BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

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Order Instituting Rulemaking to Examine the Commission's Post-2005 Energy Efficiency Policies, Programs, Evaluation, Measurement and Verification, and Related Issues.	Rulemaking 06-04-010 (Filed April 13, 2006)

APPLICATION FOR REHEARING
OF DECISION 08-12-059

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I. INTRODUCTION

On January 2, 2009, the Commission issued Decision (D.) 08-12-059, "Decision Granting in Part and Denying in Part the Petition for Modification" (Decision). The Decision modified D.07-09-043 and D.08-01-042 by authorizing incentive payments to Pacific Gas and Electric Company (PG&E), Southern California Edison Company (SCE), San Diego Gas & Electric Company (SDG&E) and Southern California Gas Company (SoCalGas)[1] for energy efficiency savings based not on Energy Division's independent verification of those savings, but instead on the Utilities' self-reported energy savings. The Decision is therefore a radical departure from previous decisions that awarded incentives only for verified achievements.[2]

In approving payment of $82 million in <u>non-refundable</u> energy efficiency incentives to the Utilities, notwithstanding the Energy Decision's draft Verification Report showing that three of the four Utilities were not entitled to incentives, the Commission disregarded its obligation to ensure that rates are just and reasonable and failed to follow its own standard for granting the relief requested in a Petition for

[1] DRA and TURN's Application for Rehearing refers to PG&E, SCE, SDG&E and SoCalGas as "Utilities."

[2] The Commission previously allowed Utilities to earn incentives for verified achievements, paid out over nine years as part of "Annual Earnings Assessment Proceedings." *See e.g.* D.06-09-038.

Modification. The Commission rushed to issue the Decision by the end of 2008 so that utility shareholders could reap profits from unverified savings despite the great body of evidence that suggests that the Utilities should earn nothing or next to nothing in incentive payments. The Decision was not supported by the findings of fact and conclusions of law necessary to support the $82 million award. For these reasons, the Decision represents an abuse of the Commission's discretion, and the Commission should grant rehearing and reverse the award of incentives.

Pursuant to Rule 16.3 of the Commission's Rules of Practice and Procedure, the Division of Ratepayer Advocates (DRA) and The Utility Reform Network (TURN) respectfully submit this Application for Rehearing. This Application for Rehearing is timely filed within 30 days of the date of the Decision's issuance.

II. BACKGROUND

A. Decision 07-09-043, as modified by Decision 08-01-042 aligned shareholder and ratepayer interests by directing the calculation of interim claims using the best *ex ante* data available, including the 2008 database for energy efficiency resource (DEER)[3] updates.

Recognizing the importance of energy efficiency as the least cost resource for serving California's energy needs and as an important tool to combat climate change,[4] the Commission designed the risk/reward incentive mechanism to encourage the Utilities to "'mine deeper' for cost-effective energy savings than ever before in California's history."[5] Decision 07-09-043 therefore established a shareholder incentive mechanism that attempted to align shareholder and ratepayer interests by (1) rewarding the Utilities for energy savings that approached or surpassed the Commission's energy savings goals and (2) by requiring the Commission's Energy Division staff and its evaluation,

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[3] DEER is a database developed jointed by the Commission and the California Energy Commission and funded by ratepayers that provides standardized energy saving parameters, including unit energy savings for various energy efficiency measures. D.08-01.042, p. 16.

[4] D.07-09-043.

[5] D.07-09-043, p. 11.

measurement and verification (EV&V) contractors to independently verify all calculations of the net benefits and kilowatt (kW), kilowatt hour (kWh) and therm achievements using adopted EM&V protocols.[6]

Decision 07-09-043 adopted a risk/reward incentive mechanism that included a minimum performance standard (MPS) of 80-85% of the Commission's energy savings goals. Requiring that Utilities meet the MPS in order to earn incentives ensures that the Utilities are rewarded only for significant progress toward the Commission's goals of saving kW, kWh and therms.[7]

In order to provide timely feedback to the Utilities for their performance in achieving energy efficiency savings, the risk/reward incentive mechanism included two interim incentive payouts based on energy savings achieved before the end of the three-year program cycle.[8] The Commission adopted an earnings claim and recovery schedule in which the two interim claims would be based on Energy Division's Verification Reports reflecting measure installations and costs, followed by a final "true-up" claim that would include Energy Division's *ex post* evaluation of energy savings, consistent with established EM&V protocols. The final true-up process would help ensure that energy efficiency produced "sizable GWh [gigawatt hour], MW [megawatt], and Mtherm [megatherm] savings that resource planners can depend upon now and in the future"[9] and that ratepayers pay incentives only for savings that were real and verified.

The ink was barely dry on D.07-09-043 before the Utilities filed their first petition for modification on October 31, 2007,[10] which sought to restrict the final true-up process

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[6] D.07-09-043, p. 4.

[7] The Commission established the Utilities' energy savings goals in D.04-09-060. The Utilities submitted energy efficiency portfolio plans, including budgets that they proposed in order to meet their energy savings goals, which the Commission approved in D.05-09-043.

[8] *See* D.07-09-043, Conclusion of Law 7, at p. 212.

[9] D.07-09-043, p. 119.

[10] Petition for Modification of Decision 07-09-043 By Pacific Gas And Electric Company, Southern California Edison Company, San Diego Gas & Electric Company And Southern California Gas Company, filed October 31, 2007 and amended November 7, 2007 (First PFM).

so that achievement of the MPS would be based on verification of measure installations, but using *ex ante* planning estimates of load impacts.[11] The Utilities requested that if final verified energy savings showed that their performance fell in the "dead band," between 65% and 85% of the Commission's adopted savings goals, they should nevertheless retain interim incentives and continue earning at the established share rate of 9%. The Utilities claimed that their requested changes were necessary in order to provide sufficient certainty to investors that energy efficiency earnings could be booked "on a regular basis for accounting purposes in a manner that can be expected and anticipated by the investment community" so that energy efficiency resources would be "on par with generation resources in the minds of investors"[12]

The Commission was persuaded that effectiveness of the incentive mechanism would be diluted if the Utilities could not book authorized earnings because of uncertainty associated with the possibility that the final true-up might require the return of incentive payments.[13] It therefore granted the Utilities' first Petition for Modification (First PFM) and modified the incentive mechanism to limit the final true-up process so that

> "if a utility meets the MPS for the interim claim based on verified measure installations and costs, and the *ex ante* savings assumptions, but falls within the 65 to 85% of energy savings goals as a result of the final *ex post* true-up of load impacts…the utility will continue to earn at the 9% shared savings rate, applied to the ex post PEB. In addition, as long as a utility continues to exceed the 65% of savings goal threshold for each individual metric on an *ex post* basis, it will not be required to pay back any interim incentives payments earned."[14]

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[11] D.08-01-042, p. 4.

[12] D.08-01-042, p. 9, quoting First PFM at p.13.

[13] D.08-01-042, p. 10.

[14] D.08-01-042, Ordering Paragraph 2, page 25.

