**BEFORE THE PUBLIC UTILITIES COMMISSION
OF THE STATE OF CALIFORNIA**

Application of Pacific Gas and Electric Company (U39E) for a certificate of public convenience and necessity to provide: (i) full facilities-based and resold competitive local exchange service throughout the service territories of AT&T California, Frontier California Inc., Consolidated Communications of California Company, and Citizens Telecommunications Company of California; and (ii) full facilities-based and resold non-dominant interexchange services on a statewide basis.	Application 17-04-010 (Filed April 6, 2017)

PROTEST OF THE UTILITY REFORM NETWORK

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PROTEST OF THE UTILITY REFORM NETWORK

On April 6, 2017, Pacific Gas and Electric Company (PG&E) filed the instant application, seeking to obtain a Certificate of Public Convenience and Necessity (CPCN) so it may become a competitive local exchange carrier (CLEC) and provide full facilities-based and resold competitive local exchange access and non-dominant interexchange services. In other words, PG&E wishes to expand from providing electric and gas services to now offer telecommunication services, and to rely largely on its existing electric utility infrastructure in order to provide such services. Pursuant to Rule 2.6 of the Commission's Rules of Practice and Procedure, The Utility Reform Network (TURN) submits this protest to PG&E's application.[1]

I. Introduction

PG&E is seeking authority to operate as a CLEC in the territories served by incumbent LECs AT&T, Frontier, Consolidated, and Citizens, and as a non-dominant interexchange carrier throughout California. At this very early juncture in the proceeding, TURN's review has identified a number of specific issues regarding PG&E's application, as further described below. TURN's protest also addresses the proposed category, need for hearing, and proposed schedule in PG&E's application.

II. Grounds of the Protest And Issues To Be Considered

A. The Commission Should Deny The Application Without Prejudice To PG&E Renewing Its Request At Some Future Point When There Is Less Reason To Be Concerned With Potential Diversion of Management Attention.

PG&E's track record of late with regard to its management of its gas and electric utility operations should give the Commission pause as to whether now is the right time to permit the

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[1] The notice of the filing of the application first appeared in the Commission's Daily Calendar on April 13, 2017.

utility become a Competitive Local Exchange Carrier. Recent years have seen, among other things, a pattern that is, at the very least, cause for concern: the San Bruno disaster, followed by several CPUC investigations into PG&E management practices and regulatory relationships, all culminating in the utility's recent felony conviction. Even if the Commission were to conclude that these events do not preclude permitting PG&E to become a CLEC,[2] it could reasonably conclude that now is not the time for the utility to be pursuing an avenue that creates a risk of diverting management attention away from activities directly associated with providing safe and reliable electric and gas service.

B. The Commission Should Require PG&E To Supplement Its Application With Sufficient Information Regarding the Potential Costs of PG&E's Proposed Telecommunication Services.

PG&E's application makes broad assertions about the costs associated with its proposed telecommunications services. There was no testimony providing any factual support for those assertions. TURN submits that the Commission needs additional cost information in at least two broad areas in order to assess the reasonableness of PG&E's proposal.

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[2] Pursuant to D. 95-12-056 and D.13-05-035, all CPCN applicants must certify that no one associated with or employed by the applicant as an affiliate, officer, director, or partner has been held personally liable or held a position with a company that has been found liable for, among other things, fraud or dishonesty, been the subject of a criminal investigation, entered into a settlement to settle unfair business practices claims, found to have violated *any* statute or regulatory rule, or is being investigated by *any* regulatory agency for failure to comply with such rules. It is worth noting that PG&E could only muster a weak acknowledgement that it, "cannot represent that none of its affiliates, officers, directors ….has not held these positions with a telecommunications carrier that filed for bankruptcy or has not been found criminally or civilly liable by a court…" (p. 15) This Commission should, at the very least, require PG&E to clarify and expand on this statement in order to assess whether the utility should be deemed fit to receive a CPCN at this time.

