Testimony of Matthew Freedman
Senate Energy, Utilities and Communications Committee
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My name is Matthew Freedman and I have been a staff attorney with The Utility Reform Network (TURN) for the past 15 years. Based on my experiences, I will highlight a few key concerns with the current *ex parte* rules and practices at the California Public Utilities Commission (CPUC), identify possible solutions, and discuss the need for statutory reforms to the standards for the disqualification of Commissioners who make private deals with utilities.

THE CURRENT RULES ARE RIDDLED WITH LOOPHOLES

The current *ex parte* rules are riddled with loopholes that can be easily manipulated by experienced parties. I will highlight a few examples to provide context for my overall recommendations.

First, utilities routinely have discussions with Commissioners and their advisors about "procedural" issues to avoid triggering the *ex parte* rules.[1] A discussion about "procedure" can easily stray into areas of substance.

Second, communications with the General Counsel, Executive Director and Directors of all the various divisions are not covered under the *ex parte* rules. Utilities frequently meet with these individuals to express their concerns about issues pending in current cases. These staff are free to speak with any Commissioner about any issue at any time and can privately pass along concerns raised by the utilities.

Third, utilities often provide Commissioners and their advisors with "general briefings" that they claim are unrelated to issues being litigated in pending cases and therefore not subject to the *ex parte* rules. But these "general briefings" often echo and reinforce specific factual, legal and policy positions that the utility is pushing the Commission to adopt in pending cases.

Fourth, representatives from credit rating agencies and investment firms regularly meet with Commissioners to discuss ongoing General Rate Cases or penalty proceedings. These individuals are concerned about the potential impact of CPUC decisions on utility profits, spending, exposure to risk and credit quality. Yet they have no *ex parte* reporting obligation.

[1] CPUC Rule 8.1(c) states that "Communications regarding the schedule, location, or format for hearings, filing dates, identity of parties, and other such nonsubstantive information are procedural inquiries, not ex parte communications."

Fifth, the *ex parte* disclosure requirements state that the party must provide various details about the timing and location of the communication, which individuals were involved, and a description of what was discussed.[2] The description of the communication itself is perhaps the most critical element of the reporting. Utilities routinely provide very generic statements about the content of their conversation and omit meaningful details.

Sixth, parties in ratesetting proceedings must provide notice of private communications with Commissioners within three working days in order to allow other parties to seek equal time.[3] Utilities have gamed this rule by meeting with Commissioners less than three days before a vote on a pending matter and releasing their *ex parte* notice after the vote has occurred. This practice, which is fully permissible, denies other parties an opportunity to even seek their equal time before the issue has been decided.

Seventh, the sanctions for non-compliance with the *ex parte* rules are not sufficient to deter repeat offenders and are not applied with any consistency. The statutory penalty is set at between $500 and $50,000 "for each offense."[4] This amounts to little more than a wrist-slap for a major utility seeking regulatory approvals worth hundreds of millions, or billions, of dollars. Instead of financial sanctions, the Commission has also devised alternative remedies such as in a 2006 case where violations by PG&E led to a requirement that the utility develop "written best practices" to guide its own *ex parte* contacts.[5] The CPUC General Counsel found that the final document submitted to comply with this requirement demonstrated that PG&E had "made a good faith effort to develop best practices in this area."[6] That document was developed by the same PG&E Vice President who was recently fired for rampant violations of the *ex parte* rules and is currently a possible target of a criminal investigation into improper influence peddling.

RECOMMENDED MODIFICATIONS TO THE EX PARTE RULES

In light of these realities, TURN urges the Legislature to enact sensible reforms that would limit loopholes and abuses. Our recommendations include the following:

Banning individual Ex Parte meetings in ratesetting cases
So long as individual parties can meet privately with Commissioners and advisors at will in cases where large amounts of ratepayer money are at

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[2] CPUC Rule 8.4
[3] CPUC Rule 8.4
[4] California Public Utilities Code §2107.
[5] Decision 08-01-021, page 15.
[6] Decision 08-01-021, Appendix B-1

stake, utilities will dominate the process. Utilities have massive staff resources devoted to lobbying the Commission that are financed through the rates charged to their customers. If individual meetings are permissible, the utilities will continually deploy their well-funded staff to make legal and policy arguments through private meetings with anyone at the CPUC who will listen.

Reliance on all-party meetings and all-party written communications
In ratesetting cases, *ex parte* contacts should be limited to meetings where all active parties are invited to participate. Any written materials provided to a Commissioner or advisor should also be circulated to all other parties at the same time.

Broaden the definition of decisionmaker to include top CPUC staff
The definition of decisionmaker should include the General Counsel, the Executive Director, and the Directors of each of the major divisions. This expansion would ensure that utilities aren't getting around the *ex parte* restrictions by simply routing their conversations through other key CPUC staff.

Make individuals working for credit rating agencies or advising investors subject to the ex parte rules
Anyone with a financial interest in the outcome of a CPUC decision should be subject to the *ex parte* rules. Since the utilities often cite the expectations of Wall Street in their requests for higher profits, individuals representing credit rating agencies and advising utility investors should be treated just like representatives of consumers for the purposes of the *ex parte* rules.

Increase the sanctions for violations of the ex parte rules
As recent media reports demonstrate, the current sanctions are ineffective in preventing repeat offenses by utilities. The sanctions should provide effective deterrence by imposing meaningful financial penalties, revoking *ex parte* privileges for repeat offenders, and perhaps even establishing criminal liability.

STANDARDS AND PROCESS FOR DISQUALIFICATION DUE TO BIAS OR PREJUDICE

Recent press accounts suggest that Commissioners have engaged in wheeling and dealing with utilities behind closed doors. This behavior is not new and, astonishingly, may not even be prohibited under the Commission's own rules. Even when a Commissioner privately directs a utility to undertake a particular action, there is little recourse for parties seeking to litigate the outcome in a

contested Commission proceeding.

