

A Public Utility's Obligation to Serve: Saber or Double-Edged Sword?

For the past decade, California's investor-owned utilities have frequently relied upon the "duty or obligation to serve" as the means for obtaining valuable concessions from the California legislature and Public Utilities Commission. The utilities have exploited this regulatory principle as one of their primary weapons to justify billions of dollars of rate recovery and concessions. It is clear, however, that the duty to serve is not a saber which is only available to the utilities. Rather, the duty to serve is a double-edged sword that might equally be brandished by ratepayers.

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I. The Obligation to Serve: The Justification for the Recovery of Billions of Dollars and the Vehicle to Solidify Monopoly Positions

A public utility's duty or obligation to serve its customers has been the regulatory principle used by utilities to justify

recovering billions of dollars from their customers. For example, with the advent of electric deregulation, California electric investor-owned utilities (IOUs) relied upon this principle as the basis for their claims that they were entitled to a special non-bypassable surcharge designed to recover stranded costs of generation. The utilities

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argued that with the introduction of competition in generation, many of the generating facilities that they had constructed to carry out their obligation to provide electric service would become non-competitive and that the investment costs associated with these facilities would be stranded. The utilities made this same argument with respect to contracts with qualifying facilities (QFs) that they were forced to execute under the state's implementation of the Public Utility Regulatory Policies Act of 1978 (PURPA). In acceding to these claims and authorizing a special non-bypassable charge known as the competition transition charge (CTC), which was imposed on all current and future electric customers taking service in the IOUs' designated service territories, the California Public Utilities Commission (CPUC) explained:

Under the current regulatory structure, we have granted utilities monopoly franchises to provide electricity to the consumers in their service territories, and we have required utilities to provide reliable service on a nondiscriminatory basis to all customers within their service territories who requested service. In fulfillment of these responsibilities, utilities developed a portfolio of generation assets by investing in power plants and entering into purchase agreements on the understanding, the utilities contend, that reasonable costs would be recovered in rates Utilities argue that these investments were found prudent at the time they were made and therefore they should be entitled to full recovery We conclude that the utilities should be allowed to

recover appropriate transitions costs We agree that recovery of retail transition costs should be subject to state jurisdiction State jurisdiction over retail transition costs extends, in our view, to costs stranded by retail customers converting to wholesale status¹

The CPUC revisited and expanded upon this explanation in discussing Pacific Gas and Electric Company's (PG&E's) complaint that certain retail customers were making

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arrangements to attempt to avoid CTC:

The Policy Decision described certain costs that the electric utilities had incurred as part of their obligation to serve their customers but that the utilities would likely be unable to recover in the competitive market foreseen in that decision. These transition costs include the uneconomic portion of the net book value of generation facilities, the above-market costs associated with nuclear power plant settlements and power purchase contracts, and costs arising from regulatory obligations. Recognizing that these costs stem from the utilities' efforts to provide reliable service to their customers, we found it fair to allow the utilities an opportunity to recover appropriate transition costs.²

Based on the premise of recovering costs that were incurred as part of their obligation to serve, but which would be stranded in a competitive electric market, California's three investor-owned electric public utilities, PG&E, Southern California Edison Company (SCE) and San Diego Gas & Electric Company (SDG&E) recovered billions of dollars from their customers.

In addition to being the conceptual basis by which the utilities convinced regulators to approve the recovery of billions of dollars of stranded costs, California's IOUs have also found the "obligation to serve" to be a potent offensive weapon to solidify their monopoly position in their respective distribution service territories and to eliminate competition from direct access energy service providers (ESPs) and public entities, such as municipalities and irrigation districts (which we'll refer to as "public power entities"). Using the obligation to serve as the primary justification, the utilities have convinced the CPUC that, with minor exceptions, all customers, both present and future, are responsible for sharing the costs incurred by the California Department of Water Resources (CDWR) when it was forced to step in and buy power to meet the IOUs' obligations.

In the proceedings to determine the means by which CDWR would recover such costs, the IOUs have argued that the costs should be spread to as many customers as possible, including

direct access customers that no longer receive CDWR power, existing customers that may be annexed by public power entities, and even by customers that are not currently in existence, but which may be served in the future by public power entities that annex a portion of the IOUs' current service territories. Once again, relying on the regulatory principle that public utilities have an "obligation to serve," the IOUs have claimed that the forecasts they gave to CDWR and which CDWR relied upon in determining its electric contract needs, reflected the principle that an IOU has an obligation to provide service to all customers in its service territory. Consequently, the utilities' forecasts assumed that direct access customers that had returned to bundled utility service would continue to take utility service. In addition, the forecasts generally did not contemplate any expanded development by public power entities, either through municipal acquisition or "green-field" development within the IOUs' service territory. As a result, the IOUs have asserted that all customers, current and future, that are located within the boundaries of their service territories are responsible for reimbursing CDWR for its costs. Of course, CDWR's costs are monumental. For direct access customers, the CPUC has imposed a special surcharge, known as the Cost Responsibility Surcharge (CRS), which is capped at 2.7 cents per kW h and which is currently not fully compensa-

tory.³ The CPUC has also decided that municipal departing load customers are responsible for CDWR's costs,⁴ as are some customers that are now generating their own electricity, rather than taking utility service.⁵

The effect of imposing CRS on all customers has been an enormous competitive benefit to the IOUs. The 2.7 cents per kW h surcharge has for all significant purposes curtailed any threat of

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competition. With the addition of this surcharge, there is insufficient margin for direct access competition to gain a foothold in public utilities' service territories. Similarly, such a surcharge has tended to eliminate any competition by public power entities. Thus, relying on the principle that public utilities have an obligation to serve and must plan for the future needs of their respective customers, the IOUs have succeeded in institutionalizing an effective weapon against competition.

The utilities also have succeeded in carrying over these same anti-competitive arguments

to new power plant development. Recently, SCE proposed that it be allowed to enter into a long-term contract to purchase electricity from an affiliate that would own the Mountainview Generating Facility. While SCE contended that the facility was needed to satisfy its public utility obligation to serve, there was considerable dispute on this issue. Therefore, while finding the plant was needed, the CPUC also hedged its bet, ordering that all SCE customers currently ineligible for direct access would be obligated to pay for any stranded costs that might be related to the Mountainview facility for the first 10 years of its life.⁶ SDG&E also has argued for the creation of a "regulatory asset" for its Otay Mesa and Palomar plants. Once again, the regulatory principle that a public utility has a duty to serve and plan for the service needs of its customers proved to be a potent utility weapon in securing cost recovery or shedding risk to ratepayers.

II. A Public Utility's Obligation to Serve

While the utilities frequently play the "obligation to serve" card when it fits their needs, there rarely is a discussion of the full import of this basic principle of public utility regulation. What exactly is a public utility's obligation to serve?

A public utility's duty to serve has its origins in common law principles. This history was

explained by Professor Rossi in his article "Universal Service in Competitive Retail Electric Power Markets: Whither the Duty to Serve?"⁷

Twentieth century U.S. regulators built on an ancient common law duty that applied to public utilities such as ferries, flour mills and railroads, imposing on electric utilities a "duty to serve," an obligation to provide extraordinary levels of service to customers, especially small residential customers. As applied today in most states, the public utility duty to serve entails several obligations, including: the duty to interconnect and extend service if requested; the duty to provide continuing reliable service; the duty to provide advanced notice of service disconnection; and the duty to continue service even though a customer cannot make full payment. Unlike other obligations that apply to private firms, including those such as inns and restaurants representing or holding themselves out as serving the public, in the public utility context the duty to serve requires service where it is not ordinarily considered profitable.⁸

The duty to serve emerged not only from common law principles but from statutory law as well. California Public Utilities Code ("P.U. Code") Section 451 lays the foundation for a public utility's duty to serve in California.⁹ It requires that every public utility furnish and maintain such adequate, efficient, just, and reasonable service instrumentalities, equipment and facilities, as are necessary to promote the safety, health, comfort, and convenience of its patrons, employees, and the public.

