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7 PACIFIC GAS AND ELECTRIC COMPANY

8  
9 UNITED STATES BANKRUPTCY COURT  
10 NORTHERN DISTRICT OF CALIFORNIA  
11 SAN FRANCISCO DIVISION

12 In re

13 PACIFIC GAS AND ELECTRIC  
COMPANY, a California corporation,

14 Debtor.

15  
16 Federal I.D. No. 94-0742640  
17

No. 01-30923 DM

Chapter 11 Case

Date: April 17, 2002

Time: 9:30 a.m.

Place: 235 Pine St., 22nd Floor  
San Francisco, California

Judge: Hon. Dennis Montali

18  
19 DECLARATION OF KEVIN DASSO IN SUPPORT OF DEBTOR'S MOTION  
20 FOR ORDER APPROVING EXPENDITURE OF FUNDS TO CONSTRUCT  
21 THE NORTHEAST SAN JOSE TRANSMISSION REINFORCEMENT PROJECT  
22  
23  
24  
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26  
27  
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Acc Add: RidsOgcMadCenter

1 I, Kevin Dasso, declare as follows:

2 1. I am the Director of the Pacific Gas and Electric Company ("PG&E")  
3 Electric Transmission and Distribution Engineering Department, a position I have held since  
4 November 1999. I make this Declaration based upon my personal knowledge of the  
5 Northeast San Jose Transmission Reinforcement Project (the "NESJ Project"), and upon my  
6 review of PG&E's records concerning the matters stated herein. If called as a witness, I  
7 could and would testify competently to the facts stated herein.

8 2. The purpose of the NESJ Project is to build electric transmission facilities to  
9 serve electric customers in the cities of San Jose, Santa Clara and Milpitas and the Silicon  
10 Valley (collectively the "San Jose area").

11 3. The San Jose area has key businesses and industries affecting the overall  
12 California economy. With only a small number of electric generation facilities in the area,  
13 PG&E relies heavily on its electric transmission facilities to import power to serve customer  
14 demand.

15 4. Before the recent energy crisis and current economic downturn, the San  
16 Jose area had been experiencing high economic expansion and electric demand growth.  
17 Between the years 1995 and 2000, peak electric demand grew from 1,320 megawatts  
18 ("MW") to 1,900 MW, or an average of 100 MW per year.

19 5. Electric demand, while lower in 2001, is expected to grow at or near the  
20 previous pace in the longer term with the recovery of the California economy. The loadings  
21 on several local 115 kilovolt ("kV") power lines and transformer equipment at PG&E's  
22 Newark and Metcalf substations are expected to exceed their capability by 2002 or 2003,  
23 depending upon the pace of economic recovery. Other 115 kV lines in south San Jose are  
24 also loaded at or close to their capability.

25 6. The California Independent System Operator ("ISO") has concluded that  
26 the transmission system in the northeast San Jose area was in violation of the ISO grid  
27 planning criteria for reliability in the summers of 2000 and 2001. To support the load  
28

1 growth and correct violations of the ISO reliability criteria, the ISO has found, and the  
2 California Public Utilities Commission ("CPUC") has agreed, that substantial additions to  
3 PG&E's transmission system will be required to be in place by 2003 to meet demand and  
4 ensure system reliability.<sup>1</sup>

5 7. The NESJ Project has been designed to solve transmission deficiencies in  
6 the San Jose area. To complete the NESJ Project as approved by the CPUC, PG&E will:  
7 acquire 20 acres of land and construct a new transmission substation, Los Esteros, with three  
8 420 MVA transmission transformers, capacitors and other electric equipment; construct  
9 approximately 7.3 miles of 230 kV double circuit transmission line (2.8 miles of  
10 underground and 4.5 miles of overhead); construct approximately 1.5 miles of 115 kV power  
11 line and reconfigure existing 115 kV power lines to make four additional 115 kV  
12 connections to Los Esteros substation; and install equipment and make required upgrades at  
13 substations impacted by the NESJ Project.

14 8. PG&E originally scheduled construction on the NESJ Project to begin in  
15 2001 so that the Project would become operational in June 2002. Because of delays in the  
16 CPUC proceedings, the NESJ Project currently is behind schedule. To meet the relevant  
17 operational deadlines for 2003, construction must begin no later than May 1, 2002.

18 9. In February 1997, PG&E's Board of Directors approved an appropriation of  
19 \$71 million to fund PG&E's proposed NESJ Project.

20 10. In July 1998, PG&E submitted an application to the CPUC for a CPCN  
21 authorizing the construction of the NESJ Project. After consultation with the Don Edwards  
22 San Francisco Bay National Wildlife Refuge, PG&E re-filed its CPCN application with a  
23 different proposed route in September 1999.

24 11. The CPUC conducted evidentiary hearings regarding the NESJ Project in  
25

26  
27 <sup>1</sup> Pursuant to the ISO's comprehensive transmission planning and approval process,  
28 the ISO Governing Board in January 2000 approved the NESJ Project as the preferred  
transmission alternative to address the identified reliability concerns on the ISO Grid.

