



BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

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Order Instituting Rulemaking to Examine
the Commission's Energy Efficiency
Risk/Reward Incentive Mechanism.

R.09-01-019
(Filed January 29, 2009)

**APPLICATION FOR REHEARING
OF ORDER INSTITUTING RULEMAKING 09-01-019**

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I. INTRODUCTION

On February 4, 2009, the Commission instituted an Order Instituting Rulemaking to Examine the Commission's Energy Efficiency Risk/Reward Incentive Mechanism (Incentives OIR). The Incentives OIR "will evaluate modifications to the RRIM for energy efficiency first adopted in Decision (D.) 07-09-043."¹ The Commission suspended the schedule for verification and review of 2006-2008 incentive claims in favor of the Incentives OIR.²

The prospective nature of the proposal to revise the incentives mechanism is typical of Commission rulemakings, but one aspect of the Incentives OIR effectively operates to change D.08-12-059, issued on January 2, 2009. D.08-12-059 required the issuance of the Energy Division Verification Report on 2006 and 2007 Energy Efficiency Activities (Verification Report) through a draft resolution, but the Incentives OIR suspended the requirement, and did so without notice or the opportunity for comment. The portion of the Incentives OIR that suspended the requirement to issue the

¹ R.09-01-019, p. 1.

Verification Report via draft resolution therefore violates Public Utility Code Section 1708's requirement that Commission orders rescinding prior orders or decisions must allow parties notice and the opportunity to be heard or a record to support the decision. Moreover, the Commission's repeated vacillation on the process for payment of interim incentives embodies the type of arbitrary decision making criticized in *Duquesne Light Co. v. Barasch*.³

Pursuant to Rule 16.1 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 Order Instituting Rulemaking's issuance.

II. BACKGROUND

The Commission has been struggling to implement a workable shareholder incentive mechanism for nearly three years. After a process that included workshops and comments in 2006 and hearings in 2007, D. 07-09-043 adopted a shareholder incentive mechanism substantially more generous than any of the proposals advocated by DRA, TURN or any other ratepayer representative. The shareholder incentive mechanism allowed the Utilities⁴ to earn 9-12% of their portfolios' net benefits if they achieved energy savings that approached the Commission's goals as measured at the end of a three-year program cycle. Decision 07-09-043 also provided that the Utilities would receive interim payments of incentives, based on the portfolio's estimated savings during the three-year program cycle. The payment of interim incentives was subject to final

(continued from previous page)

² *Id.*

³ *Duquesne Light Co. v. Barasch*, 488 U.S. 299 (1989).

⁴ DRA and TURN's Application for Rehearing refers to Pacific Gas and Electric Company, Southern California Edison Company, San Diego Gas & Electric Company and Southern California Gas Company, the respondents in the Incentives OIR and R.06-04-010 as "Utilities."

true-up at the end of the program cycle by the verification of savings by Energy Division and its team of independent evaluation contractors.⁵

Pursuant to D.07-09-043, if Utilities achieved more savings than estimated in their interim incentive claims, they would receive additional payment as part of the final true-up. If Utilities achieved fewer savings than estimated in their interim incentive claims, they would refund the overpayment to ratepayers.

Decision 08-01-042 modified the interim incentive claim process in response to the Utilities' first Petition for Modification.⁶ If Utilities achieved more savings than estimated, they would receive additional payment as part of the final true-up. However, if Utilities achieved fewer saving than estimated, they would keep the overpayment.⁷ To mitigate the asymmetry of this "heads I win, tails you lose" approach, the Commission required the calculation of interim incentive payments to use the most up-to-date savings parameters rather than using Utility savings estimates based on outdated saving parameters.⁸ Use of more recent and independently developed savings parameters would decrease the risk of non-refundable overpayment as compared to using Utility savings estimates based on outdated savings parameters to calculate the interim payments.⁹

In response to the Utilities' next Petition for Modification of the incentives mechanism,¹⁰ D.08-12-059 authorized the payment of incentives to Utilities based on their self-reported, unverified energy savings estimates, which were calculated without

⁵ See D.07-09-043, Findings of Fact 107-111 at pp. 199-200 and Attachment 7.

⁶ 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.

⁷ D.08-01-042, Ordering Paragraph 2, p. 25.

⁸ The Commission required the use of updated savings parameters reflected in the Database for Energy Efficiency Resources (DEER). DEER is a database developed jointly 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.