The Commission also incorporated important changes designed to mitigate the risk of large swings in earnings and decrease the risk of overpayment, including "[u]pdating *ex ante* load impacts using the DEER database prior to payout of interim claims in 2008 and 2009"[15] and requiring that 35% of the interim payment be held back.[16] While restricting the final true-up decreased "the incentive for utility managers and staff to support the most accurate estimate of energy savings" and worked against the interest of ratepayers in "shar[ing] the net benefits with shareholders at precisely the adopted share rate,"[17] use of updated DEER numbers to calculate interim claims and increasing the hold back offered decreased the possibility that shareholders would retain incentives for mediocre performance. The Commission explained in response to the first PFM that "[a] combination of updated *ex ante* values combined with a larger hold-back will substantially mitigate ratepayer risk brought upon by the changes we adopt to the true-up mechanism."[18]

B. Decision 07-09-043 recognized the possibility of delay in the calculation of interim incentive claims.

Prior to establishing the procedure for the payment of interim claims in D.07-09-043, the Commission considered parties' proposals and consulted with Energy Division in order to develop an interim claims schedule that would "link claims and payments to EM&V results, produce a stream of earnings during and at the end of the program to provide ongoing incentives to the utilities" while also recognizing resource limitations and competing priorities of staff time.[19] The Commission's adopted proposal[20] provided for "two interim claims and a final true-up claim, resulting in one claim per calendar year for the 2006-2008 and each subsequent program cycle, beginning

[15] D.08-01-042, Finding of Fact 15, p. 21.

[16] D.08-01-042, Finding of Fact 13, p. 21

[17] D.08-01-042, Ordering Paragraph 2, at p. 27.

[18] D.08-01-042, Finding of Fact 11, p. 20.

[19] D.07-09-043, p. 122.

[20] The interims claim proposal was appended to D.07-09-043 as Attachment 6.

in 2008. The interim claims were tied to interim Verification Reports, with the final claim tied to the Final Verification and True-Up report. The Commission adopted an Advice Letter process for the submittal of claims, with "approximate dates of those submittals"[21] reflected in the proposal, but explicitly recognized that the actual due dates for claims depended on the issuance date of Energy Division's reports. While D.07-09-043 observed that Energy Division staff is "fully committed to meeting the deadlines" for producing reports, the Commission acknowledged that "no one can guarantee that unforeseen circumstances will never require delay to that schedule."[22]

The Commission considered but rejected the suggestion that the Utilities be allowed to submit estimated earnings claims and receive interim payments based on estimated savings in the event of a delay in the Energy Division Reports, observing "Ratepayers' interest are best served when the payout of earnings (or imposition of penalties occurs only after the installations, program costs and (for the final claim) load impacts have been verified by our staff and its contractors."[23]

C. The evaluation, measurement and verification process encountered delays, but the initial results show that the Utilities' performance entitles only one of the four Utilities to incentives.

The EM&V process of measuring energy saved by the Utilities' 2006-2008 portfolios encountered delays related to contracts[24] and in at least one documented instance, because of the Utilities' slow responses to staff data requests.[25] Moreover, in granting the Utilities' request to restrict the final true-up of energy savings, D.08-01-042

[21] D.07-09-043, p. 122 (emphasis added).

[22] D.07-09-043, p. 122.

[23] D.07-09-043, p. 123.

[24] *See* Administrative Law Judge's Ruling Revising Protocols for Process and Review of Post-2005 Evaluation, Measurement and Verification (EM&V) Activities, and Addressing Next Steps for Finalizing The Annual Reporting Requirement, January 2, 2007 (describing delays due to contracting issues).

[25] *See e.g.,* July 8, 2008 letter from Paul Clanon to Kayode Kajopaiye granting the request for extension of time to issue 2007 energy efficiency audit reports pursuant to D.05-11-011 (extension requested because of delays in getting data request responses, as well as planned time-off of assigned staff.)

changed the interim claim process and required the use of 2008 DEER data for the first interim claim. This significantly increased the complexity of preparing the first Verification Report.

On November 18, 2008, rather than in August as originally planned, the Energy Division issued its "Energy Efficiency 2006-2007 Verification Report, Review Draft" (Draft Verification Report).[26] The Draft Verification Report showed that SoCalGas would earn a 2008 interim incentive payment of $3.6 million, PG&E and SDG&E's performance would fall in the dead band and would therefore not entitle them to interim incentive payments, and SCE 's performance would require payment of a $6.9 million penalty.[27]

The Energy Division's Draft Verification Report demonstrates that the importance of using independently verified data is not hypothetical: the report shows significant differences between the Utilities' self-reported savings and the savings calculated through the process of independent verification.[28] While the results of the Draft Verification Report may change through the comment process, the Draft Verification Report provides critical analysis that should not have been ignored in the haste to pay incentives in a "timely" manner. This is particularly true when the Draft Verification Report shows that PG&E, SCE, and SDG&E are all very close to the penalty threshold of 65% of goals.[29]

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[26] The Draft Verification Report and accompanying appendices consist of more than 150 pages of detailed analysis explaining the savings parameters used and the rationale for the results.

[27] The Draft Report shows a $17.8 million penalty for SCE, but this was corrected to $6.9 million in a November 19, 2008 erratum.

[28] These differences between the Utilities' self-reported energy savings and the savings verified by the Draft Verification Report interim claims are the result of differences that include the net -to -gross metric, but also expected useful life (EUL), unit energy savings (UES), and installation rates. The Utilities and the Natural Resources Defense Council (NRDC) continue to assail the use of net-to-gross metrics in spite of the importance of this metric in guiding program implementation and in measuring real energy savings impacts. The October 5, 2007 Assigned Commissioner Ruling Addressing Net-to-Gross Ratio True-Up and Methodology for Lighting Programs in the 2006-2008 Energy Efficiency Portfolios (October 5, 2007 ACR) explained the history and importance of the net-to-gross adjustment for improving programs.

[29] Draft Verification Report, Table 26, p. 65: SCE, 64%; PG&E, 65%, SDG&E, 67%.

Energy Division's Final Verification Report was scheduled for release on January 15, 2009, but the release of the report was delayed at the request of the Energy Division's new director.[30]

D. The Second PFM

In response to the delays in the process for calculating their interim incentives, the Utilities filed a Second PFM that sought the following relief:

- Immediate payment of interim incentives for 2006-2007 totaling $152.7 million, net of 35% holdback ($235 million before holdback).[31]
- Calculation of interim incentives payments based on self-reported measure savings and cost estimates in the event that Energy Division's EM&V reports are delayed; [32]
- Removal of the requirement that interim earnings claims be based on updated DEER estimates;[33] and
- The opportunity for Commission review earnings-related issues raised in evaluation, measurement, and verification reports, outside of the current advice letter process.[34]

The Utilities claimed in their Second PFM that the delay in the Verification Report would prevent the Utilities from booking incentive earnings in a timely manner. Their claim for $152 million in incentives assumed that that the Commission granted their request to calculate interim claims without using updated DEER values, in contravention of D.08-01-042's directive to use the most current energy savings parameters.