Encompassed within the duty to serve is the duty to render "adequate" service. Although difficult to define with precision, the broad contours of the adequacy requirement have been sketched out by commentators, regulators, and courts. As discussed in "The Duty of a Public Utility to Render Adequate Service: Its Scope and Enforcement,"¹⁰

[t]he primary duty of a public utility is to render adequate service

California courts have interpreted "reasonable diligence" to require affirmative actions to avoid unreasonable risk to customers.

to its consumers. This obligation, originally imposed by the common law and presently incorporated in state utility statutes, arises independently of any contractual relations between the company and its customers. The duty to render adequate service has two aspects; it delimits the areas of the community to which, and the particular individuals to whom, service must be rendered, and it establishes standards of adequacy of service.

The standard of adequacy is incapable of precise definition and depends initially on the type of service rendered and the needs of the area in which the utility operates. Statutes declare that the minimum obligation of any utility is to provide safe, continuous, comfortable, and efficient service

with facilities that reflect technological developments in the industry.¹¹

Because adequacy means "safe, continuous, comfortable, and efficient service," the utilities' tariffs require them to act diligently to avoid power shortages. For example, Rule 14 of SCE's electric tariff provides:

Shortage and Interruption.

SCE will exercise reasonable diligence to furnish/deliver a continuous and sufficient supply of electricity to its customers and to avoid any shortage or interruption of delivery thereof. It cannot, however, guarantee a continuous or sufficient supply or freedom from interruption.¹²

California courts have interpreted "reasonable diligence" to require affirmative actions to avoid unreasonable risk to customers. The seminal case is *Langley v. Pac. Gas & Elec. Co.*,¹³ in which Chief Justice Roger Traynor explained the duty to serve and its interrelationship to PG&E's Rule 14:

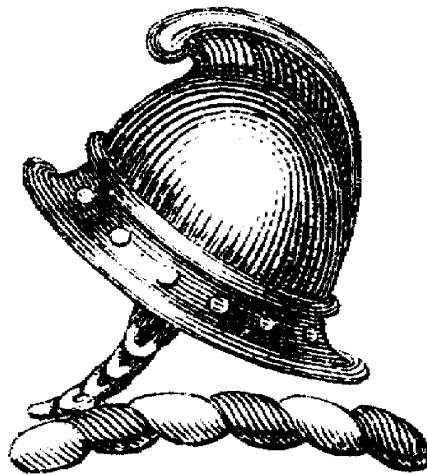
[D]efendant agreed to furnish electricity in accordance with the applicable rules and regulations of the Public Utilities Commission. Rule 14 requires defendant to exercise "reasonable diligence and care" to furnish a continuous and sufficient supply of electricity to its customers. It further provides that defendant shall "not be liable for interruption or shortage or insufficiency of supply or any loss or damage of any kind or character occasioned thereby ... except that arising from its failure to exercise reasonable diligence." Defendant contends that under these provisions its duty is limited to

exercising reasonable diligence to furnish a continuous and sufficient supply of electricity, and that it is under no duty to exercise reasonable care or diligence to prevent loss from power failure when it is not legally responsible for the power failure itself. These provisions deal with the duty to supply power, and they make clear that defendant is not an insurer or guarantor of service. In no way, however, do they abrogate defendant's general duty to exercise reasonable care in operating its system to avoid unreasonable risks of harm to the persons and property of its customers.¹⁴

Building on *Langley's* reasonable care requirement, a recent unpublished opinion found that the duty to serve includes an affirmative obligation on the part of the utilities to take precautions against the harm caused by power supply disruptions.¹⁵ In *Mobil Oil*, the court interpreted SCE's Rule 14 and its obligation to serve and held that, despite an interruption of electric supply in the Pacific Northwest which was outside of SCE's direct control, a suit against the utility for failing in its duty to serve had sufficient merit to reach trial.¹⁶ The court stated:

In this case, unlike *Langley*, it was disputed whether Edison was responsible for the disturbance inasmuch as it connected itself to the western grid, leaving Mobil vulnerable to any deficiencies in any of Edison's neighboring systems in addition to its own. BPA had clearly violated multiple industry standards in the events precipitating the disturbance, but Edison, not BPA, contracted with Mobil as its customer.

Moreover, there was substantial evidence that Edison knew of Mobil's particular need for reliable power and that Mobil faced considerable loss without a continuous supply of electricity as established by the factual summary set out above. Further, there was substantial evidence that Edison had repeatedly assured Mobil that it was committed to taking every step necessary to maximize the reliability of



power to Mobil. As Mobil acknowledged, "perfect" power is an impossibility. The reality of power outages caused by a car hitting a utility pole, for example, always exists. As Edison's Nola testified, however, even if Edison could not prevent certain events, it could take steps to plan for such occurrences and minimize ... the effects on Mobil of the August 1996 disturbance.¹⁷

The Court went on to state:

Causes within a party's control include causes that could have been *prevented* by foresight and sufficient expenditure, and "reasonable control" includes the notion that a contracting party must exercise reasonable diligence in taking steps to ensure performance and to prevent an event from occurring.¹⁸

It is absolutely clear that adequate service means not only providing safe electricity over a well-maintained system, but it also requires the utilities to provide enough electricity to meet their customers' needs. In a recent case the CPUC addressed the utilities' roles in assuring reliability of service with respect to energy procurement. In D.04-07-028 the Commission stated:

The Commission and the Legislature have expressed their clear intent that utilities should procure resources in a manner consistent with utilities' statutory obligation to serve their customers. The utilities' obligation to serve customers is mandated by state law and is a fundamental element of the entire regulatory scheme under which the Commission regulates utilities pursuant to the Public Utilities Act. (See, e.g., §§ 451, 761, 762, 768, 770.) While § 345 clearly assigns the CAISO [California Independent System Operator] responsibility for ensuring reliable grid operations, this statutory obligation does not diminish in any respect the utilities' obligation to procure resources for their loads to ensure reliability. To be clear, it is our view that while the CAISO has the responsibility to ensure and maintain reliable grid operations, it is the LSEs' [load-serving entities'] responsibility to have sufficient and appropriate resources to make that reasonably possible.¹⁹

The penalty for breaching the duty to serve is money damages, as codified in California law.²⁰ In both *Langley* and *Mobil Oil*, the plaintiff was suing for monetary damages. The Court in *Langley* affirmed the damages award, holding: "By undertaking to

supply electricity to plaintiff, defendant obligated itself to exercise reasonable care toward him, and failure to exercise such care has the characteristics of both a breach of contract and a tort.”²¹ And in *Mobil Oil*, the Court allowed the matter to go to a jury.²²

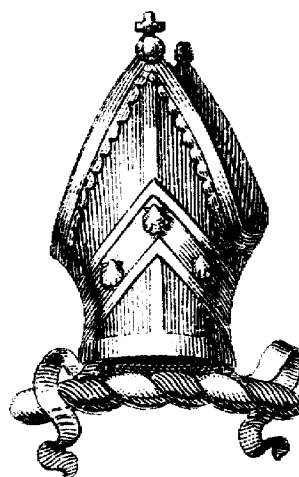
III. The Energy Crisis: PG&E and SCE Fail to Provide Service to Their Customers

A. Background to the energy crisis: the passage of legislation restructuring California's electric industry

California's energy crisis has its roots in California's failed attempt to deregulate and restructure its electric industry. Following the issuance by the CPUC of its Policy Decision restructuring electric markets,²³ in 1996 Gov. Pete Wilson signed Assembly Bill 1890, which paved the way for restructuring California's electricity market in 1998.²⁴ A key feature of the restructured electricity market was that retail rates were to remain frozen for a period not to exceed four years.²⁵ Under A.B. 1890, to the extent a utility's charges for energy, transmission, distribution, and other services were less than the frozen rates that they were allowed to charge (the differential being known as “headroom”), the utilities were allowed to collect and keep the additional amounts. The residual

amounts were referred to as the competition transition charge and, as described previously, were intended to pay off any stranded costs the utilities might claim associated with restructuring.

