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

Bill No:	AB 3263	**Hearing Date:**	7/2/2024
Author:	Calderon		
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Urgency:	No	**Fiscal:**	Yes
Consultant:	Nidia Bautista		

SUBJECT: Electrical corporations: financing orders

DIGEST: This bill authorizes electrical corporations to finance categories of costs that would be recovered through a fixed charge on customers' electric utility bills, including costs for vegetation management and other operational and maintenance expenses related to wildfire mitigation, and costs stemming from a state or federal emergency declaration. This bill also authorizes a large electrical corporation to issue recovery bonds for vegetation management expenses, including costs that have already been recovered from customers, up to a $10 billion and a 15 year average repayment period.

ANALYSIS:

Existing law:

1) Establishes and vests the California Public Utilities Commission (CPUC) with regulatory authority over public utilities, including electrical corporations, also known as electric investor-owned utilities (IOUs). (Article XII of the California Constitution)

2) Authorizes the CPUC to fix the rates and charges for every public utility, and requires that those rates and charges be just and reasonable. (Public Utilities Code §451)

3) Defines "large electrical corporation" as an electrical corporation with 250,000 or more customer accounts in the state. (Public Utilities Code §3280)

4) Requires the CPUC to authorize an electrical corporation to recover costs and expenses arising from a covered wildfire occurring after January 1, 2019, if the CPUC finds the costs and expenses are just and reasonable. Establishes a standard of reasonable conduct of an electric IOU, for purposes of cost recovery, based on whether a reasonable utility would have undertaken the action in good faith under similar circumstances. Specifies the electric IOU

bears the burden to demonstrate that its conduct was reasonable, unless it has a valid safety certificate; at which point, the electric IOU's conduct is deemed reasonable unless a third party creates serious doubt as to the reasonableness of the electric IOU's conduct. (Public Utilities Code §451.1)

5) Authorizes an electric IOU to request securitization of costs and expenses from wildfires in 2017 that were either determined by the CPUC as recoverable from ratepayers or disallowed by the CPUC for rate recovery but in excess of a CPUC determination of the maximum amount the electric IOU can pay without harming ratepayers or materially impacting its ability to provide service. This CPUC determination was known as the "stress test" or "customer harm threshold." (Public Utilities Code §451.2)

6) Prohibits a public utility from issuing bonds, or any form of indebtedness at periods of more than 12 months, unless first authorized by the CPUC. (Public Utilities Code §818)

7) Authorizes the CPUC to issue a financing order for securitized bonds to finance the unamortized balance of the regulatory asset awarded to Pacific Gas and Electric Company (PG&E) following the energy crisis. (Public Utilities Code §840)

8) Authorizes an electrical corporation to file an application requesting the CPUC to issue a financing order to authorize the recovery of costs and expenses related to a catastrophic wildfire, including fire risk mitigation capital expenditures, through the issuance of bonds by the electrical corporation that are secured by fixed recovery charges. Authorizes an electrical corporation to request the CPUC issue a financing order to authorize the recovery, through securitization, of costs and expenses related to a catastrophic wildfire (with an ignition date in 2017 or after January 1, 2019) or undercollection amounts accrued in 2020 with those cost and expenses recovered through a fixed charge. (Public Utilities Code §850)

9) Specifies the conditions that must be satisfied, as determined by the CPUC, for recovery bonds eligible for securitization. These conditions include that the costs to be recovered in bonds are just and reasonable, the bonds are consistent with the public interest, and the bonds reduce (to the maximum extent possible) the rates consumers would pay compared to traditional financing mechanisms. (Public Utilities Code §850.1)

10) Authorizes a large electric IOU to request securitization to finance its share of the first $5 billion of approved wildfire mitigation capital expenditures and

the debt financing costs of those expenditures. Prohibits the CPUC from allowing the large electric IOUs to earn a return on equity on the mandated fire risk mitigation capital expenditures. (Public Utilities Code §8386.3)

11) Defines "Wildfire Fund allocation metric" means for large electrical corporations the arithmetic of land area of their territory and proportion of the line miles of transmission and distribution in high fire-threat districts, among other factors. Requires the Director of the Department of Finance to determine by July 17, 2019, which was determined to be the expectation in the statute of: 64.2 percent for PG&E, 31.5 percent for Southern California Edison (SCE), and 4.3 percent for San Diego Gas & Electric (SDG&E). (Public Utilities Code §3280 (n))

This bill:

1) Authorizes the use of a financing order, in addition to expenses related to catastrophic wildfires, to recover the costs of wildfire mitigation efforts, operational and maintenance expenses related to an electrical corporation's wildfire mitigation plan, wildfire risk mitigation costs, vegetation management costs and expenses, or to recover an electrical corporation's costs related to any federal or state declaration of a state of emergency.

