SENATE COMMITTEE ON ENERGY, UTILITIES AND COMMUNICATIONS
Senator Steven Bradford, Chair
2023 - 2024 Regular

Bill No:	AB 3256	**Hearing Date:**	7/2/2024
Author:	Irwin		
Version:	4/29/2024 Amended		
Urgency:	No	**Fiscal:**	Yes
Consultant:	Nidia Bautista		

SUBJECT: Memorandum and balancing accounts: audits: reports to the Legislature

DIGEST: This bill requires the California Public Utilities Commission (CPUC) to conduct a comprehensive audit, with specified criteria, of each wildfire- or emergency-related memorandum account balancing account of each electrical corporation on or before July 1, 2025, or, on or before January 1, 2027, if the CPUC is unable to review all those accounts by July 1, 2025, as provided.

ANALYSIS:

Existing law:

1) Establishes and vests the CPUC with regulatory authority over public utilities, including electrical corporations, gas corporations, heat corporations, telegraph corporations, telephone corporations, and water corporations. (Article XII of the California Constitution)

2) Directs the CPUC to require a public utility to establish and maintain a balancing account whenever the CPUC authorizes a change in rates reflecting and passing through to customers specific changes in costs to reflect the balance between the related costs and revenues. Requires the CPUC to develop a risk-based approach for reviewing those balancing accounts periodically to ensure that the transactions recorded in the balancing accounts are for allowable purposes and are supported by appropriate documentation. Requires the CPUC to maintain an inventory of the balancing accounts and requires public utilities to record all related costs and revenues in their balancing accounts. Requires the CPUC to adopt balancing account review procedures that are consistent with a risk-based approach. (Public Utilities Code §792.5)

3) Requires the CPUC to annually provide the Legislature with an update on the status of its review of balancing accounts as part of an annual report or by posting it on its internet website, as provided. (Public Utilities Code §910.7)

4) Requires that all charges demanded or received by any public utility, or by any two or more public utilities, for any product or commodity furnished or to be furnished or any service rendered or to be rendered shall be just and reasonable and provides that every unjust or unreasonable charge demanded or received for such product or commodity or service is unlawful. (Public Utilities Code §451)

This bill:

1) Requires the CPUC to include, as part of its annual update to the Legislature on the status of its review of balancing accounts, the amount of funds in, and the expenditures from, the memorandum accounts and balancing accounts of each public utility.

2) Requires the CPUC to conduct a comprehensive audit, with specified criteria, of each wildfire- or emergency-related memorandum account balancing account of each electrical corporation on or before July 1, 2025, or, on or before January 1, 2027, if the CPUC is unable to review all those accounts by July 1, 2025, as provided.

3) Requires the CPUC, if it determines that any actual costs recorded in those electrical corporation accounts have already been authorized and collected from customers, to deny the electrical corporation a 2nd recovery of those costs and to close the account after granting the electric corporation recovery of any just and reasonable costs that have not been collected from customers.

4) Requires the CPUC to make those determinations and take those actions in a manner that ensures that the rates are sufficient to enable the public utility to recover a just and reasonable rate of return.

Background

Cost Recovery Processes: GRCs, balancing accounts, and memorandum accounts. Utilities employ a number of accounts to track expenses, both anticipated and unanticipated. Anticipated costs are determined through the General Rate Case (GRC) proceedings at the CPUC. The GRCs evaluate both past expenses and utility forecasts of likely future costs. They cover four years of a utility's anticipated costs. The GRC establishes how much money the utilities are allowed to collect, and a fixed escalation rate is applied to expenses for the subsequent three years captured in the GRC cycle. Once the CPUC authorizes the costs, the costs are allocated to different classes of customers and built into future billing.

Balancing accounts. Balancing accounts are typically used for costs that are expected and occur on a regular basis, but cannot be estimated accurately. For instance, the Energy Resource Recovery Account (ERRA) is a balancing account that tracks, and utilities are pre-approved to collect, costs of fuel and power purchases. These accounts are subject to audit and adjustment, but do not automatically undergo a reasonableness review. Rather the CPUC authorizes a scope of the recorded activity, and maximum level of acceptable expense, before the utility undertakes the activity. But forecasts are imperfect. If the CPUC authorizes a forecasted amount and also a balancing account for that activity, then when actual costs are higher or lower than the authorized forecast, rates are adjusted up or down to compensate for the forecasting error.

Memorandum accounts. Memorandum accounts are used for activities that are likely to be a reasonable use of ratepayer funds. The CPUC does not decide on the reasonableness of the costs recorded in the memorandum accounts; rather they authorize the tracking of costs that *may* be reasonable. Costs recorded in memorandum accounts are subject to a later reasonableness review, with the potential inclusion in rates, but such recovery is not guaranteed. Memorandum accounts are meant to address expenditures that are much less certain than balancing accounts. For example, per statute, utilities record costs incurred in responding to emergencies in Catastrophic Event Memorandum Accounts.

CPUC review of balancing accounts. The CPUC has a responsibility to authorize the rates that regulated utilities may charge their customers. The CPUC does not audit every large balancing account or utility record every year. Statute requires the CPUC to review or audit balancing accounts *periodically* using a risk-based approach, but allows it to forgo the review or audit if an independent auditor has performed a review in the preceding five years. In a 2014 State Auditor report regarding the CPUC's monitoring of balancing accounts, the auditor recommended that the CPUC adopt a risk-based approach to select a sufficient number of accounts to review. This was recommended after the CPUC was found to have not reviewed many balancing accounts over the years reviewed by the auditor, despite a statutory mandate requiring audits at least once every three years. In 2022, the Legislature made the auditor's recommendation of risk-based auditing a requirement.