⁹ D.08-01-042, Finding of Fact 15, p. 21

¹⁰ Petition for Modification of Decisions 07-09-043 and 08-01-042 by Pacific Gas and Electric Company, Southern California Edison Company, San Diego Gas & Electric Company and Southern California Gas Company, filed August 15, 2008.

using the updated energy savings parameters as directed in D.08-01-042. The Commission chose to ignore the results of the draft Verification Report, issued on November 18, 2008, which showed that only one of the four Utilities was entitled to incentives, such that D.08-12-059's authorized amount of \$82 million would result in non-refundable overpayments of about \$78 million.

Nevertheless, D.08-12-059 directed the issuance of the Energy Division Report via draft resolution on January 15, 2009.¹¹ The Commission ordered that the Verification Report and subsequent verification reports be issued via draft resolutions that included "detailed information regarding the underlying assumptions relied upon as well as supporting information and documentation that provides the basis for those assumptions."¹² The draft resolution would be subject to public comment before issuance by the Commission as a final resolution.¹³

The issuance of the Verification Report was delayed at the request of the Energy Division's Director, but when it was posted on February 5, 2009, it confirmed that only Southern California Gas Company was entitled to interim incentives and even then, only in the amount of \$2.8 million. None of the other Utilities had achieved sufficient savings to earn incentives.

Most recently, the Commission issued its new Incentives OIR that will consider "a more transparent, more streamlined and less controversial RRIM program."¹⁴ However, the Incentives OIR does more than establish a process for revamping the incentives mechanism. The Incentives OIR ordered that:

"[t]he requirement in Decision 08-12-059 that the Energy Division Verification Report be issued via resolution as a basis for earnings claims for 2006 and 2007 activities is suspended pending resolution of those issues in this

¹¹ D.08-12-059, Ordering Paragraph 7, at p. 28.

¹² D.08-12-059, Ordering Paragraph 6, at p. 28.

¹³ Commission Rule of Practice and Procedure 14.5

¹⁴ R.09-01-019, p. 4.

rulemaking, though the Verification Report may be issued for other informational or planning purposes.”¹⁵

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. When a reviewing court examines the validity of a Commission order pursuant to Section 1757 of the Public Utilities Code, it determines, among other things, whether the Commission has proceeded in manner required by law, and whether the decision is an abuse of discretion.¹⁶

IV. DISCUSSION

A. **The Incentives OIR’s order “suspending the issuance of the Energy Division Verification Report as a basis for earnings claims for 2006 and 2007 activities pending resolution of those issues in this rulemaking” modified D.08-12-059 without notice and opportunity to be heard.**

Decision 08-12-059 ordered the issuance of the Verification Report via draft resolution no later than January 15, 2009, and specified that the draft resolution include “detailed information regarding the underlying assumptions relied upon as well as supporting information and documentation that provides the basis for those

¹⁵ R.-9-01-019, Ordering Paragraph 4, at pp. 8-9.

¹⁶ 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 courts 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 be limited to determining whether, on the basis of the entire 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.”

assumptions.”¹⁷ Barely a month later, the Incentives OIR “suspended” the requirement that the Verification Report be issued via a draft resolution for purposes of considering the 2006-2007 incentives claim, although the Incentives OIR acknowledged the Verification Report could be used for “informational and planning purposes.”¹⁸

Ordering that the Verification Report be issued via a draft resolution in D.08-12-059 no later than January 15, 2009, and then “suspending” that requirement without providing the opportunities for parties to comment fails to comply with Public Utilities Code Section 1708.

Section 1708 provides:

The [C]ommission may at any time, upon notice to the parties, and with opportunity to be heard as provided in the case of complaints, rescind, alter, or amend any order or decision made by it. Any order rescinding, altering, or amending a prior order or decision shall, when served upon the parties, have the same effect as an original order or decision.¹⁹

For example, the Commission granted rehearing after TURN pointed out that D.02-07-037, in establishing rules for California natural gas utilities and the state’s largest electric utilities regarding subscription to turned back capacity on the El Paso Natural Gas Company, effectively negated D.95-12-046 without providing the requisite notice and opportunity to be heard.²⁰ Decision 03-04-061 recognized that “[b]y permitting full recovery of PG&E’s Transwestern subscription costs in the event [that] PG&E complies with the adopted rules and without any requirement that the utility comply with D.95-12-046, we have inadvertently modified the earlier Commission

¹⁷ D.08-12-059, Ordering Paragraphs 6 and 7 at p. 28.

¹⁸ R.09-01-019, Ordering Paragraph 4 at p. 9.

¹⁹ See e.g. *California Trucking Assn. v. Public Utilities Comm.* (1977) 19 Cal.3d 240, 244; D. 07-12-006, p. 6.

²⁰ D.03-04-061, Ordering Paragraph 1 at p. 10.

decision regarding recovery of Transwestern costs.”²¹ The Commission therefore granted TURN’s application for rehearing.