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[30] The letter explained that "Energy Division staff have completed the completed the work to finalize the report and resolution in time to issue it today, January 15, 2009 as required by the decision," but requested additional time for the new Energy Division Director to review and understand "the highly complex underlying analysis." January 15, 2009 letter from Julie Fitch to Paul Clanon. The Executive Director granted the request, even though it was not made at least not made at least three business days, for a delay was before the deadline, as required by Rule 16.6 of the Commission's Rules of Practice and Procedure.

[31] Second PFM, p. 6.

[32] Second PFM, pp. 3-4.

[33] Second PFM, p. 4.

[34] Second PFM, p. 4.

E. Decision 08-12-059

The Decision authorized payment of interim incentives of $41.5 million to PG&E; $24.7 million to SCE, $10.8 million to SDG&E and $5.2 million of SoCalGas based on their requests in their Second PFM. While the Decision increased the holdback of interim claims payments from 35% to 65%, if the Utilities are not entitled to incentive payments, then no holdback, short of 100%, would protect ratepayers from the risk of paying non-refundable incentives. Similarly, while the Decision claimed to reinstate the dead band for purposes of conducting the *ex post* true-up for the 2006-2008 program cycle, it only provides that no "additional" incentives will be awarded.[35] Since this decision did not otherwise change the non-refundability of incentive overpayments, it did not truly reinstate the deadband as established by D.07-09-043. Thus, it remains true that "payment of awards to utility shareholders for incentive-based savings is a one-way street."[36]

III. STANDARD OF REVIEW

Rule 16.1(c) requires an applicant for rehearing to "set forth specifically the grounds on which the applicant considers the order or decision of the Commission to be unlawful or erroneous," making specific references to the record or law. Section 1705 of the Public Utilities Code requires Commission decisions to be based on "findings of fact and conclusions of law on all issues material to the order or decision." When a reviewing court examines the validity of a Commission decision pursuant to Section 1757 of the Public Utilities Code, it determines whether the decision is supported by the findings and whether the findings in the decision are supported by "substantial evidence in light of the whole record."[37] The reviewing court also examines, among other things, whether the

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[35] D.07-09-043, Ordering Paragraph 4, p.28.

[36] D.08-12-059, dissent, p. DMG-2.

[37] Public Utilities Code §§ 1757(a)(3)-(4). Section 1756 of the Public Utilities Code provides that a party may petition for a writ of review in the court of appeal or the Supreme Court so that the court can determine the lawfulness of a Commission order. Section 1757(a) provides that in a complaint or enforcement proceeding, or in a ratemaking or licensing decision of specific application that is addressed to particular parties, the court's review shall is limited to determining whether, on the basis of the entire

(continued on next page)

Commission has proceeded in manner required by law, and whether the decision is an abuse of discretion.

IV. DECISION 08-12-059'S AWARD OF INCENTIVES, WHICH ARE BASED ON UNVERIFIED CLAIMS, RESULTS IN RATES THAT ARE NOT JUST AND REASONABLE.

Section 451 of the Public Utilities Code requires that:

> All charges demanded or received by any public utility, . . . for any product or commodity furnished or to be furnished or any service rendered or to be rendered shall be just and reasonable. Every unjust or unreasonable charge demanded or received for such product or commodity or service is unlawful.

The obligation to ensure just and reasonable rates has been characterized by one customer group as the Commission's "'oldest and most basic responsibility.'"[38] Exercising that responsibility requires that the Commission "assure the public that the prices they pay for electric and gas distribution service are in fact just and reasonable, and reasonably related to costs prudently incurred by efficient, conscientious managers to provide the quality of service we expect."[39] The Decision fails to uphold this obligation.

The Decision approves $82.2 million in incentives, in the face of a Draft Verification Report demonstrating that SoCalGas would be entitled to $3.6 million in incentives, but the other three Utilities would be entitled to nothing. The result could be

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(continued from previous page)
record, whether any of the following errors occurred: "(1) The commission acted without, or in excess of, its powers or jurisdiction. (2) The commission has not proceeded in the manner required by law. (3) The decision of the commission is not supported by the findings. (4) The findings in the decision of the commission are not supported by substantial evidence in light of the whole record. (5) The order or decision of the commission was procured by fraud or was an abuse of discretion. (6) The order or decision of the commission violates any right of the petitioner under the Constitution of the United States or the California Constitution."

[38] D.07-12-052, Appendix C, p. 12 (summarizing intervenor positions on Utilities' Long Term Procurement Plans; the California Large Energy Consumers Association requested that in reviewing the utility procurement plans that the Commission "to keep in mind its oldest and most basic responsibility—that embedded in Public Utilities Code Section 451—which is to assure ratepayers that they pay rates which are just and reasonable, and just and reasonable rates are those based on the cost to serve."

[39] D.04-10-034, p.6.

an overpayment of more than $78 million, most of which could never be recovered even if the Final Verification Report continues to demonstrate that the Utilities are entitled to less than $78 million. As the dissenting opinion aptly observes:

> There is no justification in the record to conclude that a payout of this magnitude, which is not subject to refund upon completion of the final staff analysis, protects ratepayers from overpayment.[40]

The Decision observes that the Utilities seek relief because "there are serious questions concerning the validity of *ex ante* assumptions used to validate the [Utilities'] claims."[41] The existence of "serious questions" about the calculation of the claim weighs in favor of resolving those questions, rather than rushing to pay incentives based on disputed assumptions.

The Utilities have extensively criticized the Draft Verification Report.[42] It is likely that the final results will change, although the magnitude and direction of those changes are currently unknown. Even though not yet final, the Draft Verification Report is the most comprehensive and unbiased analysis of the Utilities' claimed energy savings. Ignoring the results and paying incentives that may exceed the Utilities' actual entitlement flies in the face of the obligation to ensure that rates are just and reasonable. This is especially true when the only evidence that supports incentive payments is the Utilities' self-reported savings, and NRDC's "analysis," both of which fail to comply with the Commission's directive to use updated *ex ante* energy savings parameters for calculating the interim claims.

The Commission recognized in D.08-09-038 that including incentive payments in rates when the utility failed to meet the performance targets of the incentive mechanism at issue resulted in rates that were unjust and unreasonable.[43] Although the circumstances

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[40] D.08-12-059, dissent, p. DMG 2.

[41] D.08-12-059, Ordering Paragraph 1, p.27.

[42] *See e.g. ex parte* notices filed in this proceeding by the Utilities in November and December 2008.

[43] D.08-09-038, p. 98.

of that case involved the utility's knowledge that the performance targets had not been achieved, the rationale applies with equal force here: rates that include awards for goals that have not been met are not just and reasonable.

V. DECISION 08-12-059 FAILS TO PROVIDE A RATIONAL BASIS FOR ITS AWARD OF $82.2 MILLION IN INCENTIVES BASED ON UNVERIFIED SELF-REPORTS.