In order to promote market transparency and to mitigate market power concerns, California's deregulated electric



market also required IOUs to sell the output of their remaining utility-owned generation to a central power exchange, the California Power Exchange (Cal PX), and to purchase all of the electricity that they required to serve their respective bundled customers from the Cal PX. Initially, the IOUs were limited to purchasing electricity from the Cal PX in the day-ahead and hour-ahead markets. In addition, for transmission system operating purposes, the utilities also made short-term purchases from the California Independent System Operator, the entity formed as part of California's deregulation scheme to operate the utilities' transmission systems.

Customers were given the option of taking “direct access” or bundled service under California's deregulated market structure. Bundled service is when a customer purchases a complete package of energy, transmission, and distribution service from the IOU. Under California's scheme, a bundled customer paid the frozen tariff rate. A direct-access customer, on the other hand, purchases its electric energy from a third party, an electric service provider, with the IOU providing transmission and distribution services in its capacity as a utility distribution company (UDC). A direct-access customer is also responsible for paying CTC to the utility. The utility, however, remained the provider of last resort. A direct access customer could return to bundled service at any time and without charge. In other words, the IOU retained its public utility obligation to serve everyone in its service territory.

For the first year or so, California's deregulated market seemed to work well. From the commencement of restructuring in early 1998 through 2000, the IOUs reaped tremendous benefits from CTC payments. SCE accumulated over \$7 billion in a special balancing account designed to track its recovery of its stranded costs and PG&E accumulated over \$9 billion in a similar account.²⁶ SDG&E recovered all of its stranded costs by summer 2000.²⁷ During the same period and continuing through 2000, the utilities

disbursed billions of dollars that had been collected through headroom in frozen electric rates as dividends to their parent corporation or through the repurchase of their common equity from their respective parents.

B. The spike in wholesale prices and the insolvency of PGE and SCE

In late May 2000, things began to change very quickly. A booming economy, a shortage of generation due to the utilities' historical failure to construct or procure sufficient generation to meet demand, drought conditions that reduced hydroelectric output, and other factors caused wholesale electricity prices to rise to such an extent that the IOUs' wholesale cost of electricity began to exceed the frozen retail rate. By the autumn of 2000, the utilities began to get desperate. Initially, they sought greater flexibility to purchase electricity from entities other than Cal PX and for periods that were greater than the Cal PX's short-term markets. The CPUC provided this additional authority.

Wholesale prices, however, continued to rise and in November 2000, both PG&E and SCE filed what they termed "Rate Stabilization Plan" applications. On Dec. 21, 2000, the CPUC acknowledged the crisis in wholesale and retail electric markets in California and expressed concern about the utilities' financial health.²⁸ After holding emergency hearings

across the holidays, on Jan. 4, 2001, the CPUC adopted D.01-01-018, granting emergency rate relief. D.01-01-018 raised rates for PG&E's and SCE's bundled and direct-access customers by 1 cents per kW h in order to "improve the ability of the applicants to cover the costs of procuring future energy in wholesale markets."²⁹ The increase was only an interim



increase, extending for a period of 90 days, and was earmarked for the utilities to "procure[] future energy in wholesale energy markets."³⁰

On March 27, 2001, after the utilities had already failed to arrange sufficient supplies of electricity to their customers, the CPUC again increased rates for bundled and direct access customers.³¹ The CPUC made the 1 cents per kW h surcharge permanent and imposed an additional 3 cents per kW h surcharge on bundled customers, noting that the increase "will cost the customers of the utilities approximately \$2.5 billion annually."³² As discussed further below, this additional surcharge

was intended to help pay CDWR's costs of providing electricity to the IOUs' customers, and specifically states that "Revenue generated by the rate increases will be applied only to electric power costs that are incurred after the effective date of this order." (*Id.* at 16.).

C. The IOUs request to be relieved of their public utility obligation to serve

During the period leading up to the imposition of the 1 cents surcharge and in the hearings that led to its issuance, SCE and PG&E threatened to cease supplying electricity to customers to the extent that they could not purchase power at a cost at or below the frozen rate or to the extent the utilities' own generation was inadequate to satisfy the needs of its customers. The irony here is that the utilities had used the obligation to serve to justify the CTC and rate freeze and it was now coming back to haunt them. But if the irony was lost on the utilities, it was not lost on the CPUC.

In response to the IOUs' threats, the CPUC issued a temporary restraining order against SCE and PG&E specifically ordering them to "continue to provide full and adequate service to all of their customers" and restraining them from refusing to act as scheduling coordinators to serve all of their non-direct-access customers.³³ The CPUC affirmed that "California utilities must serve their customers. This requirement,

known as the 'Obligation to Serve' is mandated by state law."³⁴ The CPUC went on to say that nothing in A.B. 1890 relieved the utilities of their obligation to serve all customers in their service territories under their respective tariffs. The CPUC further found:

State law clearly requires utilities to serve their customers, and a threatened bankruptcy filing or threat of insolvency does not change that obligation.

....

Under Public Utilities Code sections 451, 761, 762, 768 and 770, PG&E and Edison have an obligation to provide full and adequate service to all of their customers, including continuing to enter into and maintain any current and future low-cost contracts to procure power.³⁵

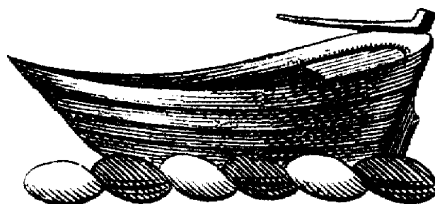
On July 12, 2001, the CPUC denied SCE's and PG&E's request for rehearing and reaffirmed their statutory obligation to serve their customers, stating: "We also affirm that California utilities have an ongoing obligation to provide adequate service to their customers, including the obligation to serve all non-direct-access, or bundled, customers and may not unilaterally act to reduce or curtail service without formal approval by the Commission."³⁶

D. The state is forced to step in

Despite the Commission restraining order affirming the utility's obligation to serve and the CPUC's efforts to strengthen the utilities by increasing rates

and granting additional flexibility in procuring electricity, the utilities continued to experience severe financial stress. In mid-January 2001, it became clear that the utilities were unable to procure electricity in wholesale markets or satisfy the obligation to serve their customers.