The Incentives OIR acknowledged that “D.08-12-059 required a review of the Energy Division Verification Report on 2006 and 2007 energy efficiency activities through a Commission Resolution” but concluded that the “upcoming Commission Resolution would likely consider the Verification Report “moot for purposes of 2006 and 2007 interim incentive payments” even though it could be used for upcoming planning purposes.”²²

Although the Commission may predict that the Commission Resolution would consider the Verification Report “moot for purposes of incentive payments,” the report’s issuance via draft resolution would have allowed parties opportunity to review the draft resolution including the “detailed information regarding the underlying assumptions relied upon as well as supporting information and documentation that provides the basis for those assumptions.”²³ This process would have allowed parties the opportunity to better understand and assess the Commission’s decision to award \$82 million in incentives, notwithstanding the clear and growing evidence that showed that the adopted amount would be an enormous overpayment. Before “suspending” issuance of the Verification Report via draft resolution, the Commission should have afforded parties the opportunity to comment on the suspension and its potential ramifications. Failure to do so contravenes Section 1708, and the Commission should grant rehearing of that aspect of the Incentives OIR.

²¹ D.03-04-061, p. 5.

²² R.09-01-019, p. 4.

²³ D.08-12-059, Ordering Paragraph 6, p. 28.

B. The Commission's Suspension of the Energy Division Verification Report as a basis for earnings claims for 2006 and 2007 activities is another arbitrary reversal of the Commission's energy efficiency incentives policy.

The Commission is charged with overseeing energy efficiency programs of the Utilities, while at the same time protecting the interest of ratepayers in ensuring the expenditures accomplish the Commission's energy savings goals. Review of the Commission's actions relating to energy efficiency incentives over the past three years reveals how heavily weighted the scales are now tipped in favor of Utility shareholders.

D.07-09-043 provided that the Utilities and the ratepayers would each be made whole in the event of over or underpayment of interim incentives to the Utilities.

D.08-01-042 abolished the symmetrical true-up established in D.07-09-043 and provided that the Utilities would be made whole in the event of underpayments, but would not be required to return overpayments of interim incentives. To reduce the risk of overpayment by ratepayers, D.08-01-042 required the calculation of interim incentives claims using the most up-to-date savings parameters as reflected in the Energy Division Verification Report.

D.08-12-059 effectively eliminated D.08-01-042's requirement that interim incentives be calculated using the most up-to-date savings parameters as reflected in the Energy Division Verification Report, and awarded the Utilities \$82 million based on their self-reported savings calculated with outdated savings parameters. D.08-12-059 ignored the results of the draft Verification Report, but ordered the issuance of the final Verification report by draft resolution no later than January 15, 2009.

R.09-01-019 then effectively conceals the Commission's potential mistake in awarding \$82 million in incentive payments by suspending D.08-12-059's requirement that the Verification Report be issued by draft resolution for purposes of the 2006-2007 incentives claim. That suspension thereby forecloses the possibility that ratepayers could perform a timely review of the rationale for the \$82 million award of incentives, notwithstanding the overwhelming evidence that showed that three of the four Utilities were not entitled to incentives.

At every step of the way when it appeared that protecting ratepayer interests in paying incentives only for verified energy savings that approach the Commission's goals might imperil the Utilities' desire for a guaranteed revenue stream, the Commission has reversed itself and decided in favor of the Utilities. The Commission's repeated fluctuation on issues related to the incentive mechanism to the detriment of ratepayers is the mirror image of the circumstances that led the United States Supreme Court to observe in *Duquesne Light Co. v. Barasch*,²⁴ that "a State's decision to arbitrarily switch back and forth between methodologies in a way that required investors to bear the risk of bad investments while denying them the benefit of good investments would raise serious constitutional questions." Although the Supreme Court in *Duquesne* considered a utility challenge to a state's ratemaking methodologies, the concern about arbitrary decision making is one that applies equally to the Commission's recent approach to balancing the risks between shareholders and ratepayers in adopting rules for energy efficiency shareholder incentives.

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²⁴ 288 U.S. at 315.

V. CONCLUSION

“Suspending” issuance of the Verification Report via draft resolution without allowing parties the opportunity to comment on the suspension and its potential ramifications contravenes Section 1708 of the Public Utilities Code. The Commission should grant therefore grant rehearing of that aspect of the Incentives OIR.

Respectfully submitted,

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March 6, 2009

CERTIFICATE OF SERVICE

I hereby certify that I have this day served a copy of “**APPLICATION FOR REHEARING OF ORDER INSTITUING RULEMAKING 09-01-019,**” by using the following service:

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 March 6, 2009 at San Francisco, California.

/s/ JOANNE LARK

Joanne Lark

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.

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