2) Authorizes a large electrical corporation to issue recovery bonds for vegetation management expenses, including for costs already collected in rates if those costs are refunded to customers, in an amount not to exceed $10 billion (multiplied by the Wildfire Fund allocation metric for each electrical corporation) with an average repayment period not to exceed 15 years.

Background

Authorizes utility financing via rate recovery bonds (also known as securitization). Rate recovery bonds are financing mechanisms that are asset-backed securities (collection of dedicated fees on ratepayers' utility bills) often structured to minimize borrowing costs in order to qualify for better credit ratings well below the rate available in the marketplace which would otherwise apply to other long-term debt. Ratepayers pay off the bonds through a special surcharge (dedicated rate component), which generates a cash flow stream. The dedicated rate component is generally in the form of an irrevocable, nonbypassable charge collected from all customers, bundled and unbundled (though low-income customers are often exempted). Beyond the reduced interest rates, credit ratings agencies will often treat this debt differently, and remove the rate recovery bonds/securitization debt from the utility's balance sheet. As a result, securitization of debt, with limits, can improve a utility's credit ratings. Additionally, bonds could help reduce immediate customer utility bill spikes by allowing the payments of the expenses (plus interest and other fees) to be spread over a longer time period. Though, of course, as with all debt the costs and benefits will depend on the particulars of the expenses, the terms of the financing (including fees).

Use of securitization by utilities. Statute authorizes the CPUC to issue financing orders that commit electric ratepayers to paying fixed charges on their utility bills to support a bond issuance by a utility. Per the statute, the issuance of a financing order requires customers to pay the principal, interest, and other costs of the bonds until those bonds are fully paid off. Statute also requires the CPUC to review requests by utilities for financing orders. As with all matters related to recovery of expenses from ratepayers, statute requires the expenses must be just and reasonable. Additionally, Public Utilities Code §850.1 requires the CPUC to only issue a financing order if the CPUC makes specified determinations that the recovery bonds (including all terms and conditions) are determined: to be just and reasonable, consistent with the public interest, and would reduce the rates on a present value basis that consumers would pay compared to traditional financing mechanisms.

History of utility securitization. Rate recovery bonds are a financing mechanism used during the energy crisis to finance the settlement terms between PG&E and the CPUC. More recently, securitization or rate recovery bonds have been authorized to finance costs and expenses related to damages stemming from specified wildfires that were caused by electrical infrastructure, specifically authorized by SB 901 (Dodd, Chapter 626, Statutes of 2018) and AB 1054 (Holden, Chapter 79, Statutes of 2019). The latter legislation also authorized the state's three large electrical corporations to securitize $5 billion of fire risk mitigation capital expenditures. Additionally, AB 913 (Calderon, Chapter 253, Statutes of 2020) authorized securitization of electrical corporation's undercollections during a time of COVID-19 impacts.

The CPUC has issued several financing orders authorizing the issuance of recovery bonds for the electrical corporations:

- CPUC Decision 21-05-015 - In May 2021, the CPUC issued a financing order authorizing PG&E to issue recovery bonds for $7.5 billion to fund costs related to the 2017 North Bay Wildfires.

- CPUC Decision 21-06-030 - In June 2021, the CPUC issued another financing order for PG&E to issue $1.2 billion in Wildfire Hardening

Recovery Bonds to finance fire risk mitigation plan capital expenditures authorized by Public Utilities Code §8386.3(e).

- CPUC Decision 21-10-025 - In October 2021, the CPUC issued a financing order for SCE to issue bonds to recover approximately $526 million in wildfire-related capital expenditures. The CPUC denied SCE's request for operations and maintenance (O&M) expenses to be recovered through this financing order.