1 August and September 2000.

2 12. The CPUC issued a decision on May 14, 2001, a true and correct copy of  
3 which is attached hereto as Exhibit 1 (the "May CPUC Opinion"), approving the NESJ  
4 Project, but selecting a different route for the 230 kV transmission line based on  
5 environmental considerations. The CPUC's "environmentally superior route"<sup>2</sup> specifies 2.8  
6 miles of underground construction, crosses more expensive land than PG&E's proposed  
7 route and requires a different interconnection to PG&E's transmission grid. Because PG&E  
8 had never estimated the costs of constructing the NESJ Project along the CPUC-selected  
9 route, the May CPUC Decision also ordered PG&E to provide detailed cost estimates for the  
10 new route within 30 days so that the CPUC could use these estimates to set a cost cap for the  
11 Project.

12 13. In June 2001, PG&E submitted a detailed cost estimate of \$182.4 million to  
13 construct the NESJ Project along the CPUC-selected route.<sup>3</sup>

14 14. Faced with the higher cost, the CPUC ordered a stay on the NESJ Project,  
15 ordered additional hearings and ordered PG&E to submit additional written and oral  
16 testimony regarding, among other things, the need for the NESJ Project to ensure system  
17 reliability under state and federal standards, the basis for the June 2001 cost estimate for the  
18

19 <sup>2</sup> The CPUC-approved environmentally superior route begins with overhead  
20 construction, tapping off of an existing 230 kV line east of Newark Substation and running  
21 south along the west side of Highway I-880. In south Fremont, the route will transition to  
22 underground construction for 2.8 miles through the Bayside Business Park (as advocated by  
the owner of the Bayside Business Park). At the southern end of the business park, the line  
will transition back to overhead construction for the remaining three miles to the proposed  
Los Esteros substation site.

23 <sup>3</sup> As PG&E witnesses testified before the CPUC in PG&E's supplemental cost  
24 testimony submitted in August 2001 and during the September 2001 hearings, the relative  
25 per-mile cost of constructing underground transmission line in the NESJ Project is  
26 substantially more than the cost of constructing overhead transmission line. The \$112  
27 million increase in the NESJ Project cost estimate reflects not only the increase in costs  
28 related to the additional miles of underground transmission line, but also higher real estate  
values due to the three-year delay and the change in selected route, environmental mitigation  
measures and electrical configuration changes due to the change in the selected route, more  
detailed design of certain components, higher indirect costs such as contingency costs  
(which are calculated as a percentage of the subtotal of labor, material, contract, and other  
direct costs), and general cost escalation due to the three-year Project delay.

1 CPUC-selected route, and the estimated costs of constructing the NESJ Project along  
2 alternative route segments various alternative Project routes. All other parties to the  
3 proceeding also had an opportunity to present evidence on the need for the NESJ Project and  
4 the accuracy of PG&E's cost estimates.

5 15. The additional costs incurred to prepare the requested additional cost  
6 estimates, written testimony and participate in administrative hearings drove PG&E's cost  
7 estimate to \$182.9 million.

8 16. After a week of hearings in September 2001, the CPUC issued a proposed  
9 draft decision on October 10, 2001 (the "Draft Decision"). In the Draft Decision, the CPUC  
10 reaffirmed the need for the NESJ Project to ensure reliable electric service, reconfirmed the  
11 Project's selected route and placement of transmission lines, and issued a CPCN for the  
12 NESJ Project. The Draft Decision, however, adopted a "cost cap" of approximately \$143.5  
13 on project expenditures.

14 17. In October 2001, PG&E filed comments on the Draft Decision objecting to  
15 the proposed "cost cap" and the purported bases for each of the "reductions" of various  
16 Project components in PG&E's cost estimate.<sup>4</sup>

17 18. On December 11, 2001, the CPUC issued a final decision (the "CPUC  
18 Order") lifting the stay and finalizing the grant of a CPCN for the NESJ Project. A true and  
19 correct copy of the CPUC Order is attached hereto as Exhibit 2.

20 19. Over PG&E's objections, however, the CPUC Order asserted the right to  
21 impose a "cost cap" on PG&E's recovery of costs for the NESJ Project and stated that the  
22 "maximum cost determined to be reasonable and prudent" for the NESJ Project is  
23 \$147,542,555. CPUC Order at 31 (Ordering Paragraph 2).<sup>5</sup> This amount is approximately  
24

25 <sup>4</sup> PG&E also objected to other components of the Draft Decision, including the  
26 CPUC's lack of authority under state or federal law to impose a cost cap on the NESJ  
27 Project, its reconsideration of the ISO's determination that all components of the NESJ  
28 Project are needed to ensure system reliability, and its order directing PG&E to submit an  
application seeking a CPUC "reasonableness review" of NESJ Project costs.