On Jan. 17, 2001, Gov. Davis, in response to the continued dete-



rioration in the utilities' financial condition, proclaimed a state of emergency and ordered CDWR to begin procuring power for the IOUs' customers. CDWR was given authority to purchase power to satisfy a portion of the "net short," i.e. the difference between the power the utilities could provide from their own resources, and the total consumer demand at any given time. In other words, because of the utilities' failure to provide electric service, CDWR was forced to step in as an alternate electric service provider "to assist in mitigating the effects of this emergency."³⁷

Two days later, the California legislature passed Senate Bill 7X, which authorized CDWR

to purchase electrical power and to provide that power at cost to customers. This authority was to extend for no more than 12 days from S.B. 7X's effective date. S.B. 7X, which became effective Jan. 19, 2001, provided two sources of funds. First, it advanced CDWR \$400 million from the State General Fund to pay for CDWR's electricity purchases. It also required the CPUC to adopt and implement emergency regulations to provide for payment mechanisms for bundled customers to pay for power purchased by CDWR on their behalf.³⁸ On Jan. 31, 2001, the CPUC issued D.01-01-016 in response to its obligations under S.B. 7X. The decision required that a percentage of the amount that bundled customers then currently paid the IOUs for electricity would be paid to CDWR.³⁹

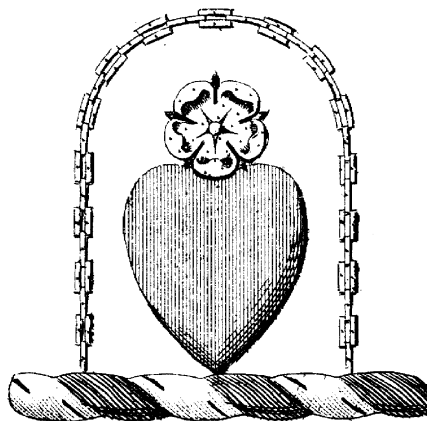
D.01-01-061 also established that CDWR should sell power directly to retail end-use customers as opposed to making direct or indirect sale to the ISO or public utilities. In ordering this action, the CPUC determined that CDWR was not a public utility, nor was it imposing an obligation to serve upon CDWR.⁴⁰ The CPUC ordered the utilities to deliver the electric power purchased by CDWR to customers, but held that CDWR would at all times maintain ownership of the electric power it purchased until it was sold to the retail end-use customer.⁴¹

The 12-day period covered by S.B. 7X expired, but the utilities continued to be unwilling or

unable to satisfy their public utility obligations. On Feb. 1, 2001, one day after the expiration of S.B. 7X, A.B. 1X became effective. The declared purpose of A.B. 1X was to provide a creditworthy buyer to purchase electricity for bundled customers in place of the insolvent utilities. Pursuant to A.B. 1X, CDWR was granted authority to purchase power necessary to meet the net short through Jan. 1, 2003. The CPUC recognized that "A.B. 1X is permissive, not mandatory, with regard to CDWR's authority to purchase power for utility's customer's use" and concluded that nothing in A.B. 1X relieved the utilities of its statutory duty to serve. The CPUC stated: "We cannot and will not relieve [the utilities] of that fundamental obligation."⁴²

A.B. 1X expanded the funding options available to CDWR. It authorized CDWR to issue bonds and to enter into contracts to purchase electricity. It provided that the power that CDWR purchased would be sold to bundled customers⁴³ and that payment to CDWR was a direct obligation of the bundled customer.⁴⁴ In furtherance of A.B. 1X, the Commission approved payment mechanisms for bundled customers to pay for the power received from CDWR.⁴⁵ In the summer of 2001, CDWR executed a series of long-term contracts with an approximate value of \$42.9 billion, with deliveries scheduled primarily over the next 10 years.

Thereafter, on Feb. 22, 2002, the CPUC issued D.02-02-051, adopting a "Rate Agreement" between the CPUC and CDWR. The Rate Agreement established a framework for discharging the CPUC's obligation under A.B. 1X to impose charges on bundled customers sufficient to meet CDWR's revenue requirement. The Rate Agreement established



that the CPUC would impose two charges on bundled customers: a "Bond Charge" and a "Power Charge." The Bond Charge would pay for or provide payment for the payment of any costs related to bonds issued by CDWR pursuant to its authority under A.B. 1X. The Power Charge would pay for the cost that CDWR incurred to procure and deliver power.⁴⁶

In November 2002, CDWR completed the issuance of \$11.3 billion in revenue bonds. The proceeds from the bonds were used to pay off both the General Fund advances and an interim bridge loan that CDWR had procured. The remaining funds were used to meet CDWR's

obligations under both the procurement contracts it had entered into as well as repayment of the bonds themselves.

The power that CDWR purchased both in the short term and under the long-term contracts proved to be very expensive. California customers will be saddled with significant costs for more than a decade to pay off the Bond Charge and the Power Charge. Recent filings with the CPUC indicate that the above-market costs of the contracts executed by CDWR total \$7.4 billion.⁴⁷ This is in addition to the \$11.3 billion in revenue bonds to pay for power purchases during the pendency of the energy crisis.

IV. Did the Utilities Breach Their Obligation to Serve?

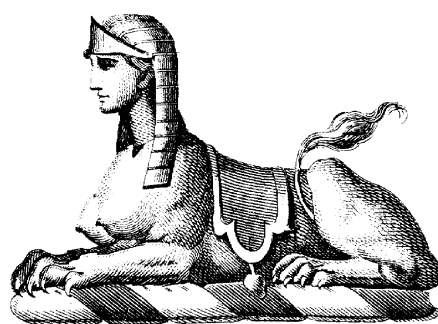
There is no doubt that the utilities failed to supply electricity to meet the full electric requirements of their customers. There is also no doubt that because of these failures, CDWR was forced to procure electricity to meet the demands of the IOUs' customers. The question therefore becomes whether the IOUs breached their obligations to serve. The answer to this question is complex. On the one hand, the CPUC has held that a threatened bankruptcy filing or the threat of insolvency does not alter a utility's obligation to serve its customers.⁴⁸ "We cannot and will not relieve [the utilities] of that fundamental obligation."⁴⁹ And, the Commission also has

held that utilities should procure resources consistent with their statutory obligation to serve their customers.⁵⁰ On the other hand, a public utility's obligation to serve does not mean that it is an insurer or guarantor of service.⁵¹ But *Langley* still requires an IOU to exercise reasonable care in operating its system to avoid unreasonable risks of harm to the persons and property of its customers.⁵² The fact that the interruption in service may have been caused or exacerbated by actions of a third party does not necessarily insulate the utility from liability for failure to carry out its public utility obligation.⁵³ So, whether the utilities breached their obligation to serve depends on whether they can demonstrate that they took reasonable care to avoid unreasonable risks of harm to their customers. While the exercise of reasonable care may not have altogether prevented the energy crisis, it may have had the salutary effect of mitigating the resulting harm to electric customers. Set forth below are six instances where it appears that the utilities failed to do so.

A. Did the utilities exercise reasonable care to avoid unreasonable harm to their customers by deliberately under-scheduling their loads in the day-ahead market?

As discussed above, until additional authority was granted by the CPUC, California's regulatory scheme required the

IOUs to sell to the Cal PX on a daily basis the power that they generated and the power they acquired under historical contracts and to purchase their additional electricity requirements from the Cal PX. The Cal PX basically offered two types of short-term products: electricity that could be purchased from the day-ahead market and electricity



from the hour-ahead market. Any additional electricity that was needed to keep the electric system in balance was purchased by CAISO in a real-time market, with the costs later passed on to the IOUs and other load-serving entities.

In undertaking their duties to procure electricity for their bundled customers, at an early juncture the IOUs adopted a strategy of lowering, and some might say "manipulating," the market price for electricity by not bidding their entire forecasted demand for the next day into the day-ahead market, but instead relying on the hour-ahead market and the CAISO's real-time market to satisfy some of their demand.

This strategy put upward pressure on real-time market prices and jeopardized reliability of service.