First, the Commission needs to get a reasonable estimate of the costs PG&E is avoiding or otherwise minimizing due to its ability to take advantage of its existing electric utility infrastructure as the backbone of its telecommunications service. As the application states,

> Applicant will primarily rely on its existing poles, buildings, fiber, conduits, ducts, rights of-way, and other facilities and structures of telecommunications carriers, utilities, and municipalities. For example, Applicant intends to utilize excess capacity on its existing fiber optic network to provide the proposed telecommunications services. In light of its existing, deployed network, Applicant anticipates offering service to certain customers without being required to undertake construction, and, to the extent Applicant is required to extend its existing network, such construction should be limited.[3]

TURN submits that additional information about the costs PG&E is able to avoid due to its ability to use its existing infrastructure is necessary to assess the competitive implications of permitting PG&E to enter the telecommunications market. It is clear that PG&E will have a "leg up" on other CLECs that lack such infrastructure of their own, and have had to invest in constructing or leasing the access that PG&E would have from day one of its telecommunications venture. Whether PG&E's entry into the market would advance the Commission's goals of broader and more effective competition is open to question under the circumstances. Additionally, the Application does not specify whether and to what extent PG&E's entry would benefit potential wholesale and retail end user customers as a result of this claimed cost savings being reflected in rates for PG&E's telecommunications services. A factual showing on the value of this infrastructure access is critical to answering such questions.

Second, the imputed cost or value of PG&E's ability to rely on its existing facilities and structures, as well as the resources devoted to maintaining those facilities and structures, is relevant to the development of any reasonable revenue sharing mechanism. As is further

[3] PG&E Application, pp. 12-13.

discussed below, ratepayers are, in effect, footing the bill for the entirety of that portion of PG&E's proposed telecommunications system. The reasonable share of CLEC-generated revenues that should flow to ratepayers would depend in part on an assessment of the value of these ratepayer-financed assets and resources.

C. PG&E's Proposed Net Revenue Sharing Should Be Rejected In Favor Of A Gross Revenue Sharing That Has The Majority Of Revenues Flowing To PG&E's Electric and Gas Customers.

PG&E proposes a net revenue sharing mechanism that would allocate net after-tax revenues 50/50 between ratepayers and shareholders. The utility would allocate to shareholders all "incremental costs of developing, marketing and offering the telecommunications services" associated with its CLEC business. The "non-incremental" costs, which include all embedded asset costs plus "Corporate Administrative and General costs," will not be allocated to shareholders, but instead would be borne 100% by PG&E's gas and electric utility customers.[4]

Should the Commission authorize PG&E to go forward with its CLEC, TURN recommends that the Commission reject PG&E's net revenue sharing approach in favor of a gross revenue sharing that assigns the majority of gross revenues to PG&E's gas and electric utility customers. The Commission has approved both gross and net revenue sharing mechanisms in the past. TURN submits that the Commission correctly recognized the superiority of a gross revenue sharing mechanism from the vantage point of "protect[ing] the ratepayers from significant downside business risk, while providing the opportunity for gains over the life of each endeavor the utility makes to utilize an asset."[5]

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[4] PG&E Application, p. 18.

[5] D.99-09-070 (approving Southern California Edison Company's gross revenue sharing mechanism for non-tariffed products and services), Finding of Fact 9.

A fundamental difference between a gross revenue sharing mechanism and a net mechanism is that under the gross revenue sharing mechanism, the ratepayers' share of the revenues is indifferent to the amount of incremental costs PG&E records to its CLEC activities.[6] In other words, if PG&E's CLEC service generates revenues of $1 million, under a 50/50 gross revenue sharing mechanism the ratepayer share will be $500,000 whether the utility records incremental costs totaling $100,000 or $250,000 or, should the utility's business case prove off-base, $600,000. But under a net revenue sharing mechanism, every dollar that is deemed an "incremental cost" reduces the ratepayer share by some amount.

PG&E presents three reasons for its "equal, 50/50, net revenue sharing mechanism." TURN submits that none of the cited reasons establish that a net revenue sharing mechanism is superior to a gross revenue sharing mechanism. In fact, for several of PG&E's cited criteria the gross revenue sharing mechanism is clearly the better option.