Securitization of capital vs operations & maintenance (O&M) expenditures. Since securitization generally requires long-term debt, capital expenditures by utilities generally involve high upfront costs for the use of a long term asset, which makes these expenditures potentially good candidates for securitization. Put more bluntly, ratepayers presumably receive the benefits of utility capital expenditures over the long-term, for the useful life of the asset, such as an electrical substation or underground vault which generally operate for over a decade or decades. On the other hand, O&M expenditures generally provide short-term benefits. These may be recurring projects or activities which are generally paid immediately. Examples include tree trimming and other vegetation management which is done on a recurring basis and where the benefits may be short-lived (as trees and vegetation continue to grow). Expenditures of recurring and short-term benefits are generally not good candidates for securitization where long-term debt would be paid by customers well beyond the short-term benefits of the activity.

Comments

Need for this bill. According to the author: "With an increase of prolonged destructive wildfires, megadroughts, and other serious effects of climate change, climate resiliency efforts are imperative. All financing mechanisms should be made available so that electric utilities can continue investing in climate resiliency without subjecting California families to significant electric bill spikes. Assembly Bill 3263 will allow an electric utility to request authorization from the California Public Utilities Commission for the bonding of their ongoing wildfire mitigation efforts to achieve greater rate stabilization for electric utility ratepayers."

Wildfire related costs a driver for increasing electric utility bills. As this committee has heard, electric utility bills have been increasing and one of the main drivers (though not the only) is wildfire-related expenses, including wildfire mitigation. In recent years, much of the wildfire mitigation has been in the O&M category, particularly as vegetation management and tree trimming. Additional wildfire related O&M expenses, include insurance premiums and wildfire damages. However, to the extent conversion of above ground lines to underground becomes a principal strategy (as PG&E has proposed) capital expenditures related to undergrounding will likely increase. Nonetheless, the challenge of O&M increased costs is these are borne on customers' utility bills nearly immediately. Although the CPUC has authorized their recovery over a more extended, but still short-term (under three years) timeframe.

CPUC has denied securitization of O&M. As noted above, the CPUC reviews electrical corporations' applications for financing orders to ensure they are just and reasonable, in the public interest, and favorable to ratepayers compared to other financing mechanisms, among other considerations. These applications undergo a formal proceeding with other stakeholders reviewing and commenting on the particulars of the request. SCE's application for recovery of various costs included a request for approximately $517 million in wildfire-related capital expenditures, $401 million in wildfire-related O&M expenses, and $77 million in residential uncollectible bad debts expense. Ultimately, the CPUC approved $526 million in wildfire capital expenditures for the requested securitization. However, the CPUC denied recovery of the O&M expenses and uncollectible debts stating that the 25 year proposed financing for these expenses would be result in intergenerational equity issues for ratepayers and not provide short- or long-term benefits for customers. However, the CPUC did authorize SCE amortizing these costs over 36 months, extending the collection over an additional one to two years to reduce impacts on utility bills.

PG&E's pending application. On June 20th, PG&E filed an application to the CPUC requesting authorization to finance up to $2.356 billion in wildfire related O&M expenses incurred in 2023-2024 that have already been approved as just and reasonable in PG&E's 2023 general rate case. PG&E contends these expenses are among the significant contributors to the increased wildfire mitigation costs in customer rates today. If approved, the bonds will be used to provide immediate rate relief in the form of a rate reduction to customers for the first year and distribute those costs over the life of the 10-year bonds. The application was only recently submitted and expected to be under review over the coming month(s).

Making it explicit, but requiring continued CPUC review. This bill makes explicit that O&M, wildfire mitigation plan costs, and costs stemming from an emergency declared by the state or federal government would be an authorized category of costs to be securitized, assuming the CPUC determines a financing order is warranted. As The Utility Reform Network notes in its opposition, typically, O&M costs are treated as a direct pass through to utility customers. The CPUC has noted that while legally permitted to authorize securitizing of O&M costs, doing so in the case of the SCE application was not in the public interest. The CPUC stated: "The time-value-of money benefits associated with present value discounting are outweighed by the associated financing costs and sustained levels of higher utility rates over time." However, the CPUC 2021 decision did not preclude all such proposals under all circumstances, as with all applications the electrical corporation must demonstrate benefits to ratepayers.