In a report issued by CAISO to the Federal Energy Regulatory Commission (FERC) on Sept. 6, 2000, CAISO asserted that excessive under-scheduling by utilities had created a reliability threat, and concluded that the volume of recent purchases in the ISO's real-time market far exceeded the original market design, often equaling 20 to 30 percent of the total market demand rather than the 5 percent of the total demand that the market's designers had envisioned. As some commentators have observed, the practice of some generators to under-schedule generation in the day-ahead market may first have developed in reaction to the utilities' under-scheduling of load and frustration with CAISO's failure to take more timely steps to address it.

Soon after, on Dec. 15, 2000, FERC responded to the report.⁵⁴ FERC expressed concern that "the ISO was being forced to supply a large portion of California's load at the last minute as the supplier of last resort. System operations were jeopardized as the ISO was effectively transformed from providing the imbalance services needed for reliable transmission to the supplier of last resort."⁵⁵ To address what it saw as the problem of chronic under-scheduling, FERC decided to impose a penalty on IOUs that failed to purchase at least 95 percent of their forecast demand in the Cal PX's day-ahead market.

The CPUC itself has emphasized that load under-scheduling is not an acceptable practice. After reaffirming the IOU's obligation to procure electricity for its customers, the Commission emphatically stated:

[W]e recognize that the CAISO has the authority to procure resources (e.g. RMR [reliability must run] contracts, other types of contracts, must-offer provisions of the CAISO tariff). It is our position, however, that these CAISO tools should not be used to supplant the utility's obligation to procure resources to meet its customer's needs. Rather, the CAISO procurement authority should be a backstop reliability tool.⁵⁶

Query: Did the IOUs exercise reasonable care to avoid unreasonable risk of harm to their customers by deliberately under-scheduling customer demand in the Cal PX's day-ahead market?

B. Did the utilities exercise reasonable care to avoid unreasonable risks of harm to their customers by failing to implement the expanded procurement authorization granted by the CPUC?

As discussed previously, the electric utilities' initial response to the burgeoning energy crisis was to ask the CPUC for greater flexibility to purchase electricity. They wanted approval to buy energy from entities other than the Cal PX and for periods greater than the short-term products offered by the Cal PX. On July 8, 1999, only about five weeks after energy prices started to escalate,

the CPUC offered its first response. It adopted Resolution E-3618, which approved rate-making for PG&E's and SCE's participation in the Cal PX's "block forward" markets. Resolution E-3618 authorized PG&E and SCE to engage in block forward transactions up to one-third of their historic minimum hourly loads by month.



Two weeks later, PG&E and SCE filed Emergency Motions seeking additional authorization from the CPUC to enter into future bilateral contracts with protection against rate disallowances, claiming that emergency consideration was needed to better hedge against the risk of price spikes during high load conditions and to introduce new supply into California. In its Emergency Motion, SCE requested that for near-term contracts, all power deliveries would be considered reasonable per se unless their average cost, over the course of an annual period, exceeded by 20 percent the average cost of SCE's Cal PX and CAISO portfolio, in which

case a reasonableness review would be triggered. For medium-term contracts, SCE would engage in purchases only if an *ex parte* determination of reasonableness had been obtained from the CPUC's Energy Division.

On Aug. 3, 2000, the CPUC granted the utilities' Emergency Motions with certain modifications.⁵⁷ D.00-08-023 authorized SCE to enter into bilateral contracts for power. For near-term contracts, the CPUC lowered the reasonableness review trigger from 20 to 5 percent. The CPUC approved the pre-approval process which SCE had proposed for medium-term bilateral contracts. This authority was affirmed and broadened in CPUC Resolution E-3723, issued Dec. 21, 2000.

For the most part, PG&E and SCE elected not to utilize the full authority granted by these CPUC resolutions and decisions. Apparently, PG&E and Edison were dissatisfied with the limits for after-the-fact reasonableness review set by the CPUC. Instead, both PG&E and SCE decided to reduce the risk of disallowance upon their shareholders by continuing to rely extensively upon the Cal PX spot market and the CAISO as a source of power since purchases from these sources were deemed to be per se reasonable.

Query: Did the IOUs exercise reasonable care to avoid unreasonable risk of harm to their customers by choosing not to implement the additional authority provided to them by the CPUC to enter into long-term

contracts, even if the utilities would be subject to after-the-fact reasonableness review? Was it in the best interest of the utility's customers to continue to disproportionately rely on spot market purchases?

C. Did the utilities exercise reasonable care to avoid unreasonable harm to their Customers by failing to enforce the first-priority obligation?

In the late 1980s and 1990s, each of the major California electric utilities petitioned the CPUC for authorization to reorganize under a holding company structure. In each instance, the CPUC authorized the reorganization, subject to certain terms and conditions.⁵⁸ One such term and condition which was common to the approval for all three utilities was a condition known as the "first-priority condition." The first priority condition imposed by the CPUC as a condition of its approval and accepted by SCE and its parent Edison International Corporation states: "The capital requirements of the utility, as determined to be necessary to meet its obligations to serve, shall be given first priority by the Board of Directors of [the holding company] and Edison."⁵⁹ The first-priority condition for PG&E is slightly different, but the import is the same. It states: "The capital requirements of PG&E, as determined to be necessary and prudent to meet the obligation to serve or to operate the utility in a

prudent and efficient manner shall be given first priority by PG&E Corporation's Board of Directors."⁶⁰

As noted previously, from the commencement of restructuring in early 1998 through 2000, the electric IOUs disbursed billions of dollars to their parent corporations through dividends and the repurchase of



common equity. With the advent of the energy crisis, the utilities became desperate for money to purchase power to meet their public utility obligations to serve. Yet, at the same time, they continued for a period to dividend money to their parent companies.⁶¹ By late 2000, the utilities were insolvent and claimed that they lacked the funds to purchase electricity to fulfill their obligation to serve. Still, they refused to call upon their parent corporations to fulfill the first-priority condition.

In April 2001, the CPUC responded by issuing an Order Instituting Investigation ("OII") directing the holding companies to demonstrate why

their "evident failure to provide sufficient capital to their utility subsidiaries to alleviate or mitigate the subsidiaries' need for capital during that time period did not violate, and does not continue to violate the 'first priority' condition. . . ."⁶² Rather than responding, the holding companies moved to dismiss the investigation against them for lack of jurisdiction.

In a Jan. 9, 2002 decision, the CPUC denied the motions to dismiss and provided an interim opinion on the meaning of the first priority condition.⁶³ The CPUC found that the condition's reference to capital must be interpreted expansively and not just limited to equity capital or to investment in the utilities' plants and equipment as the utilities had claimed. It found that under certain circumstances, "the condition includes the requirement that the holding companies infuse all types of 'capital' into their respective utility subsidiaries when necessary to fulfill the utility's obligation to serve."⁶⁴ The CPUC, however, made no finding at that time that the holding company or utility had actually violated the first-priority condition.⁶⁵

In a separate action brought by the Attorney General of California, it has been determined that the right to enforce the first priority condition rests with the utility itself. Here, for reasons known only to them,

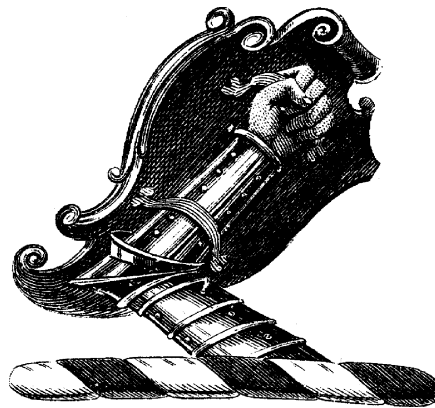
none of the IOUs ever called upon their parent to enforce their promise.⁶⁶ As a result, while the parent companies had received enormous sums from the utilities, they never were called upon to help their subsidiary electric utilities meet the financial demands of the energy crisis.