Pursuant to Public Utilities Code Sections 1705 and 1757(a)(4), the Commission must base its decisions on findings of fact and conclusions of law on all issues material to the order or decision, and the findings must be supported by substantial evidence in light of the whole record. The substantial evidence test not only requires an agency to base its decisions on solid evidence in light of the whole record, but also to explain the basis for its decisions.[44] In *McBail & Co. v. Solano County Local Agency Formation Commission*, the Court of Appeal held that an agency's failure to provide an explanation of the basis for its decision is a "fundamental error:"

> We hold that in order for the trial court to intelligently evaluate whether substantial evidence supports the decision to deny the petition, LAFCO must first articulate the basis or reason for that decision. This is so because evidence does not relate to a decision in the abstract, but must be connected to the basis or reason for that decision. Because the court cannot apply the substantial evidence test in a vacuum, logic and reason dictate that for purposes of meaningful review the administrative agency must state its reason for a decision in order to provide the framework within which the reviewing court can apply the substantial evidence test.[45]

The court further held, "Without the benefit of an agency's reasoning, the court has nothing against which to weigh the substantiality of the evidence."[46]

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[44] Public Utilities Code Section 1757(a)(4); *McBail & Co. v. Solano Co. Local Agency Formation Comm'n*, 62 Cal. App. 4th 1223, 1227 (1998).

[45] Mc*Bail*, 62 Cal. App. 4th at 1227.

[46] *McBail*, 62 Cal. App. 4th at 1230, citing *California Hotel & Motel Ass'n v. Industrial Welfare Comm'n*, 25 Cal. 3d 200, 222 (1979)(conc. op.).

This requirement goes beyond the Commission's obligations under Section 1705 of the Public Utilities Code to make findings on all material issues. The Commission must "do more than simply state ultimate factual conclusions."[47] It must explicitly weigh the relevant evidence. A detailed evaluation of every piece of evidence or testimony is not required, but the agency "must articulate, at some minimal level, its analysis of the evidence."[48]

Prior to issuance of D.08-12-059, the Commission firmly adhered to independent verification of net benefits, kW, kWh and therm achievements as a threshold feature of a "risk reward mechanism" that encourages real energy savings. Yet in the interest of "timeliness," the Decision used the Utilities' self-reported and unverified energy savings as the basis for interim incentives payments, despite the independent Draft Verification Report that showed three of the four Utilities failed to achieve the Commission's energy savings goals and were therefore not entitled to incentives. Such a fundamental change from past decisions requires findings of fact supported by the record on every material issue, with a rational explanation for the basis of the findings. Instead, some of the Decision's findings fail to support the award, while findings that would justify the Decision's radical departure from past policy are lacking. In short, the Decision lacks the reasoned decision making required of administrative agencies by reviewing courts.

A. Decision 08-12-059 fails to offer adequate support based on substantial evidence for its finding that "[r]egular and timely issuance of incentive payments is critical to the ability of the RRIM in creating a meaningful linkage

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[47] *Stewart v. Secretary of Health, Education, and Welfare of the United States*, 714 F.2d 287, 290 (3rd Cir.1983); *California Manufacturers Ass'n v. Public Utilities Commission*, 24 Cal. 3d 251, 258-259 (1979) (Supreme Court annulled decision where the Commission failed to show that the adopted rate design was more likely than other rate designs to encourage conservation.)

[48] *Green v. Shalala*, 51 F.3d 96, 101 (7th Cr. 1995); *see also Motor Vehicle Mfrs. Ass'n v. State Farm Mut. Auto. Ins. Co.,* 463 U.S. 29, 43, (1983) (quoting *Burlington Truck Lines, Inc. v. United States,* 371 U.S. 156, 168, (1962) (agency must "examine the relevant data and articulate a satisfactory explanation for its action including a 'rational connection between the facts found and the choice made'" to avoid making an arbitrary and capricious determination.)

between utility investments in energy efficiency and utility earnings."[49]

Decision 07-09-043 recognized "that an effective incentive mechanism must include provisions for earnings (or penalties) at interim points during the three-year program cycle, as opposed to waiting nearly five years after portfolio implementation for any financial feedback to utility managers and investors."[50] Decision 08-01-042 similarly acknowledged the importance of providing "effective feedback to utility managers and investors, a risk/reward incentive mechanism for energy efficiency" by including "provisions for earnings (or penalties) at interim points during the three-year program cycle."[51] Nevertheless, the Commission recognized the possibility of a delay in the process for verifying interim incentive claims, given the importance of verifying claims.

There is no guarantee that Energy Division's schedule for completing EM&V reports will never be delayed, based on unforeseen circumstances. However, ratepayer interests are best served if the payout of earnings (or imposition of penalties) occurs only after the installations, program costs and (for the final claim) load impacts have been verified by Commission staff and its contractors.[52]

Yet the Decision, issued less than a year after the prior decision modifying the incentive mechanism, now ascribes paramount importance to "timely" payment of incentives, even if those incentives have not been verified. This finding is not supported by substantial evidence. The Utilities claimed in their Second PFM that in order to make energy efficiency a regular part of the Utilities' business, the shareholder incentive mechanism must produce predictable, regular, and systematic earnings which can be reported to Wall Street, but presented no evidence that a delay of several months in the first interim incentive payments would harm their shareholders or their energy efficiency

[49] D.08-12-059, Finding of Fact 3, p. 25.

[50] D.08-01-042, citing D.07-09-043 Conclusion of Law 7, at p. 212.

[51] D.08-10-042, Finding of Fact 1, at p. 19.

[52] D.07-09-043, Finding of Fact 118, at p. 201.

programs.[53] The record is therefore devoid of factual information demonstrating that a short delay in payment of the first interim earnings would significantly impact stock prices, dividends, and credit ratings. In contrast, DRA, TURN and CE Council explained that based on economic fundamentals, a one-time delay of two to three months in the 2008 interim claim would produce only a minor impact on the value of shareholder incentives.[54]

In fact, as DRA, TURN, and CEC pointed out in their response to the Second PFM, Wall Street was well aware of the potential for delay in the payment of incentives because the Securities Exchange Commission (SEC) filings of the four Utilities disclosed the potential for delays,[55] yet the Utilities produced no evidence that such a delay was problematic to investors. In contrast, the First PFM cited reports by CitiGroup and Lehman Brothers expressing concerns about the impact of unrestricted true-up on the effectiveness of the shareholder incentive mechanism adopted in D.07-09-043.[56]

B. Decision 08-12-059's finding that "NRDC offers an analysis that it believes shows that the interim claim amounts sought by PG&E, SCE, and SDG&E, SoCalGas are reasonably conservative and, thus, combined with the existing holdback provisions are unlikely to result in overpayment"[57] does not support the incentive award.

The Natural Resources Defense Council (NRDC) filed a Response to Utilities' Second PFM in which it supported a "timely decision" resolving the Utilities' incentive

[53] Second PFM, p. 2. The Utilities claimed that they needed to book earnings with certainty by the end of 2008. Yet the Decision is subject to applications for rehearing filed no later than February 2, 2009, and then to potential judicial review. Public Utilities Code Section 1756. Thus, while the Utilities sought a decision that would allow them to book earnings in 2008 without the threat of ultimate claw back, the Decision does not accomplish that goal.

[54] DRA/TURN/CE Council Response to Second PFM, p. 17, n.55.