PG&E touts its 50/50 net revenue sharing proposal as one that "provides equal benefits to both ratepayers and shareholders."[7] This is an overly simplistic analysis – a 50/50 sharing might provide "equal benefits" if the sharing parties bear an equal share of the underlying costs. Here, as PG&E concedes, its gas and electric utility customers bear the far greater share of the costs as "non-incremental" and A&G costs. If the goal is to achieve a relatively "equal" allocation of benefits, the share of benefits should better reflect each party's share of the total costs of providing the new service.

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[6] There would remain a concern about whether all costs "incremental" to offering the CLEC service are recorded as such, rather than included in the GRC revenue requirement.

[7] PG&E Application, p. 19.

The Commission should reject PG&E's assertion that "several recent cases" used the 50/50 sharing approach in a manner consistent with what the utility proposes here.[8] These "recent" cases are from the 1990s, and the five cases involving SCE leases pre-dated the <u>gross</u> revenue mechanism adopted for that utility in D.99-09-070. Furthermore, it's not clear from PG&E's application if the utility believes that these twenty-year old decisions adopted revenue sharing on a <u>gross</u> or <u>net</u> basis.

The most recent decision addressing revenue sharing mechanisms of which TURN is aware is the Sempra Utilities' 2012 general rate case decision. There the Commission adopted a 75/25 ratepayer/shareholder revenue allocation for SDG&E's research and development activities (rather than the 60/40 allocation SDG&E proposed). It also rejected as unreasonable a 50/50 net revenue sharing mechanism for new non-tariffed products and services, in part because the return to ratepayers was not commensurate with their bearing up to 50% of the total costs of providing the product or service.[9]

The second reason PG&E cites in support of its net 50/50 sharing proposal is that it would be "simple and easy to understand and administer."[10] TURN submits that a <u>gross</u> revenue sharing mechanism is far simpler and easier to understand and administer. It reduces the likelihood of disputes about the reasonableness of the amounts treated as "incremental" costs. And the share received by ratepayers can be calculated based on the gross revenues, without the need for any calculation of cost offsets or tax impacts in order to derive of an "after-tax" amount.

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[8] *Id.*, p. 20.

[9] D.13-05-010 (Sempra Utilities' 2012 GRC), pp. 600 and 1023-1024.

[10] PG&E Application, p. 20.

The third reason PG&E cites is its ability to "predict with certainty" how its CLEC revenues would be treated.[11] TURN submits that in this regard a gross revenue sharing mechanism provides at least equal certainty.

PG&E presents a hypothetical that it claims demonstrates why a gross revenue sharing mechanism would not give it sufficient incentive to go forward.[12] The Commission should ignore this hypothetical, as it is based on a counter-factual assumption that PG&E would need to incur $80 of expense to produce $100 of gross revenue. The utility's experience with telecommunication-related services as non-tariffed products and services tells a very different story. In its 2017 GRC, PG&E's rebuttal testimony made clear that for its "wireless" and "fiber" services provided as NTP&S, it reports "net expense" of a small fraction of the revenue recorded for each service.[13] For the "wireless" service, the annual net expense averaged less than 10% of annual revenue in five of six years from 2010-2015, and reached only 12% the one year it exceeded 10%. The annual net expense figures for "fiber services" were even lower as a percentage of annual revenues (in the range of 8%). Therefore a more appropriate figure for illustrating the revenue sharing impacts would be net expenses of 20% (or $20 instead of $80 in PG&E's illustration).[14] Using the same illustrative sharing ratios from PG&E's application, the more realistic $20 of "shareholder-funded expense" on $100 of gross revenue yields a very different result than PG&E reported. Under PG&E's Case 1 (25/75 ratepayer/shareholder gross revenue sharing), ratepayers would get $25 as their 25% share of the gross revenues, and PG&E

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[11] *Id.*, p. 20.

[12] *Id.*, pp. 22-23.

[13] See Attachment 1 (Attachment D to Chapter 2 of PG&E-25 - Rebuttal Testimony on New Revenue Development).