A motion seeking to disqualify the Commissioner assigned to a particular case for impermissible bias or prejudice is typically ruled upon by the Commissioner accused of bias. This sounds absurd but it is established Commission practice. Even worse, the legal standard for disqualification in a ratesetting proceeding (the most common type of case) is whether there is "clear and convincing" evidence that the Commissioner "has an unalterably closed mind on matters critical to the disposition of the proceeding."[7]

Although this issue has been litigated in a number of proceedings, I want to discuss a specific case involving San Diego Gas & Electric Company, one of its affiliates, and the Calpine Corporation. In May of 2003, SDG&E conducted a solicitation and sought bids to satisfy an identified need for 291 MW of new resources in its local area by 2007.

In the litigation that followed this solicitation, TURN and the Utility Consumer Action Network (UCAN) uncovered significant evidence demonstrating that CPUC President Michael Peevey had personally intervened to ensure that SDG&E selected Calpine's Otay Mesa Power Plant as a winning bidder. The evidence demonstrated that Commissioner Peevey engaged in a series of *ex parte* meetings with both Calpine and SDG&E executives. Commissioner Peevey also sent Commission staff to directly participate in negotiations over the plant. TURN obtained notes from these negotiations describing Commission representatives explicitly telling SDG&E that Commissioner Peevey wanted SDG&E to own or contract with Otay Mesa.[8]

Despite originally expressing interest in a single new combined-cycle plant to satisfy its identified need of 291 MW, SDG&E ultimately proposed 2 such plants as part of over 1200 MW of new resources including a $739 million contract for Calpine's 573 MW Otay Mesa Power Plant and the acquisition of Sempra Generation's 542 MW Palomar project. The Commission ultimately approved SDG&E's proposals on a closely contested 3-2 vote, with Commissioner Peevey providing the deciding vote.[9]

TURN and UCAN filed two motions seeking to have Commissioner Peevey disqualified from voting on the matter.[10] Consistent with standard practice at the

[7] See Decision 05-06-062, page 14 (denying rehearing of D.04-06-011 and rejecting efforts to require recusal of Commissioner Peevey)
[8] Concurrent brief of TURN and UCAN on the Motion of SDG&E for Approval to Enter into New Electric Resource Contracts, Rulemaking 01-10-024, March 8, 2004.
[9] Decision 04-06-011.
[10] Motion of TURN and UCAN Seeking the Recusal of Commission President Peevey, Rulemaking 01-10-024, April 26, 2004; Motion of TURN and UCAN for Reconsideration of

CPUC, Commissioner Peevey himself considered, and then denied, our motions. In his denial, he stated that although he had indeed facilitated negotiations between Calpine and SDG&E, there was insufficient evidence to demonstrate that he had an "unalterably closed mind" on the final proposal. He refused to apologize for his active role and insisted that he would have done a "disservice" to the public by failing to become involved.[11] The Commission ultimately concluded that, even if all the allegations of involvement were true, Commissioner Peevey could not have been shown to have an "unalterably closed mind" because he may have been open to different combinations of terms and conditions governing the deal.

Today, we are publicly releasing new evidence highlighting the extent to which Commissioner Peevey intervened in that case. This evidence comes in the form of an eyewitness account from an individual who worked as a lawyer for Sempra Generation during this period. In her account, she describes being called into a meeting with representatives of SDG&E, Sempra Generation, Calpine, Commissioner Peevey and the individual subsequently assigned to be the Administrative Law Judge reviewing the reasonableness of the Otay Mesa contract. In that meeting, Commissioner Peevey explicitly told SDG&E to make a deal with Calpine for Otay Mesa and promised that all approvals related to Otay Mesa, including SDG&E's separate request for over $200 million in new transmission, would be granted. According to the eyewitness account, Peevey also told SDG&E that failure to complete a deal for Otay Mesa would lead to a rejection of SDG&E's efforts to acquire Sempra's Palomar plant.

There is little doubt that Commissioner Peevey's direct involvement forced SDG&E to sign an expensive long-term contract that it did not want or need. None of the entities participating in this meeting provided any public notice or disclosure as required under the *ex parte* rules. Yet even if news of this meeting had become public, it is not clear that Commissioner Peevey would have been disqualified because it is almost impossible to demonstrate that a decisionmaker has an "unalterably closed mind". Indeed, no Commissioner has ever been disqualified based on the "unalterably closed mind" standard.

The CPUC has repeatedly concluded that the "unalterably closed mind" standard is a matter of law. This means that only a change in the law will cause the CPUC to modify its own practices. The Legislature can address this problem by making two specific statutory changes. First, under no circumstances should the ALJ or Commissioner accused of bias or prejudice be permitted to rule on any motion seeking their own disqualification. Second, the appropriate legal

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Assigned Commissioner's Ruling Denying Motion of TURN and UCAN Seeking the Recusal of Commission President Peevey, Rulemaking 01-10-024, June 4, 2004.

[11] Assigned Commissioner Ruling Denying Motion of TURN and UCAN Seeking the Recusal of Commission President Peevey, Rulemaking 01-10-024, May 25, 2004.

standard should be modified to ensure that if the Commissioner was directly involved in shaping a utility request or directing a specific contract to be executed, they should not be allowed to vote on the proposal. These are modest reforms but they represent a step in the right direction.

The Legislature must recognize that the CPUC is very unlikely to reform itself. Real reform will require changes to state law. There are several reform bills that will soon be coming before this committee. Hopefully, these bills will allow legislators and stakeholders to find agreement on the desirable elements of meaningful change.

I would be happy to answer any questions from the Chair and members of the Committee.