[55] *See e.g.* DRA/TURN/CE Council Response to Second PFM at pp. 15-16 (noting for example, that SCE 10-K report dated February 27, 2008 pointed out the linkage between the timing of the reports and the timing of any interim earnings: "Timing of progress payment claims is linked to the completion of CPUC reports. Delays in CPUC reports could cause delays in recognizing earnings for these claims."

[56] First PFM, p. 2.

[57] D.08-12-059, Finding of Fact 8, p. 25.

claims.[58] NRDC claimed that energy savings estimates for PG&E, SCE and SoCalGas "are based on reasonable and conservative assumptions."[59] The analytical framework for NRDC's belief that the energy savings estimates are "reasonable and conservative" was summarized in a single table on page 5 of its response. NRDC admitted that its conclusion that the Utilities' energy savings estimates represented "robust lower bounds for the final total incentive payment entitlement" required "setting aside" net-to-gross ratio adjustments, in direct contravention of Commission's directive in D.08-01-042 to calculate interim claims with updated *ex ante* estimates, including the net-to-gross ratio.[60] NRDC's support of the Utilities claims hinges on a change to the incentive mechanism, which it explicitly requested in their September 15, 2008 comments, yet this critical detail is not reflected in the Decision.

DRA also raised questions regarding the nature of NRDC's analysis, and to what it extent it relied on calculations provided by the Utilities, and whether it was truly an independent analysis.[61] While a series of letters was circulated to the service list debating this issue, this information in not a part of the record in this proceeding. DRA's concern regarding NRDC's analysis was never vetted, and is not addressed in the Decision.

DRA, TURN and CE Council presented their own analysis of the Utilities' energy savings claims.[62] DRA explained that because the Second PFM requested payment of $152 million dollars on a single sheet of figures with no description of methodology, illustrative formulas, or citations of data sources, it requested supporting information from the Utilities. SCE, PG&E, and SDG&E responded sufficiently in advance of the deadline for filing the response to the PFM to allow review of whether the Utilities'

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[58] NRDC Response to The Petition for Modification of Decisions 07-09-043 And 08-01-042, filed September 15, 2008 (NRDC Response to Second PFM), p. 2.

[59] NRDC Response to Second PFM, p. 3.

[60] NRDC Response to Second PFM, pp. 5-6,

[61] DRA/TURN Response to PD on Second PFM, dated November 24, 2008, p. 6, footnote 17; *see also* Prehearing Conference Transcript October 3, 2008, 224:225:23.

[62] DRA/TURN/CE Council Response to Second PFM, pp. 15-17 and in Appendix A.

claimed energy achievements could be traced back to previously reported data sources and required reports; whether the claims accurately reflected the energy savings goals of D.04-09-060; and whether they accurately applied the rules adopted in D.07-09-043 and the Commission's energy efficiency Policy Rules.[63] DRA made no attempt to verify the accuracy of data in the underlying E3 calculators, which are the basis of calculating the interim incentive claims.[64] DRA's limited review revealed inconsistencies between the Utilities' claims in their Second Petition and the performance presented in their fourth quarter 2007 reports, that underscored the importance of "independently verifying the accuracy of measure installation, savings assumptions, and all program costs on which incentives are based."[65]

TURN estimated what the interim claims would be if the Utilities had complied with the Commission's directive to use updated DEER numbers for calculating their interim claims. Using available data, DRA and TURN completed a rough calculation of the impact of adjusting the net-to-gross ratio, unit energy savings, and storage rates for upstream manufacturer buy-down for compact fluorescent light bulbs (CFLs).[66] Adjusting the Utilities interim claims to reflect all the updated DEER values for all measures was not feasible, but the result of the analysis is shown in Table 1 of DRA, TURN, and CE Council's response to the Second PFM. This analysis indicated that the energy savings of PG&E, SCE and SDG&E would fall in the dead band, meaning that the interim incentive claims would be zero.[67] DRA, TURN and CE Council acknowledged

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[63] The most current energy efficiency policy rules were adopted August 6, 2008 pursuant to an "Assigned Commissioner's and Administrative Law Judge's Ruling on Revision 4.0 of the Energy Efficiency Policy Manual" in this proceeding.

[64] A full verification is an enormous undertaking. "There are more than 220 E3 calculators, each of which has from between 1 and 1,000 measures in addition to program costs. Each measure has a user defined installation schedule, kWh savings assumptions (UES, EUL, NTG), therm savings assumptions (UES), load shapes, and other parameters. There are hundreds of thousands of data points to be verified and no automated method of doing so." DRA/TURN/CE Council Response to Second PFM, Appendix A, p. 10.

[65] DRA/TURN/CE Council Response to Second PFM, Appendix A, p. 10.

[66] DRA/TURN/CE Council Response to Second PFM, Appendix A, p. 10.

[67] DRA/TURN/CE Council Response to Second PFM, p. 18.

that their analysis of the incentive claims was not intended to substitute for the Draft Verification Report, but to illustrate the potential risk of paying the Utilities unverified energy claims.

The Energy Division's Draft Verification Report further substantiated the risk of paying unverified incentive claims. The Draft Verification Report showed that while SoCalGas would earn a 2008 interim incentive payment of $3.6 million, PG&E and SDG&E's performance were not entitled to interim incentive payments, and SCE's would be required to pay a $6.9 million penalty.[68]

The finding that "NRDC offers an analysis that it believes shows that the interim claim amounts sought by PG&E, SCE, and SDG&E, SoCalGas are reasonably conservative and, thus, combined with the existing holdback provisions are unlikely to result in overpayment" does not support the incentive award. Without more evidence, NRDC's "belief" does not support the Commission's decision, especially in light of the Decision's failure to consider and make findings on the DRA,TURN and CE Council analysis, or to explain why the Commission found it less persuasive than the analysis offered by NRDC. After all, NRDC's analysis admittedly did not comport with D.08-01-042, which directed the Utilities to use updated DEER numbers for calculating the interim incentive claims. Similarly, the Decision should contain a finding on the Draft Verification Report, and explain why, even though it is only a draft, is less persuasive than the NRDC analysis. Finally, the Decision should contain findings supported by substantial evidence that reflect whether the Utilities have achieved the Commission's energy savings goals.

C. Decision 08-12-059's findings that "[a]ll else equal, imposing a higher holdback amount can help mitigate the risk of incentive overpayment"[69] and "[r]einstating the deadband for purposes of conducting the *ex post* true-up

[68] The Draft Report shows a $17.8 million penalty for SCE, but this was corrected to $6.9 million in a November 19, 2008 erratum.

[69] D.08-12-059, Finding of Fact 10, p.25.

for the 2006-2008 program cycle will further reduce the risk of overpayment t"[70] do not support the incentive award.