[14] The 20% figure represents a conservative (that is, high) figure given the recent recorded figures for wireless and fiber services.

would realize $55 of before-tax net revenues ($75 - $20 = $55), or approximately $33 after-tax. ($55 – (40.75% X 55) = $32.59.) So rather than resulting in less net revenues to the utility than what it spent, a 25/75 gross revenue sharing mechanism would provide PG&E with net after-tax revenues of approximately **150**% on the $20 of "net expenses" it incurred to provide the service.

TURN submits that the calculations PG&E has provided do not demonstrate the purported superiority of a net revenue sharing mechanism over a gross revenue sharing mechanism. Once corrected to reflect a more reasonable forecast of the net expenses associated with this new service, such calculations illustrate well the need to adopt a sharing mechanism that allocates the greatest share of gross revenues to PG&E's ratepayers. Such an allocation is more consistent with the new service relying very heavily on ratepayer-funded assets devoted primarily to providing gas or electric utility service, and would provide PG&E with a return that is more proportionate to the costs the utility purports would be borne by its shareholders. For example, with a gross revenue sharing mechanism allocating 70% of gross revenues to ratepayers and 30% to shareholders, and assuming $20 of shareholder-funded expense, PG&E would still realize nearly $6 of after-tax net revenues on its $20 investment, for a return on investment of nearly 30%.

Shareholder Gain Calculation (See PG&E Application, p. 23)	
Gross Revenue	$100
Less: Ratepayer Share	$70
Shareholder Share	$30
Less: Shareholder-funded Expense	$20
Pre-tax Shareholder Gain	$10
Tax at 40.75%	$4.07

Post-tax Shareholder Gain	$5.93
Post-tax Shareholder Gain as %-age of Shareholder-funded Expense	29.6%

This is an incomplete illustration, of course, given that the nature of this service makes it likely that the bulk of any incremental cost to the utility's shareholders will be incurred in year 1, while the resulting revenues will be collected over a multi-year period. So while the year 1 return on investment appears to be approximately 30%, in future years PG&E's post-tax shareholder gain would likely accrue with little additional investment to produce the revenues, thus producing an even higher imputed return on that investment.

TURN submits that if the Commission determines that the other issues associated with PG&E's application do not warrant outright denial of the requested CPCN, the revenues generated as a CLEC should be subject to a gross revenue sharing mechanism that allocates 70% of the gross revenues to PG&E's gas and electric ratepayers.

D. The Commission Should Require PG&E To Provide More Detailed Information Regarding The Business Plans For Its New Venture.

PG&E's application does not provide sufficient information to allow the Commission to understand the business plans for its new CLEC business venture. While PG&E supports its request with a laundry list of benefits of its market entry that it predicts will encourage and support competition in California's telecommunications marketplace, it provides no specifics on the types of services that it will be offering.[15] To add to the mystery, PG&E estimates "it will have approximately 1-5 customers after one year and will have more than 5 customers by the

[15] PG&E clearly states that it will *not* offer local exchange service to residential customers. (Application, p. 13). With this authority, however, PG&E could offer other types of telecommunications services to residential customers relying on its existing facilities, billing relationships, and data regarding those residential customers residing in its service territory.

fifth year after commencing provision of the services."[16] These are surprisingly low numbers given the utility's name recognition, significant existing network, and existing relationships with many potential wholesale and enterprise customers. And it suggests PG&E might have in mind a specific relationship with a specific business partner, or a very small set of potential business partners.

The Commission should request further information regarding PG&E's plans, including the possibility that, despite the vague promises in its Application, the utility actually has very specific and concrete plans for the use of its new found telecommunications authority, and that it already intends to target select large wholesale customers. For example, AT&T recently announced a project to place antennas for broadband service on power lines that will enter technical trials this year.[17] If PG&E's plans are to use this requested authority solely to facilitate AT&T's technical trials, the Commission would appropriately look at the application differently than if the utility intends to be a robust provider of wholesale services. Moreover, if granted this authority, it is not clear whether PG&E will continue to offer the dark fiber access it currently provides, which would eliminate a supplier of important wholesale services in an already shrinking market.[18] PG&E should be required to provide more information about its plans so the Commission can determine if granting this authority to PG&E is in the public interest, including adequate protections for ratepayer revenue sharing and nondiscriminatory access for potential competitors.