<sup>5</sup> The CPUC Order also stated that the CPUC retains jurisdiction to review the

1 \$35.5 million less than the amount of PG&E's estimated cost for the CPUC-approved NESJ  
2 Project. Following PG&E's stated concerns about proceeding with the NESJ Project in  
3 light of the CPUC's attempts to interfere with PG&E's recovery of the actual costs of the  
4 Project, the CPUC also ordered PG&E to construct the NESJ Project.

5 20. The CPUC Order requires PG&E to "file a written notice with the  
6 Commission . . . executed by an officer of PG&E duly authorized . . . to acknowledge  
7 PG&E's acceptance of the conditions set forth in Ordering Paragraphs 1 through 11 and 13,  
8 inclusive, of this decision." May CPUC Decision at 91 (Ordering Paragraph 12). The  
9 CPUC's "cost cap" is not contained in those ordering paragraphs; however, Ordering  
10 Paragraph 4 of the May CPUC Decision states: "This order shall become effective once the  
11 Commission reviews the cost data and comments thereon and incorporates a cost cap and  
12 any other necessary changes into this decision." *Id.* at 89.

13 21. PG&E filed its written notice with the CPUC on February 22, 2002.  
14 PG&E's written notice affirmatively asserts PG&E's right to seek recovery of all Project  
15 costs from the Federal Energy Regulatory Commission ("FERC"), even if actual costs  
16 exceed the CPUC's "cost cap."

17 22. In January 2002, PG&E filed an application for rehearing of the CPUC  
18 Order ("Rehearing Application"), in which PG&E stated its position, among other things,  
19 that: (a) the CPUC has no authority, under either the FERC-approved ISO Tariff or state  
20 law, to reconsider ISO's determination that the NESJ Project is needed to ensure the  
21 reliability of the electrical transmission system; (b) the CPUC has no authority under state or  
22 federal law to impose a "cost cap" on the Project; (c) the CPUC has no authority under state  
23 or federal law to order PG&E to construct the Project; and (d) the CPUC has no authority  
24 under federal law to conduct a duplicative "reasonableness review" of PG&E's NESJ Project  
25 expenditures because FERC sets rates to recover transmission costs. A true and correct copy

26  
27 reasonableness of PG&E's final NESJ Project expenditures. CPUC Order at 30  
28 (Conclusions of Law 3).

1 of the Rehearing Application is attached hereto as Exhibit 3.

2 23. On February 20, 2002, PG&E's Board of Directors approved updated  
3 capital expenditures in the aggregate amount of \$183 million, subject to Bankruptcy Court  
4 approval.

5 24. In deciding whether to approve construction of the NESJ Project and seek  
6 Bankruptcy Court approval to expend the necessary funds, PG&E management weighed the  
7 risks posed by the CPUC's identification of the "maximum reasonable and prudent cost"  
8 (assuming, as PG&E must, that PG&E's Rehearing Application is denied). Due to the  
9 aggregate amount of the "reductions" to PG&E's cost estimate (\$35.5 million), the  
10 identification of the "maximum reasonable and prudent cost" as \$147,542,555 poses  
11 potential substantial risks to cost recovery on the NESJ Project. Because of the need for the  
12 NESJ Project to maintain reliable electrical service and PG&E's belief that the CPUC "cost  
13 cap" likely will not interfere with cost recovery for the reasons set forth below, PG&E  
14 management is willing to proceed with the NESJ Project despite the CPUC having purported  
15 to identify the "maximum reasonable and prudent cost" approximately \$35.5 million below  
16 PG&E's estimated costs for the Project.<sup>6</sup>

17 25. In addition to being the only CPUC-certified approach for providing the  
18 electric transmission capacity required to serve the projected loads in the San Jose area, the  
19 NESJ Project is the lowest cost alternative to serve new electric customer demand in the San  
20 Jose area.

21 26. The overall NESJ Project is expected to increase the Company's revenue  
22 requirement by a net present value of \$243 million. Generally speaking, the cost of  
23 transmission facilities is expected to be included in PG&E's base utility revenue  
24 requirements and is expected to earn the rate of return authorized by FERC.

25  
26 <sup>6</sup> PG&E's decision to proceed with the NESJ Project despite the CPUC's arbitrary  
27 "cost cap" does not mean that PG&E will recommend proceeding with any other  
28 transmission project where the CPUC sets a "cost cap" below PG&E's estimated costs. The  
risk associated with each project will be considered individually.

1                   27. As of the date hercof, the CPUC has not ruled on the Rehearing  
2 Application.  
3

4                   I declare under penalty of perjury under the laws of the United States of America  
5 that the foregoing is true and correct. Executed this 1 day of <sup>April</sup>~~March~~, 2002, at San  
6 Francisco, California.  
7

8                   Kevin J Dasso  
9 Kevin Dasso  
10  
11  
12

13 HOWARD  
14 RKF  
NEMEROVSKI  
CANADY  
PUBLIC  
ATTORNEY  
15 A PROFESSIONAL CORPORATION



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