California State Senate

COMMITTEE ON
ENERGY, UTILITIES AND COMMUNICATIONS

STEVEN BRADFORD
CHAIRMAN

STAFF
CHIEF CONSULTANT
NIDIA BAUTISTA
CONSULTANT
SARAH E. SMITH
COMMITTEE ASSISTANT
MELANIE CAIN
1021 O STREET, SUITE 3350
SACRAMENTO, CA 95814
TEL (916) 651-4107
FAX (916) 642-8979

OVERSIGHT HEARING

Annual Update to the Legislature by the California Public Utilities Commission and Public Advocates Office: A Focus on Utility Bill Affordability

1020 O Street, Room 1200
Tuesday, February 28, 2023
9:00 a.m.

BACKGROUND

"We will make electricity so cheap that only the rich will burn candles." ---
Thomas A. Edison *(attributed, but not verified)*

Californians have, generally, enjoyed lower energy bills when compared to the rest of the country, largely due to milder weather and investments in energy efficiency, even as electric rates have been higher than many other states. However, in more recent years, these trends have been changing as California's higher energy rates are also resulting in higher energy utility bills. As such, there are growing concerns about the affordability of utility bills on household budgets and commercial/industrial entities' balance sheets. These concerns are exacerbated by the interest to adopt policies to reduce the state's greenhouse gas emissions by shifting away from fossil fuels towards alternatives, including electrification in the transportation and building sectors. Such a transition relies on changing customer behaviors, in addition to policies. However, Californians may be reluctant to switch fuels if utility costs are unaffordable, thereby potentially slowing progress towards the state's climate goals. Yet, more importantly, many Californians have also struggled to overcome economic challenges, including impacts from the COVID-19 pandemic. Low-income and fixed-income residents have fallen behind on paying their bills, including the utility debt accumulated over the time of the pandemic. The Legislature and Governor have helped alleviate these concerns by approving over $2 billion in funding to address energy utility bill arrearages and another $1 billion to address water utility bill arrearages. Nonetheless, the growing costs for goods and services due to inflation and supply shortages is also affecting the cost of utility bills and the ability for Californians to manage their household budgets. Just this winter, Californians throughout the state have been affected by skyrocketing costs of natural gas which resulted in shock to customers when their natural gas utility bills arrived in January and February, in many cases the costs were three times or more than their previous year's natural gas utility bill. The effect of the surge in natural gas prices is also expected to impact electric utility bills as those costs get rolled into generation costs.

Today's hearing is the annual update to the Legislature by the California Public Utilities Commission (CPUC) and the Public Advocates Office (PAO), with a focus on utility bill affordability. As part of today's hearing, the CPUC will share its efforts to help address utility bill affordability, including actions and outcomes to respond to the recent natural gas price spikes and calls for an investigation into the causes, as well as, steps to help mitigate impacts to Californians. The PAO will also share their annual update, with a focus on utility bill affordability. After the CPUC's and PAO's presentations, a panel composed of a small subset of stakeholders will provide suggestions for addressing utility bill affordability.

CPUC role in setting utility rates.

Investor-owned utilities. Privately-owned utilities, commonly referred to as investor-owned utilities (IOUs), are afforded an exclusive license to provide service in a specific geographic area (known as a service territory) in exchange, the IOUs' rates are regulated by the regulatory body. IOUs, as private companies, earn a rate of return (authorized profit from rate base) on utility-owned and capitalized assets and equipment. The regulatory construct is intended to limit the ability of the monopoly entity to charge unfettered rates. In general, utilities operate on access to long-term financing with rates determined by their credit ratings. In California, the CPUC reviews and approves rates for IOUs to ensure they are "just and reasonable." Most Californians, about 75 percent receive electricity services from electric IOUs; publicly owned utilities (POUs), whose rates are set by local governing boards, provide service to the remaining 25 percent. On the other hand, the vast majority of Californians receive natural gas utility service from an IOU, with some exceptions (such as the City of Long Beach, which provides its own natural gas utility service).

Bundled and unbundled customers. Electric and natural gas IOU customers may be both bundled (meaning they receive distribution and procurement service from the utility) and unbundled (meaning they only receive distribution services from the utility and receive procurement services from another provider). In the case of electric IOUs, customers may receive procurement service from a community choice aggregator (CCA) or electric service provider (ESP). CCAs and ESPs set their own rates, though most CCAs, which are overseen by local government entities, seem to index their rates to those of the electric IOU. When a local government launches a CCA, they develop an implementation plan and schedule to automatically enroll customers to the CCA, unless the customer proactively opts-out. In the case of natural gas IOUs, core customers (mostly residential and small commercial) may receive procurement services from either the utility or opt-in to receive service from a third party provider known as a core transport agent (CTA). Non-core customers (usually large industrial customers, including natural gas power plants that generate electricity) procure their own natural gas, but utilize the utility's transmission and distribution pipelines to deliver their gas.