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[16] PG&E Application, p. 13.

[17] See, *AT&T in Advanced Discussions with Power Companies and Others to Trial Project AirGig* (January 31, 2017) at http://about.att.com/story/trial_project_airgig.html

[18] PG&E Application, p. 11 ("The recent wave of mergers and acquisitions within the telecommunications industry – reducing competition –further increases the importance of Applicant entering the market.")

Further information may also help the Commission make sense of the Application's extensive discussion regarding CEQA requirements and PG&E's proposal to be granted an exemption or, in the alternative, an expedited 21-day CEQA process for construction activities related to its telecommunications services.[19] This request does not match PG&E's insistence that it will have to do little, if any, construction to extend its facilities and that any work would at most be "minor ground-disturbing activities."[20]

Additionally, PG&E should be called upon to further explain its claim that it is "not aware of a specific safety issue beyond what is already required by applicable rules."[21] The Application is silent as to whether PG&E's expansion of its telecommunications service offerings will impact the safety and reliability of existing equipment on its poles, conduits and other support structures, as well as the reliability of its current communications networks. PG&E must provide more information about its business plans, marketing, and network infrastructure to allow the Commission to gauge and, if necessary, require mitigation of any impacts on the safety and reliability of both its electric utility services and its new telecommunications service offerings.

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[19] PG&E Application, pp. 5-9.

[20] PG&E Application, p. 5 (See recent approval of Cal.net CPCN application, refusing a request to exempt Cal.net expansion activities in sites that have not yet been identified, except where local authorities have granted approval, and imposing extensive documentation requirements for 21-day expedited review. D.17-02-008, p. 6.)

[21] PG&E Application, p. 2.

III. Proposed Categorization, Need for Hearing and Schedule

PG&E proposes that this application be categorized as ratesetting.[22] TURN agrees that this is the appropriate category.

On the need for evidentiary hearings, PG&E states that its application "includes the requisite information" on its proposed revenue-sharing mechanism "such that hearings should not be necessary for the Commission to resolve these issues."[23] TURN disagrees, and contends hearings are sufficiently likely to be necessary that the Commission should adopt a procedural schedule that anticipates evidentiary hearings. As described above, TURN disputes the reasonableness of PG&E's proposed revenue-sharing mechanism, and proposes a very different alternative. The underlying issues are largely fact-based. They include not only the specifics of the different proposed sharing mechanisms, but also extent to which the PG&E-proposed service intends to rely on electric utility infrastructures whose costs are recovered through the authorized revenue requirement, as compared to the amount of incremental investment likely to be borne by the utility. Where the outcome will likely turn on such factual determinations, the Commission should anticipate that evidentiary hearings will be needed.

TURN does not have a fully-developed alternative schedule at this time. This is partly due to the likely need to have PG&E provide supporting testimony – at this stage, PG&E's showing is contained entirely in its application. Whether or not PG&E is directed to provide direct testimony to support its requested relief here, parties must be provided sufficient time to engage in discovery and to prepare testimony analyzing PG&E's proposal and developing alternatives should they choose to present one. TURN submits that intervenor testimony should

[22] PG&E Application, p. 2.

[23] *Id.*, p. 3.

be due no earlier than six weeks from either the prehearing conference or the date on which PG&E serves testimony in support of the application. The remaining dates on the procedural schedule should not be hard to fill in during discussions leading up to or during the prehearing conference.

TURN does not dispute PG&E's assertion that in 1995 the Commission stated that it intended to grant applications for CLEC CPCNs on a streamlined basis. However, TURN submits that the Commission's statement was made in the context of a CPCN application that was not submitted by a regulated energy utility for which the Commission might have legitimate concerns regarding the potential diversion of management attention from its core operations providing regulated utility service. TURN further submits that the statement likely did not have in mind a CPCN application that would present issues such as reliance on facilities and equipment intended to be primarily devoted to providing other regulated utility service, or the need to develop appropriate cost assignment and revenue sharing between the company and customers of that regulated utility service.

May 15, 2017 Respectfully submitted,

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