As directed by statute, the Utility Audits Branch (UAB) utilizes a risk-based approach for reviewing or auditing balancing accounts to ensure that the transactions recording in the balancing accounts are for allowable purposes and are supported by appropriate documentation. According to the CPUC's 2022 Annual Report, as of December 31, 2021, the total population of balancing accounts consisted of 8 energy and 12 water utility companies, encompassing a total of 486 balancing accounts (367 electric and gas, and 119 water). UAB's completed audits seek to ensure that balancing accounts operate within the context of what has been authorized. The CPUC reported in its annual report that UAB completed 45 utility audits in 2023.

In addition to the CPUC's UAB, the California Public Advocates Office (PAO) likewise reviews utility balancing accounts. PAO typically reviews a selection of balancing accounts, usually based on whether the utility requests rate changes related to an account, not based on the size of the account, noted in the 2023 State Auditor Report. According to the same report, PAO audited between 35-42 electricity balancing accounts over three years, or about 6-33 percent of each electric utility's balancing accounts.

Comments

Need for this bill. As shared by the author's office, outlined in a report by the PAO, utilities have gained additional mechanisms to charge for wildfire mitigation and energization beyond the GRC. Balancing accounts allow utilities to ensure the recovery of certain costs and have usually been used for highly predictable costs each year. Memorandum accounts have typically been used for costs with high year-to-year volatility. Since 2020, the PAO has noted over $14 billion of utility wildlife-related balancing and memo account requests. These regulatory accounts have expanded the investor-owned utilities' (IOUs) ability to request increased budgets, passing along the costs to ratepayers. AB 3256 would require the CPUC to audit emergency-related balancing and memo accounts to determine if the costs in the accounts were authorized, if the costs have already been collected from ratepayers, and the impact to ratepayers outside of the GRC. This will provide increased oversight and accountability for how regulatory accounts funds are managed.

Impacts to ratepayers. Energy utility rates have been rising and affordability continues to be a central concern for the Legislature and Californians. In the 2023 State Auditor report on the CPUC and the PAO reports that as of December 2022, the large energy IOUs maintained over 300 balancing accounts tracking $16.8 billion in balances. This represents a third of IOU authorized revenue. In some scenarios a balancing account is a helpful tool that allows the utility to track costs that are otherwise difficult to forecast in advance. In other scenarios, the opportunity to track costs in a balancing account may undermine or even removes the incentives for the utility to assert spending discipline. By requiring the CPUC to audit the balancing and memorandum accounts by July 1, 2025, this bill attempts to focus the CPUC's resources on these accounts. However, this bill recognizes some flexibility is needed and provides the CPUC the ability to determine criteria to prioritize accounts that may have the biggest impact.

Opponents raise concern about language requiring closing accounts. Among its provisions, this bill would require balancing accounts to be closed where a utility has already recovered those costs. The opponents raise concern that closing accounts for what may be a bookkeeping errors could jeopardize critical utility work, including wildfire mitigation. They suggest such an approach fails to recognize why balancing accounts were created to help ensure critical utility work is not delayed between GRCs. In this regard, the opposition raises a valid concern about the practical effect of the requiring the accounts to close. *In this regard, the author and committee may wish to amend this bill to delete this section while preserving the other required review and other elements of this bill.*

Prior/Related Legislation

AB 2054 (Bauer-Kahan, 2024) among its provisions, authorizes the CPUC to allocate between ratepayers and shareholders any costs recorded in a balancing account above an authorized forecast. The bill is pending in this committee.

AB 2666 (Boerner, 2024) requires the CPUC to review the actual past costs an electrical or gas corporation records following each GRC test year, and adjust the authorized revenue requirement in the subsequent GRC, as appropriate.
The bill is pending in this committee.

AB 2847 (Addis, 2024) requires electric and gas IOUs to provide in their request for capital expenditures their best estimation, alongside supporting documents, of the impact of the proposed expenditures on the utility's authorized revenue for each year of the life of the capital asset, as well as the asset's net present value. The bill is pending in committee.

FISCAL EFFECT: Appropriation: No Fiscal Com.: Yes Local: Yes

SUPPORT:

Sonoma Clean Power

OPPOSITION:

California State Association of Electrical Workers
California Water Association
Coalition of California Utility Employees

Pacific Gas and Electric Company
San Diego Gas and Electric Company
Southern California Edison

ARGUMENTS IN SUPPORT: Sonoma Clean Power states:

> The number, size, and scope of memorandum and balancing accounts subject to Public Utilities Commission jurisdiction have grown significantly in recent years, with minimal oversight. This has led to significant ratepayer impacts, including to those ratepayers served by Sonoma Clean Power. At a time of rapid growth in utility rates, the state of California needs to explore all possible avenues to keep costs contained where feasible. AB 3256 is a common-sense measure that will impose a basic level of accountability on some of the biggest drivers of utility rates today. Again, we strongly support AB 3256

ARGUMENTS IN OPPOSITION: SCE, SDG&E, and PG&E state:

> AB 3256 could undercut investments in the grid, impacting safety and reliability. Closing a memorandum or balancing account in mid-GRC cycle could lead to bookkeeping challenges. How will a utility conduct wildfire mitigation efforts in the second or third year of the GRC cycle if the balancing account in which the costs are tracked is closed? The utility would likely have to submit an application for a new balancing account mid-GRC cycle, creating unnecessary administrative inefficiencies. And, while we wait for Commission's authorization, the critical safety and reliability work that the previous account would have allowed is now on hold. CPUC and Cal Advocates are already taking steps to strengthen transparency. …The CPUC and Cal Advocates have agreed to take appropriate actions to implement the State Auditor's recommendation. AB 3256 disregards the State Auditor's recommendation and would institute more rigorous changes before the Auditor's recommendations can be accomplished.

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