convenes the ClimateSmart™ External Advisory Group (EAG), a group of diverse stakeholders that make up a core part of the transparency of the ClimateSmart™ Program. Among other things, the EAG provides key feedback on the selection of the highest quality projects in the ClimateSmart™ Program. The Program plans to convene the EAG during the interim period to provide feedback on the bids received by the Program in the sixth RFP.

The total request for these greenhouse gas reduction costs is $114,000 for the three month period, or $38,000 per month.

The total of all costs for essential administrative, compliance, customer communications, and greenhouse gas reduction projects costs are summarized in Table 1 below.

Table 1: Total Required Monthly Costs

Description	Amount
Administrative costs	$47,500 per month
Marketing “infrastructure” costs	$6,200 per month
GHG reduction procurement and contract management costs	$38,000 per month
Total Monthly Budget	$91,700 per month

IV. IF THE COMMISSION DETERMINES THAT A CAP ON ADMINISTRATIVE EXPENSES SHOULD BE ESTABLISHED BASED ON THE RATIO OF APPROVED ADMINISTRATIVE EXPENSES TO THE OVERALL ADMINISTRATIVE AND MARKETING BUDGET, THE PD’S CALCULATION SHOULD BE REVISED TO CORRECT A CALCULATIONAL ERROR

The PD proposes a cap on administrative expenses of $20,000 per month by calculating a ratio of the approved Administrative budget to the total authorized Administrative and Marketing budget of $16.26 million. By applying this ratio to $1.6M which was the reported A&M balance as of March 31, 2009, the PD calculated that approximately $480,000 of the unspent funds should be available for administrative expenses. If this amount were allocated evenly over the two year extension period, this would equate to approximately $20,000 per month, which the PD proposes be adopted as a cap on PG&E’s administrative expenses during the interim period.

Although PG&E disagrees with this approach, nonetheless PG&E believes that the PD contains a calculational error, because the total amount of unspent funds at the end of 2009 is projected to be $4..078 million and not $1.6 million as stated in the PD. The PD errs in applying a ratio to an incorrect amount of available unspent funds and then dividing this amount over the two year extension period. If the calculational error is corrected, the correct monthly expense cap would be $51,000 per month, not $20,000 per month.

In addition, as discussed in Section II, above, pro-rating the twenty-four month total expenses to determine an interim budget for three months is arbitrary and is not reflective of the budget necessary to operate the Program. Nor does the formula reflect the higher material costs that normally occur in the first quarter to meet regulatory reporting requirements.

PG&E's data request responses in this proceeding are a more accurate reflection of reasonable funding needs during the day-to-day extension period. As directed by the ALJ's ruling (p. 13), PG&E provided a copy of all responses to TURN's data requests as part of the Pre-workshop Statement filed on October 13, 2009. As noted in PG&E's response to TURN's data request on the use of unspent funds during the two year extension period, PG&E prepared a forecast of administrative and marketing funds required to operate the Program. Given that no additional ratepayer funding was requested during the two year extension period, the total approved funds would be expended over a five year period if PG&E's extension request is granted. (See PreWorkshop Statement/TURN's data request 1, Q-5).

These budget forecasts utilize a combination of past Program operating experience and included necessary material costs. If the Commission deems it necessary to follow a ratio approach to derive a budget during the day to day extension period, it should use the proposed administrative and marketing forecast for the first year of the proposed extension period as this forecast represents a reasonable forecast of expected expenditures necessary to operate the Program under the performance guarantee. This forecast can be adjusted to remove estimated one-time material expenses from the administrative budget that occur in the first quarter as a result of annual reporting requirements in order to derive a monthly budget.

Under this scenario, a proposed monthly budget would be calculated as follows. Year 1 administrative costs are projected to be $918,000. If one-time material costs of $36,000 are first removed from this calculation, the resulting Year 1 budget is $882,000 before dividing by 12. Pro-rating by month yields a proposed monthly administrative budget of $73,500 plus material costs of $36,000 (or $12,000 per month) during the day-to-day extension period. Adding to this the $6,200 per month required for marketing infrastructure effectively provides the same result as under our "bottoms up" approach: $91,700 per month. In either case, the $918,000 projected to be spent on administration in 2010 represents a reduction of 24% compared to the $1,205,000 spent on administration in 2008.

PG&E does not support the approach of pro-rating total expenses across a twenty-four month period because it believes it is arbitrary and not reflective of the budget necessary to operate the program. Nor does it reflect the higher material costs that normally occur in the first quarter to meet regulatory reporting requirements. PG&E provides these comments in order to ensure that if the Commission uses a pro-rating approach, it corrects what PG&E believes is an inadvertent calculational error in the PD.

V. CONCLUSION

PG&E supports the PD, but requests that the PD be revised to delete the restriction on administrative and marketing expenses during the day-to-day extension period. Continuity of essential activities under the ClimateSmart™ Program, as well as the continued support of PG&E's greenhouse gas reduction activities on behalf of the

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30,000 customers enrolled in the Program, depend upon PG&E receiving the minimal funding needed during this interim period.

Respectfully Submitted,
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By: /s/
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CERTIFICATE OF SERVICE

I hereby certify that I have this day served a copy of **"OPENING COMMENTS OF PACIFIC GAS AND ELECTRIC COMPANY ON PROPOSED DECISION GRANTING DAY-TO-DAY EXTENSION OF CLIMATE SMART PROGRAM"** on the parties listed in the official service list for A.09-05-016 by

- transmitting an e-mail message with the document attached to each party on the official service list providing an email address; or
- by first-class mail, postage prepaid, to each party on the official service list not providing an email address.

Executed on November 10, 2009, at San Francisco, California.

/s/
MARTIE L. WAY

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Last Updated: October 28, 2009

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