Query: Did the IOUs exercise reasonable care to avoid unreasonable risk of harm to their customers by failing to require their parent corporations to comply with the first-priority condition?

D. Did the utilities exercise reasonable care to avoid unreasonable risks of harm to their customers by failing to use the emergency rate increases granted by the CPUC for procurement?

As previously discussed, in January 2001, the CPUC temporarily increased electric rates for bundled and direct access customers by 1 cents per kW h. This rate increase was made permanent as part of the Commission's April 2001 decision increasing rates by an additional 3 cents per kW h. While the 1 cent increase was insufficient to cover escalating wholesale electric costs, the utilities did not even attempt to use it for the intended purpose prescribed in the CPUC's decisions approving the surcharges. They could have chosen to pay all suppliers in part, or a few suppliers in full, in order

to minimize the net short that had to be supplied by CDWR. But instead, evidence suggests that the utilities chose simply to keep the increase to build up their own cash reserves. The same is true for the April 2001 3 cents per kW h rate increase. While a large portion of that rate increase to bundled customers was earmarked by the CPUC to pay



CDWR for its costs of acquiring electricity, the utilities retained the remainder to build up their own cash reserves. The utilities did not try to use the cash from this rate increase to purchase electricity on its own and thereby reduce the amount of electricity that CDWR was forced to purchase to satisfy the net short, which ironically had been caused by the utilities' failure to satisfy their obligations to serve.

Query: Did the IOUs exercise reasonable care to avoid unreasonable risk of harm to their customers by keeping for their own corporate purposes all or part of the two rate increases

intended to purchase power and lighten the CDWR's burden?

E. Did the utilities exercise reasonable care to avoid unreasonable risks of harm to their customers by failing to pay PX credits, thereby increasing the utilities' own bundled service requirements?

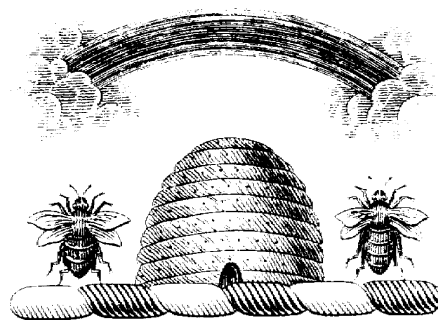
Under California's deregulated market structure, customers that received direct-access service were entitled to receive a credit on their monthly bills equal to the cost of power that the IOUs would have purchased from the Cal PX to serve them, minus certain costs. The credit, known as the PX Credit, recognized that those utility customers which took direct-access service were procuring their own power and, therefore, the utility should not receive payment for the commodity portion of bundled service. As originally conceived, the PX Credit was used to reduce the customer's bill, but that bill could never be less than zero. However, in a settlement reached in 1999, which was expressly approved by the CPUC,⁶⁷ the utilities agreed that the PX Credit theoretically could be greater than the frozen rate and therefore, agreed to waive the floor.

When the energy crisis arrived in 2000, the theoretical became the actual: Cal PX energy costs skyrocketed, causing PX Credits to exceed frozen tariff rates. In some months, PX Credits to direct access customers were greater

than the total bill rendered by the utility acting as a utility distribution company. For a period of time, both PG&E and SCE continued to pay the PX Credits in compliance with the settlement. Commencing in late 2000 and early 2001, however, PG&E and SCE, in violation of the settlement order, each stopped making payments of PX Credits to direct-access customers' ESPs under consolidated billing arrangements. Even after being notified of the utilities' suspension of PX Credits, the CPUC took no action to enforce its June 1999 Order. In contrast to direct access customers, bundled customers continued to receive the benefit of the capped rates and effectively were immunized from the effect of the suspension of PX Credits to ESPs.

Unlike the utilities that had not mitigated or hedged the risk of their wholesale electric purchases, many of the ESPs used the PX Credit as a hedge against escalating energy prices. While the ESPs had to purchase electricity in energy crisis markets, the PX Credit acted as a hedge because it tended to increase as there were increases in wholesale markets. When the IOUs stopped making these payments, the ESPs' hedge was suddenly eliminated. Consequently, the ESPs had no other choice but to return their direct access customers to utility bundled service. The utility, as the supplier of last resort, immediately saw its own loads increase significantly. By failing to pay PX Credits, in violation of the June

1999 settlement order, the utilities shifted this entire burden to CDWR, thereby increasing the amounts owed to CDWR by all customers, including direct-access customers. Moreover, the utilities' action could be construed as interfering with the contracts between ESPs and their customers for direct-access service.



The IOUs' choice to selectively suspend payments to ESPs is remarkable for yet other reasons. ESPs represent a potent source of competition to IOUs. By selectively choosing not to pay ESPs for the power delivered to direct-access customers, the IOUs could effectively eliminate significant competitors and solidify their monopoly positions. As noted below, the anti-competitive impacts of the nearly simultaneous decisions of SCE and PG&E to interrupt the payment of PX Credits were magnified by their virtually contemporaneous decisions to also stop paying QFs for their power supplied to the IOUs, drastically weakening their main

competitors in the power generation market.

Query: Did the IOUs exercise reasonable care to avoid unreasonable risks of harm to their direct-access customers by refusing to pay PX Credits in violation of D.99-06-058?

F. Did the utilities exercise reasonable care to avoid unreasonable risks of harm to their customers by failing to pay QFs?

Under PURPA and its implementing regulations issued by FERC, a utility is required by law to purchase power from QFs at the utility's avoided costs. Since the mid-1980s California IOUs had entered into a series of standard offer contracts with QFs and by the commencement of deregulation, QF generated power represented a substantial portion of the IOU's generation portfolio.

But the energy crisis and the utilities actions threw this program into disarray. In 2000, as energy costs escalated, the price for QF power also increased, and in late 2000 and early 2001, the IOUs simply ceased paying QFs. This was done, even though under California's deregulation structure the utilities were required to bid electricity generated from QF contracts into the Cal PX market as part of their own utility retained generation and were paid the market-clearing price for it. As a result of the IOUs' actions, many of the QFs either sought to terminate their contracts with the utilities or

suspended operations, and a few of them were forced into bankruptcy, unable to pay for fuel and other operating costs. This put more pressure on CDWR to purchase additional electricity, at least in the short run. Eventually, the utilities settled the QF lawsuits regarding non-payment by entering into contract amendments providing for a 5.37 kW h fixed energy price over a five-year period. But, as with the selective cessation of payments to ESPs, stopping payments to QFs had the effect of putting additional financial pressure on competitors, thereby presenting the opportunity to the IOUs to solidify their monopoly positions.

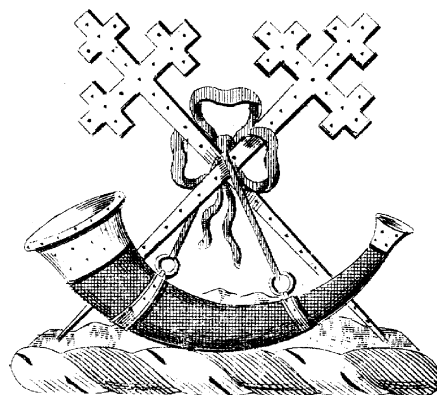
Query: Did the IOUs exercise reasonable care to avoid unreasonable risks of harm to their customers when they ceased paying QFs for electricity, driving some QFs out of business and forcing others to terminate contracts and/or accept contractual amendments at high prices?