The Decision implemented two changes to the incentive mechanism designed to reduce the risk that ratepayers will pay incentives on self-reported, unverified claims that subsequently are found to be unjustified. First, it increased the holdback from 35% to 65%. Second, it offered a limited reinstatement of the dead band for purposes of conducting the *ex post* true-up for the 2006-2008 program cycle. Neither change will eliminate the risk that the Utilities will receive incentives for performance that falls short of the Commission's goals. The Decision does not explain why, in the face of the Draft Staff Report demonstrating that three of the four Utilities are entitled to no incentives, it awards over $78 million to those Utilities, even though the payments are non-refundable. The Draft Staff Report was the second data point, subsequent to TURN's analysis, that indicated that the 65% holdback was insufficient to protect ratepayers from over payment. The Decision's Conclusion of Law 2 therefore errs in stating that the specific 65% holdback is sufficient.

D. Decision 08-12-059 fails to recognize the critical linkage between incentives and energy efficiency achievements.

The Decision contains no finding recognizing the essential linkage between incentives and the verified energy savings that the Commission seeks to achieve. Although California has already removed many disincentives that would prevent the Utilities from pursuing all cost-effective energy efficiency, the Commission took the additional step of adopting a risk/reward incentive mechanism to encourage the Utilities to "'mine deeper' for cost-effective energy savings than ever before in California's history."[71] To date, there is little evidence that the Utilities are in fact "digging deeper"

[70] D.08-12-059, Finding of Fact 11, p.26.

[71] D.07-09-043, p. 11.

for cost effective energy savings or that they are prudently managing the forecasting risk that is inherent in managing energy efficiency portfolios.[72]

During the peer review process of the 2006-2008 portfolios, "several peer review group members, as well as Energy Division consultants, noted that [net-to-gross] values for a variety of strategies were too high."[73] Evaluation, measurement and verification of the Utilities' 2004-2005 portfolios demonstrated that savings from lighting programs was considerably lower than Utilities had estimated when planning their 2006-2008 portfolios. The prudent response to this information should have been to shift program dollars from lighting programs in which the market was transforming to other areas where significant savings still remained. There is little evidence that SDG&E, SCE or PG&E did that during 2006-2008. In fact, their pending 2009-2011 portfolio applications are largely comprised of lighting measures.

The Draft Verification Report's use of updated DEER numbers shows the result of the Utilities' continued reliance on lighting measures: all three electric Utilities fall short of the Commission's goals. While the Draft Verification Report is not yet final, it raises serious questions about whether the Utilities in fact deserve incentives. Providing "timely incentives" to the Utilities even if they have failed to meet the Commission's goals does not advance the Commission's goals of increasing energy savings.

E. Decision 08-12-059 incorrectly states that the payments it authorizes are based on the Utilities' Fourth Quarter Reports and fails to reconcile differences in the Utilities' claims.

The Decision claims that the incentive awards in authorizes are based on the Utilities' Fourth Quarter Reports.[74] As explained Appendix A of DRA/TURN and CE

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[72] ALJ Gottstein noted that "[T]he nature of *ex post* EM&V means that there will be uncertainties facing both ratepayers and shareholders in the deployment of energy efficiency in 2006 and beyond, and managing those uncertainties is part of the energy efficiency portfolio administrator's responsibility." October 5, 2007 ACR, p. 5. (emphasis added.)

[73] October 5, 2007 ACR, p. 3.

[74] D.08-12-059, Conclusion of Law 1, p.26 ("[T]he Commission should authorize interim payments to the IOUs based on their quarterly performance reports…").

Council's Response to the Second PFM, the Utilities' claims in their Second PFM cannot all be reconciled with their Fourth Quarter Reports. Moreover, the Decision's reliance on the Utilities' unverified savings fails to reconcile a fundamental discrepancy in their calculation: the claims of SDG&E and SoCalGas include energy savings from 2004 and 2005, while those of PG&E and SCE do not. There is no rational basis for the Commission to use a different basis for calculating rewards for different Utilities without providing a justification. Accordingly, the Decision errs in awarding payments for SCE and PG&E that are measured one way, while payments for SoCalGas and SDG&E are measured another way.

F. Decision 08-12-059's finding that"[u]pdates to the DEER energy efficiency performance assumptions and the methodologies supporting those updates have been the subject of considerable controversy over the course of this proceeding, particularly with respect to NTG ratios"[75] does not support the award.

The Decision finds that use of updated DEER numbers, especially the net-to-gross ratio, have been controversial throughout this proceeding. While the finding is accurate, it does not support the award of incentives. "Considerable controversy" does not change the fact that the Commission intended that energy savings be measured net of free riders, and that the net-to-gross metric should be updated based on the most recent data.

The Commission established specific energy savings goals for the 2006-08 energy efficiency programs in D.04-0-060. Those goals, which are net of free riders, have not changed.[76] The Utilities' achievement of those goals will be based on *ex post* evaluation of the 2006-08 programs after they have been completed. In September 2005, before the program cycle began, Commission clearly stated "that NTGs will in fact be adjusted (trued-up) on an *ex post* basis when we evaluate actual portfolio performance."[77] These

[75] D.08-12-059, Finding of Fact 12, p. 26,

[76] D.04-09-060, Finding of Fact 15, p.47.

[77] D.05-09-043, p.97.

rules established how performance will ultimately be measured, and they have not been changed since their adoption in 2005.

The Commission revised its policy regarding the true-up of Utility performance prior to the final *ex post* impact evaluation by adopting D.08-01-042, which addressed Utility concerns about certainty and timeliness of interim incentive claims. Among other things, the decision made interim payment non-refundable to protect Utilities from "claw back." However, the Commission also required the calculation of interim claims using updated savings assumption data to "mitigate the risk of extremely large swings in earnings (positive or negative) at the final earnings true-up, which serves the interests of both utility shareholders and ratepayers."[78] D.08-01-042 established that since the ultimate goal is to reward *ex po*st performance, should attempt to approximate those which will apply in the final claim. and since interim overpayments are not refundable, the data used for the interim claims

The finding that the Utilities and NRDC continue to assail the use of updated DEER metrics does not support the incentives award.

VI. THE COMMISSION COMMITTED LEGAL ERROR WHEN IT GRANTED A PETITION FOR MODIFICATION THAT FAILED TO DEMONSTRATE CHANGED CIRCUMSTANCES THAT WOULD JUSTIFY MODIFICATION OF D.07-09-043 OR D.08-01-042.

The Commission committed legal error in D.08-12-059 by granting the relief sought in a petition for modification despite that petition's failure to present evidence that would meet the appropriate "preponderance of the evidence" standard and to support the underlying factual allegations of new or changed facts with an appropriate declaration or affidavit.

Two recent Commission decisions articulated the standard of proof that must be met by a party seeking to modify a decision under Rule 16.4 under circumstances substantially similar to those present here. In D.08-04-057 (addressing the revisions

[78] D.08-01-042, p.17.