Proceed with caution! As drafted, AB 3263 would also allow electrical corporation's to securitize on their own without the CPUC review. However, the author has noted their intent to not circumvent the CPUC. Subparagraph (B) of paragraph (2) of subsection (a) of this bill would authorize the large electrical corporations to issue rate recovery bonds for vegetation management expenses, including for costs already collected in rates if these costs are refunded to customers. This provision also prescribes limits as to the amount, up to $10 billion multiplied by the electrical corporation's wildfire allocation metric (roughly up to $6.4 billion for PG&E, $3.15 billion for SCE, and $430 million for SDG&E), and the average repayment of no more than 15 years. While the opportunity for customers to receive refunds may be appealing, it raises many concerns about the particulars and necessity of such an approach. As noted above, the CPUC has authority to review applications for utility's cost recovery and requests for financing orders, including a utility's request for rate recovery bonds. As currently drafted, this bill would authorize the large electrical corporations to issue these recovery bonds without the CPUC review. Moreover, this bill's proposal would explicitly authorize expenses to be financed where the utility has already received recovery from ratepayers. Beyond the concerns noted above about long-term financing costs for the short-term benefits of vegetation management, this provision also raises additional questions about retroactive refunds, about the terms and amounts that would be authorized and their effects on ratepayers. Many of these issues are best addressed by the CPUC within a proceeding where a utility submits an application with necessary documents to allow for a review by the agency, including the involvement of other stakeholders. In this regard, the Legislature may wish to proceed with caution.

Need for amendments. To preserve the CPUC's authority to review applications for cost recovery of vegetation management expenses and the review of requests for financing orders by electrical corporations, including the amount and terms, along with full consideration to existing, future, and past customers, *the author and committee may wish to delete subparagraph (B) of paragraph (2) of subdivision (a) proposed in this bill.*

Prior/Related Legislation

AB 1513 (Calderon, 2023), the final version had related provisions to this bill, would have authorized categories of costs and expenses arising from electrical IOU wildfire mitigation to be eligible for securitization. The bill died in the Assembly Committee on Appropriations.

AB 2937 (Calderon, 2022), similar to this bill, sought to expand the categories of expenses for which an electric IOU may request the CPUC allow the IOU to finance through issuance of a bond, backed by a reoccurring charge to the IOU's ratepayers. The bill died in the Assembly Committee on Appropriations.

AB 913 (Calderon, Chapter 253, Statutes of 2020) authorized the CPUC to approve the securitization by electric IOUs of undercollection of utility bill amounts for the year 2020. Additionally, the bill aligns the "eligible claims" period with a utility's insurance policy period for purposes of wildfire related claims.

AB 1054 (Holden, Chapter 79, Statutes of 2019), among its many provisions, authorized the issuance of financing orders for the recovery of costs and expenses related to catastrophic wildfires (in 2019 and after). Also permits securitization of fire risk mitigation capital expenditures associated with the electrical IOU's proportionate share of $5 billion in safety improvements.

SB 901 (Dodd, Chapter 626, Statutes of 2018) among its many provisions, authorized the issuance of financing orders to finance costs, in excess of insurance proceeds, incurred, or that are expected to be incurred, by an electrical corporation, excluding fines and penalties, related to 2017 wildfires.

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

SUPPORT:

California Hawaii State Conference of the NAACP
Pacific Gas and Electric Company
Southern California Edison

OPPOSITION:

The Utility Reform Network

ARGUMENTS IN SUPPORT: Southern California Edison (SCE) states:

> AB 3263 is an important tool for electrical utilities as it will allow for the securitization of wildfire mitigation operation and maintenance (O&M) and vegetation management costs. Like home mortgages or large purchases of a car or appliance, many people cannot afford to pay the entire cost up front

and often opt to finance the purchase by paying for it over time. Wildfire mitigation O&M costs are associated with major projects with significant costs. Without securitization, those costs could be reflected in rates immediately resulting in sudden rate spikes to customer bills. With securitization, the costs would be reflected in rates over a longer period.

ARGUMENTS IN OPPOSITION: The Utility Reform Network (TURN) contends:

> AB 3263 would, subject to a dollar limit, permit electrical corporations to, on their own initiative and without regulatory oversight, undo Commission direction and securitize costs the Commission previously directed to be collected in rates. Securitization is not always the best solution. Securitization may or may not benefit ratepayers depending on the specific situation and costs to which this tool is applied. When securitization is requested as a means of achieving utility cost recovery, the CPUC, and the CPUC alone, must be permitted to determine whether this tool is the best option to advance the public interest. …The language of AB 3263 should be rejected because it is not in ratepayers' interests and could result in even higher costs than they would otherwise face under existing ratemaking mechanisms. Allowing the utilities to determine, on their own, when securitization is appropriate diminishes its power as a tool for the Commission to use to protect ratepayers.

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