G. Conclusion

In each of the six circumstances discussed above the electric utilities arguably failed to fulfill their obligations to serve. To the extent the utilities breached their obligation to serve, customers may seek relief in court for breach of contract, violations of CPUC orders, and implied equitable indemnity relating to their payment of surcharges resulting from the utilities' breaches. Whether the utilities exercised reasonable care in operating their systems to

avoid unreasonable risks of harm to the persons and property of their customers can only be answered by a court after carefully evaluating all of the evidence.

V. The Effect of the CPUC Settlements and PG&E Bankruptcy



In October 2001, SCE and the CPUC entered into a settlement agreement, whereby in exchange for SCE dropping its lawsuit against the CPUC,⁶⁸ the CPUC agreed to take certain actions designed to restore SCE to financial health. It allowed SCE to continue to collect revenues from rates that were set at artificially high levels until SCE collected certain procurement related liabilities that were set forth in a Procurement Related Obligations Account, or "PROACT." As finally agreed upon, the PROACT account opening balance was approximately \$3.3 billion. SCE's parent, Edison International, was not a signatory to the settlement agreement and the agreement

specifically provides that there are no third-party beneficiaries to the agreement.⁶⁹

PG&E charted a significantly different course of action than SCE. On Apr. 7, 2001, PG&E filed for bankruptcy, thereafter proposing a very aggressive reorganization plan that would have removed many of its assets from CPUC jurisdiction. PG&E, like SCE, also had filed a lawsuit against the CPUC claiming that it was entitled to reflect the cost of the wholesale power purchases in its rates, despite California's deregulation scheme which froze retail rates, and despite the fact that PG&E had already recovered billions of dollars through CTC headroom prior to the energy crisis. On June 19, 2003, PG&E, the CPUC, and PG&E's parent, PG&E Corporation, announced a settlement. In exchange for resolving the competing plans for reorganization in the utility's Chapter 11 proceeding and ending litigation between PG&E and the CPUC related to the energy crisis, the settlement adopted a plan whose declared goal was to return PG&E to financial health. In addition, the CPUC agreed to release all claims against PG&E Corporation related to past utility holding company actions. Again, like the SCE settlement, PG&E was allowed to retain rates at artificially high levels for a significant period of time into the future. In addition, however, PG&E was allowed to create a new \$2.21 billion "regulatory asset" that would be recovered in electric rates over the next nine years. As

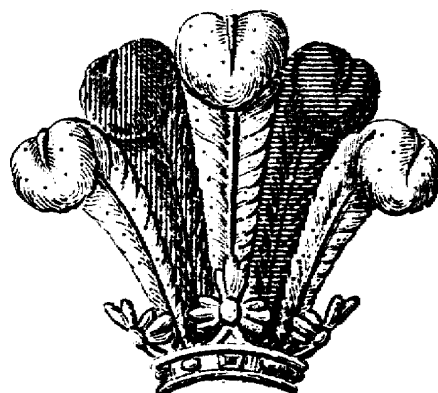
originally proposed, PG&E would be allowed to earn its rate of return on the regulatory asset. A subsequent settlement allowed for the recovery of the regulatory assets through a dedicated rate.⁷⁰ The CPUC approved the settlement in December 2003.⁷¹ Thereafter, the bankruptcy court issued an order confirming the plan of reorganization and approving the settlement agreement.⁷² Consistent with the provisions of the reorganization plan, PG&E released PG&E Corporation and its directors from any claims that it might have for restitution.⁷³

The Public Utilities Code provides customers that have been injured by a utility's unlawful actions with an independent cause of action. California Business and Professions Code Section 17200 further reinforces these remedies. However, PG&E will undoubtedly try to argue that this remedy may not be available for reasons linked to PG&E's bankruptcy. Although the bankruptcy area is beyond the expertise of the authors of this article, PG&E will likely contend that failure to submit a claim in PG&E's bankruptcy proceeding operates to limit or preclude recourse against PG&E. In turn, PG&E's defense may have been weakened by failing to notify customers of its bankruptcy. These issues are beyond the scope of this article.

In addition, while PG&E Corp. is not technically protected by a bankruptcy filing, it may attempt to capitalize on the fact that it was a party to the

settlement with the CPUC, which was approved by the Bankruptcy Court. Furthermore, PG&E has apparently waived its individual claims for restitution against its parent, including any claim that it might have for violation of the first-priority condition.⁷⁴

SCE, on the other hand, did not file for bankruptcy and thus, unlike PG&E, cannot claim



whatever shield that bankruptcy protection might provide to PG&E. Nor was Edison International a party to the settlement with the CPUC. As a result, SCE and Edison International do not have the protections that may be enjoyed by PG&E and its parent from suits by customers that were injured by the utility's failure to carry out its obligation to serve.

VI. Conclusion

For the last decade and continuing to today, California's IOUs have frequently relied upon the "the duty or obligation to serve" as the means for obtaining valuable concessions from the Cali-

fornia legislature and Public Utilities Commission. The utilities have exploited this regulatory principle as one of their primary weapons to justify billions of dollars of rate recovery and concessions. It is clear, however, that the duty to serve is not a saber which is only available to the utilities. Rather, the duty to serve is a double-edged sword that might equally be brandished by ratepayers. It is a potent weapon which provides ratepayers with an independent cause of action to ensure that California's electric utilities did not violate their duty to exercise reasonable care to avoid unreasonable risks of harm to their customers.

Endnotes:

1. Decision 95-12-063 (as modified in D.96-01-009), 1996 Cal. PUC LEXIS 28, at *55-56, 84 (Jan. 10, 1996) (asterisks represent LEXIS cross-reference page citation).
2. D.96-04-054, 1996 Cal. PUC LEXIS 274, at *6 (Apr. 10, 1996).
3. See D.03-07-030, 2002 Cal. PUC LEXIS 988, at *1 (July 10, 2003).
4. D.03-07-028 (limited rehearing granted in D.03-08-076 (Aug. 7, 2003)), 2002 Cal. PUC LEXIS 989, at *46, 52, 68, 74 (July 10, 2003).
5. D.03-04-030, 2003 Cal. PUC LEXIS 246, at *64 (Apr. 3, 2003).
6. D.03-12-059, 2003 Cal. PUC LEXIS 608, at *34 (Dec. 18, 2003).
7. 21 Energy L.J. 27 (2000).
8. *Id.*, at 30.
9. Cal. Pub. Util. Code § 451 (Deering 2004). See also Cal. Pub. Util. Code §§ 761, 762, 768 and 770 (Deering 2004).
10. *The Duty of a Public Utility to Render Adequate Service: Its Scope and Enforcement*, 62 COLUM. L. REV. 312 (1962).

11. *Id.*, at 312–13.

12. PG&E's Rule 14 is similar. It states:PG&E will exercise reasonable diligence and care to furnish and deliver a continuous and sufficient supply of electric energy to the customer, but does not guarantee continuity or sufficiency of supply. PG&E will not be liable for interruption or shortage or insufficiency of supply, or any loss or damage of any kind of character occasioned thereby, if same is caused by inevitable accident, act of God, fire, strikes, riots, war, or any other cause except that arising from its failure to exercise reasonable diligence.

13. 262 P.2d 846 (Cal. 1953).

14. *Langley*, 262 P.2d at 849 (emphasis added).

15. *Mobil Oil Corp. v. S. Cal. Edison Co.*, No. B145834, 2003 Cal. App. Unpub. LEXIS 595 (Cal. Ct. App. 2d Jan. 21, 2003).

16. *Id.*, at *38.

17. *Id.*, at *22–24 (citations omitted).

18. *Id.*, at *30–31 (citations omitted).