AT&T proposed to its Rule 12 tariff), the Commission treated AT&T's Rule 12 Advice Letters as the equivalent of a petition to modify an earlier decision, subject to a petition's standard of proof:

> Consistent with this approach, we placed on AT&T the burden of proving that the marketing controls imposed on AT&T in the Rule 12 Decision were no longer necessary. In keeping with long-standing Commission practice, the standard of proof that AT&T must meet in order to carry its burden is a "preponderance of the evidence." In short, AT&T must show that the evidence supporting its modification of the marketing restrictions imposed in the Rule 12 Decision outweighs the evidence against maintaining all the restrictions in the Rule 12 Decision.[79]

The Commission similarly concluded in D.08-03-009 that "[T]he proponent of the petition for modification . . . bears the burden of demonstrating that our recent decision in this proceeding, D.07-12-020, should be modified."[80]

In D.08-12-059, the Commission fails to point to any evidence that would support granting any part of the utilities' request for relief, much less evidence that meets the "preponderance" standard or that demonstrates a need to modify the recent decision in this proceeding.

The failure to present evidence is highlighted by the petition for modification's failure to comply with Rule 16.4(b) of the Commission's Rules of Practice and Procedure. To the extent there are factual allegations that support the petition, those allegations must either be supported by citations to the record or matters that may be officially noticed, or (if a new or changed fact) by an appropriate declaration or affidavit. The Utilities' request for relief asserted that a delay in the authorization of the first interim earnings claim would undermine the effectiveness of the energy efficiency incentive mechanism. There is no citation to the existing record or matters subject to official notice, nor is there any declaration or affidavit in support of that assertion. The

[79] D.08-04-057, p. 29 [cite omitted]; see also Conclusion of Law 1.

[80] D.08-03-009, p. 3.

only material supporting the request consists of unverified pleadings from the Utilities and NRDC. D.08-12-059 simply ignores the "preponderance of evidence" standard the Commission relied upon in two recent decisions, and glosses over the failure of the Utilities to support their allegations.

A. There Is Inadequate Factual Support In The Record For A Determination That Changed Circumstances Warrant Any of the Modifications D.08-12-059 Made to D.07-09-043 and D.08-01-042.

Decision 07-09-043 adopted an incentive mechanism in which amounts paid as interim claims remained subject to full reconciliation upon the Final Verification and Performance Basis Report.[81] This approach ensured that to the extent the interim payments were, upon final review, more than the Utilities had earned, ratepayers were protected because the final true-up would adjust such overpayments. Yet even with this protection in place, the Commission rejected the proposal to permit payment of interim claims based on the Utilities' estimated savings.[82] Instead, the Commission embraced verification of even interim claims:

> Ratepayers' interests are best served when the payout of earnings (or imposition of penalties) occurs only after the installations, program costs and (for the final claim) load impacts have been verified by our staff and its contractors.[83]

Thus even when overpayment posed less risk to ratepayers because the final claims were ultimately subject to a full and complete reconciliation the Commission required the mechanism to pay earnings based on verified savings, not utility estimates.

In D.08-01-042, the Commission (among other things) eliminated the full and complete reconciliation in the final claim verification so long as the overall performance was not in the penalty band for the incentive mechanism. D.08-12-059 acknowledges the change's impact on ratepayer risk:

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[81] D.07-09-043, pp. 121-124.

[82] D.07-09-043, p. 125.

[83] *Id.*; repeated with slight paraphrasing in Finding of Fact 118.

> Because this decision reduced the share of IOU incentive claims that would be subject to *ex post* review and true-up, all else equal it necessarily increased the risk of incentive overpayment.[84]

The Commission recognized that this increased risk of overpayment also increased the importance of calculating the interim payments as accurately as possible and, by extension, increased the importance of basing incentives on verified claims rather than utility estimates:

> A combination of updated *ex ante* values combined with a larger hold-back will substantially mitigate ratepayer risk brought upon by the changes we adopt to the true-up mechanism.[85]

The Commission therefore specified the *ex ante* assumptions for purposes of calculating the first and second interim claims, in light of the other modifications to D.07-09-043.[86]

In D.08-01-042, the Commission recognized that to maintain any balance of ratepayer and shareholder interests, changes to the incentive mechanism that increase the risk of overpayment must be coupled with more rigorous *ex ante* evaluation of the incentive claims. Unfortunately, D.08-12-059 reversed this approach, and instead elevated payment of incentives by the end of 2008 above the goal of avoiding overpayment without the requisite basis for doing so. It generally weakened (if not abandoned) the reliance on *ex ante* evaluation for those claims.

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[84] D.08-12-059, p. 5.

[85] D.08-01-042, Finding of Fact 11; see also Finding of Fact 13.

[86] D.08-01-042, p. 16 and Findings of Fact 15 and 16.

B. The Commission's "Belief" That Paying Interim Incentives In Early 2009 Rather Than By The End Of 2008 Undermines The Incentive Mechanism Does Not Warrant Introducing The Risk Of Overcharging Ratepayers $82.2 Million.

Immediately after expressing its discomfort with making interim payments on the basis of the Utilities' estimates, the Commission observed that "we also believe that allowing the schedule for interim payments to slip undermines the effectiveness of the mechanism."[87] No matter whether this "belief" is held in good faith, the underlying assertion is a factual one, yet there is nothing in the record supporting such an assertion. To the contrary, all of the factual evidence runs counter to the assertion.

For starters, the same conditions and circumstances were considered and addressed in D.07-09-043. The Commission acknowledged that unforeseen circumstances might cause Energy Division to miss its target dates for EM&V reports, thus potentially requiring modifications to the adopted schedule, but in the very next breath, the Commission rejected a proposal to base interim earnings on the utility estimates in the event of a delay.[88] Rarely has the Commission been so clear in its decision that a potential outcome had been anticipated, fully commented on by the parties, considered and addressed. At the time the Commission adopted D.07-09-043, it did not "believe that allowing the schedule for interim payments to slip undermines the effectiveness of the mechanism."[89] Therefore, in order for D.08-12-059 to be legally defensible, it must point to something that has changed since the issuance of that decision that would warrant the Commission's reversal regarding these elements of the shareholder incentive mechanism.

The concerns raised in the Utilities' First PFM and addressed in D.08-01-042 do not support an about-face on the question of whether interim incentives should be paid

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[87] D.08-12-059, p. 16.

[88] D.07-09-043, p. 125, also Finding of Fact 118.

[89] D.07-09-043.

based on utility estimates. The Commission seems to suggest that the seeds for its outcome were planted there:

> [I]n D.08-01-042 the Commission accepted the notion that regularity and timeliness of interim claims is part and parcel of an effective incentive mechanism.[90]

Tellingly, the Decision cites no provision of the earlier decision that reflects the Commission's acceptance of any "notion" that would have ratepayers bear the risk of an overpayment as high as $82.2 million in order to avoid a delay of perhaps several months for an interim claim. That is because there is no way to read D.08-01-042 as supporting the outcome adopted in D.08-12-059.

In D.08-01-042, the Commission addressed circumstances that put at risk a utility's ability to book payments made based on fully verified interim claims if, at the time of the final true-up required in D.07-09-043, the utility were found to have fallen short of the threshold for earnings.[91] The result would be that the utility could receive payment for interim earnings according to the schedule established in D.07-09-043, but would not be able to "book" those authorized payments until several years later, and then only to the extent that the final true-up supported the interim payment. That scenario is a far cry from the relief granted in the Decision, which permits the Utilities to recover amounts based on unverified estimates of interim claims, due to a risk of a several month delay in order to obtain the verified figures on which the mechanism is premised. There is no suggestion that the value of the Utilities' ability to book its interim earnings once authorized turns depends on whether the earnings authorization issues in 2008 rather than early 2009.

Since the issuance of D.08-01-042, the only evidence regarding how delay might impact the effectiveness of the incentive mechanism are the statements the Utilities made in their SEC filings, and the lack of any apparent response from the financial community. In D.08-12-059, the Commission correctly interpreted those statements to "find that the

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[90] D.08-12-059, p. 13.

[91] D.08-01-042, p. 4.

utilities were aware of potential delays in the Energy Division review process and understood that earnings claims might not be finalized in 2008."[92] However, it attempted to dismiss the import of those SEC filings when it later stated that such "recognition is not, in [and] of itself a reasonable or logical counterargument to the concern that such delays undermine the effectiveness of the incentive mechanism."[93]

The approach adopted in D.08-12-059 is flawed in at least two important ways. First, it effectively requires intervenors to prove the negative, that is, to demonstrate that "such delays" do not undermine the effectiveness of the mechanism. But the burden is on the Utilities and, having at least implicitly embraced the claim, the Commission to demonstrate that the "concern" is valid and of such magnitude that it warrants putting ratepayers at risk of overpaying as much as $82.2 million in the first interim incentive claim.

Second, the logic embraced in D.08-12-059 ignores or misconstrues all that led up to the Utilities filing the instant petition for modification:

> • If there were any valid concern that a potential delay in the processing of interim earnings claims might undermine the mechanism, one would expect that concern to be addressed in the decision adopting the mechanism. Instead, as noted before, D.07-09-043 simultaneously acknowledged that there might be some delay to the adopted schedule, and rejected the suggestion that in the event of such delay, payments be made based on the utilities estimated savings.[94]
>
> • If the investment community or the Utilities had any second-thoughts about the impact that such delays might have on the viability of the overall mechanism, one would expect those misgivings would be raised as part of the first petition for modification of D.07-09-043. Instead, the Utilities addressed only the elements of the mechanism that might delay their ability to "book" interim earnings awards for one or two years, even if those awards were processed according

[92] D.08-12-059, p. 13.

[93] *Id.*, at 16.

[94] D.07-09-043, p. 125.

> to the precise schedule set forth in the decision. The material provided by members of the investment community made no mention of the potential for delays due to the verification of interim claims.
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> • The Utilities' SEC filings after D.08-01-042 was issued represent clear statements to the investment community that there was substantial uncertainty about whether the Commission would authorize the first interim incentive amounts before the end of 2008. Had this announcement caused any substantial concern that delays of this magnitude would undermine the effectiveness of the incentive mechanism, the investment community would have weighed in on the subject. The Utilities' failure to cite anyone other than NRDC as placing any stock in their current claims is telling.

In sum, nothing has changed since D.08-01-042 was issued that justifies any modification to that decision. At the time the mechanism was first adopted in D.07-09-043, the Commission identified the risk of delay in the payout of interim earnings should Energy Division's reports not issue as scheduled, and recognized that this risk did not warrant paying interim claims based on utility estimates. At the time the mechanism was first modified D.08-01-042, the risk of delay tied to Energy Division's reports remained, while the risk of overpayment from relying on utility estimates actually grew. Even if the belief and concern expressed in the D.08-12-059 were genuine, they are not a sufficient basis for modifying the shareholder incentive mechanism. The Utilities have to demonstrate that a "preponderance of the evidence" supports that belief. There is <u>no</u> evidence that a several month delay in the interim incentive payments will cause a real problem. Therefore, the Commission committed legal error and abused its discretion, because the findings in the decision are not supported by substantial evidence in light of the whole record, and the Commission did not have a sufficient basis for modifying the decision.

VII. DECISION 08-12-059 REFLECTS AN ABUSE OF THE COMMISSION'S DISCRETION.

An abuse of discretion is established if: (1) an agency does not proceed in the manner required by law**;** (2) an order or decision is not supported by the findings; or (3) the findings are not supported by the record.[95] Because the Decision contravenes the Commission's obligation pursuant to Section 451 of the Public Utilities Code to ensure that rates are just and reasonable, because the Decision in not supported by the findings necessary to support the incentives award, and because Finding of Fact 3 is not supported by substantial evidence, the Decision awarding incentives based on self-reported energy savings amounts to an abuse of discretion.

VIII. CONCLUSION

The Commission adopted a risk/reward mechanism that offers the opportunity for the Utilities to earn incentives for energy savings that approach or exceed the Commission's energy savings goals. Whether or not the Utilities' achievements in administering the 2006-07 energy efficiency programs deserve incentives is the subject of continuing debate in which some parties claim outstanding performance, and others document mediocre performance. The Decision fails to resolve this debate and instead allows the timing of incentive claims to trump the accuracy of their calculation. It dismisses the significant risk of overpayment that ratepayers face when they are required to pay incentives based on the Utilities' self-reported achievements, buttressed only by NRDC's analysis that admittedly contravenes the Commission's directive in D.08-01-042 to use updated metrics for calculating interim claims. It does so without evidence that a short delay in approving an incentives award will harm utility shareholders.

Providing "timely incentives" to the Utilities even if they have failed to meet the Commission's goals (unless self-reported savings based on outdated metrics are used) and have not effectively managed the forecasting uncertainties that are part and parcel of

[95] *Davis v. Civil Service Commission,* 55 Cal.App.4th 677, 686-687 (1997); *Sierra Club v. State Board of Forestry*, 7 Cal.4th 1215, 1236-1237 (1994); see also Code of Civ. Proc., §1094.5.

energy efficiency will not advance energy efficiency in California. Independent verification of utility energy savings claims has been an integral component of the incentive mechanism from the onset. The Commission has authorized spending $163 million on independent verification for the 2006-2008 energy efficiency programs. It is unconscionable for the Commission to ignore the independent verification results that it set in place as part of the incentive mechanism in the absence of substantial evidence that such a significant step is warranted.

Rather than sacrificing the integrity of the shareholder incentive mechanism in the interest of "timeliness," the Commission should grant rehearing and award incentives based on the Energy Division's Final Verification Report.

Respectfully submitted,

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February 2, 2009

CERTIFICATE OF SERVICE

I hereby certify that I have this day served a copy of "APPLICATION FOR REHEARING OF DECISION 08-12-059," in **R.06-04-010**. by using the following service:

[**X**] **E-Mail Service:** sending the entire document as an attachment to an e-mail message to all known parties of record to this proceeding who provided electronic mail addresses.

[ ] **U.S. Mail Service:** mailing by first-class mail with postage prepaid to all known parties of record who did not provide electronic mail addresses.

Executed on February 2, 2009 at San Francisco, California.

/s/ ROSCELLA GONZALEZ

Roscella Gonzalez

N O T I C E

Parties should notify the Process Office, Public Utilities Commission, 505 Van Ness Avenue, Room 2000, San Francisco, CA 94102, of any change of address and/or e-mail address to insure that they continue to receive documents. You must indicate the proceeding number on the service list on which your name appears.