19. D.04-07-028, at 7–8 (July 8, 2004).

20. Public Utility Code § 2106 states:Any public utility which does, causes to be done, or permits any act, matter, or thing prohibited or declared unlawful, or which omits to do any act, matter, or thing required to be done, either by the Constitution, any law of this State, or any order or decision of the commission, shall be liable to the persons or corporations affected thereby for all loss, damages, or injury caused thereby, or resulting therefrom. If the court finds that the act or omission was willful, it may, in addition to the actual damages, award exemplary damages. An act to recover for such loss, damage, or injury may be brought in any court of competent jurisdiction by any corporation or person.

21. 262 P.2d at 850.

22. *Mobil Oil Corp.*, 2003 Cal. App. Unpub. LEXIS at *37.

23. See D.95-12-063 (as modified by D.96-01-009), 1996 Cal. PUC LEXIS 28 (Jan. 10, 1996).

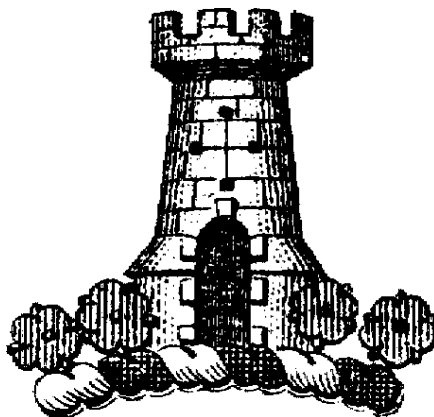
24. A.B. 1890, Ch. 854 (1996).

25. Cal. Pub. Util. Code § 368 (Deering 2004).

26. D.01-01-018, 2001 Cal. PUC LEXIS 44, at *23 (Jan. 4, 2001).

27. D.99-05-051, 1999 Cal. PUC LEXIS 291, at *1 (May 27, 1999).

28. D.00-12-067, 2000 Cal. PUC LEXIS 992, at *1 (Dec. 21, 2000)



(acknowledging that there is an "extraordinary and unforeseen crisis in wholesale and retail electric power markets in California").

29. D.01-01-018, 2001 Cal. PUC LEXIS 44, at *2 (Jan. 4, 2001).

30. D.01-03-018, 2001 Cal. PUC LEXIS 44, at *2 (Jan. 4, 2001).

31. D.01-03-082, 2001 Cal. PUC LEXIS 217, at *1 (Mar. 27, 2001).

32. *Id.*

33. D.01-01-046, 2001 Cal. PUC LEXIS 35, at *25 (Jan. 19, 2001).

34. *Id.*, at *1.

35. *Id.*, at *10, 23.

36. D.01-07-033, 2001 Cal. PUC LEXIS 877, at ¶1 (July 12, 2001).

37. Press Release, Executive Department, State of California, Proclamation by the Governor of the State of California (Jan. 17, 2001).

38. Cal. Water Code § 200 (Deering 2001) (repealed 2001).

39. D.01-01-061, 2001 Cal. PUC LEXIS 30, at *5 (Jan. 31, 2001).

40. *Id.*

41. *Id.*, at *3.

42. D.01-03-082, 2001 Cal. PUC LEXIS 217, at *79 (Mar. 27, 2001).

43. Cal. Water Code § 80002.5 (Deering 2004).

44. Cal. Water Code § 80104 (Deering 2004).

45. See D.01-03-081, at attachments B, C, D, and E (Mar. 29, 2001).

46. D.02-02-051, 2002 Cal. PUC LEXIS 170, at *1–2 (Feb. 21, 2002).

47. In a recent Settlement Agreement filed with the CPUC, it is proposed that PG&E be assigned \$43.2 billion of this total, SCE \$3.1 billion and SDG&E \$1.0 billion. See Application 00-11-038, Motion to Adopt Settlement Agreement (Apr. 22, 2004).

48. D.01-01-046, 2001 Cal. PUC LEXIS 35, at *1 (Jan. 19, 2001).

49. D.01-03-082, 2001 Cal. PUC LEXIS 217, at *79 (Mar. 27, 2001).

50. D.04-07-028, at 7 (July 8, 2004).

51. See *Langley*, 262 P.2d at 849.

52. *Id.*

53. See *Mobil Oil. Corp.*, 2003 Cal. App. Unpub. LEXIS at *30–31.

54. See *San Diego Gas and Elec. Co.*, 93 F.E.R.C. ¶ 61,294, 2000 FERC LEXIS 2491 (Dec. 15, 2000).

55. *Id.*, at ¶ 61,993.

56. D.04-07-028, at 8 (July 8, 2004).

57. D.00-08-023, 2000 Cal. PUC LEXIS 555, at *10–12 (Aug. 3, 2000).

58. The CPUC has approved each IOU's reorganization plan. See D.88-01-063, 1988 Cal. PUC LEXIS 2 (Jan. 28, 1988) (SCE); D.95-12-618, 1995 Cal. PUC LEXIS 931 (Dec. 6, 1995) (SDG&E); D.96-11-017, 1996 Cal. PUC LEXIS 1141 (Nov. 6, 1996), *aff'd*, 1999 Cal. PUC LEXIS 242 (Apr. 22, 1999) (PG&E).

59. The first-priority condition imposed for the SDG&E

reorganization was virtually the same as SCE's.

60. D.96-11-017, 1996 Cal. PUC LEXIS 1141, at *50 (Nov. 6, 1996).

61. California Corporations Code § 500 sets forth certain requirements that must be met before dividends can be declared and § 501 prohibits any distribution to the corporation's shareholders if the corporation or the subsidiary making the distribution is, or as a result thereof would be, likely to be unable to meet its liabilities (except those whose payment is otherwise adequately provided for) as they mature. Cal. Corp. Code §§ 500-01 (Deering 2004).

62. Investigation No. 01-04-002, 2001 Cal. PUC LEXIS 405, at *24 (Apr. 3, 2001).

63. On June 21, 2004 the CPUC's jurisdiction was affirmed on appeal.

64. D.02-01-039, 2002 Cal. PUC LEXIS 5, at *2 (Jan. 9, 2002).

65. On June 21, 2004, the Court of Appeals affirmed the CPUC's finding that it had jurisdiction over the parent holding companies for purposes of enforcing the first-priority condition.

66. On Apr. 12, 2004, as part of the approval of its reorganization plan, PG&E released PG&E Corporation and its directors from any claims that it might have had for restitution. In addition, as part of its Settlement with PG&E and its parent, the CPUC released both for past holding company actions during the energy crisis.

67. See D.99-06-058, 1999 Cal. PUC LEXIS 316, at *27-28 (June 10, 1999).

68. See *S. Cal. Edison Co. v. Lynch*, No. CV-00-12056-RSLW (C.D. Cal. Nov. 13, 2000).

69. Settlement Agreement, Section 5.5, at 24.

70. In early June 2004, the Governor signed S.B. 772, ch. 46, authorizing a

dedicated rate component to securitize PG&E's newly formed \$2.21 billion regulatory asset.

71. D.03-12-035, 2002 Cal. PUC LEXIS 1051 (Dec. 18, 2003).

72. Amended Memorandum Decision Approving Settlement Agreement and Overruling Objections to Confirmation of Reorganization Plan, U.S. Bankruptcy Court, Northern District of California, No. 01-30923DM, Jan. 5, 2004.

73. See PG&E Corporation Form 8-K filed with the Securities Exchange Commission on May 25, 2004.

74. One still might argue whether PG&E was using reasonable care to avoid unreasonable harm to its customers when it waived any claim against its parent. The Bankruptcy Court addressed this action. See *In re Pac. Gas and Elec. Co.*, 304 B.R. 395, 416-19 (Bankr. N.D. Cal. 2004).



The Public Utilities Code provides customers that have been injured by a utility's unlawful actions with an independent cause of action.