Cost recovery proceedings and processes.

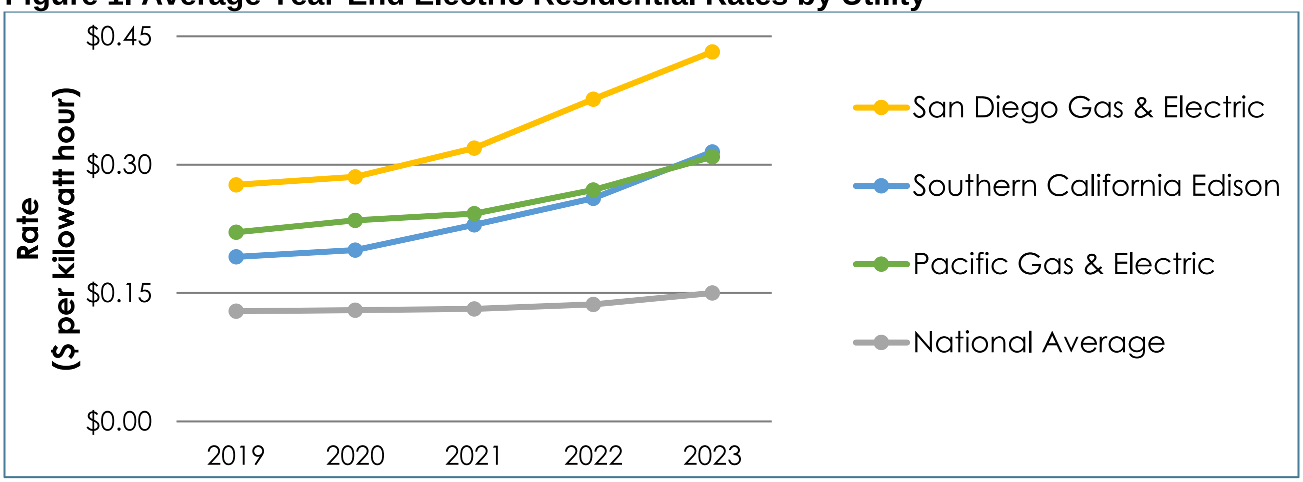
The General Rate Case. The CPUC reviews and approves IOU costs and revenues through various applications submitted by the IOUs – most notably the General Rate Case (GRC). The GRCs are generally conducted on three-year cycles, though are now shifting to four-year cycles. The proceedings can last 18 months to two years, or more, whereby all aspects of the IOUs' costs of operating and maintaining the utility system are reviewed. More recently, per statutory requirements adopted following the San Bruno pipeline explosion, IOUs must also ensure their forecasted expenses associated with investments on their systems are informed by safety and other risks to the system. The GRC has two main components: Phase I determines the total amount the IOU is authorized to collect, known as the "revenue requirement" (the size of the pie), and Phase II determines the share of the costs attributed to each customer class and the corresponding rate schedules (the slicing of the pie). GRCs are forward-looking, as IOUs forecast and estimate their anticipated costs to operate their respective utility. In addition to GRCs, IOUs submit other applications for cost recovery.

Other cost recovery processes at the CPUC. In the case of electric IOUs, Energy Resource Recovery Account (ERRA) proceedings are used to reconcile estimated versus actual fuel and purchased power costs. The CPUC annually reviews these costs, and to the extent they are deemed reasonable, passes through those costs without any mark-up or profit to the utility. The costs are forecasted for the year ahead. If the actual costs are lower or higher than forecasted, then the electric IOU credits or charges customers, respectively, for the difference. In the case of natural gas utilities, natural gas procurement costs are rolled into rates monthly and are therefore seen more immediately on utility bills. Natural gas costs are also not marked up, solely passed on to customers as pass-through costs. Beyond these proceedings, IOUs also submit applications (or advice letters) for other program allocations or cost recovery. Some of these applications can be for substantial amounts of cost recovery, such as electric vehicle charging infrastructure investments or wildfire-related expenses, which when approved by the CPUC get rolled into customer rates.

Transmission-related costs. Lastly, in addition to CPUC cost recovery processes, IOUs also undergo similar reviews at the Federal Energy Regulatory Commission (FERC)for transmission (generally high voltage electric lines and high volume natural gas pipelines) for costs associated with operating transmission systems. However, these tend to have fewer stakeholders actively involved in the proceedings. The CPUC represents California ratepayers' interests in these proceedings.

Below is a chart provided by the PAO noting average residential rates by large electric IOU in California.

Figure 1. Average Year-End Electric Residential Rates by Utility



Sources: PG&E, SDG&E, SCE data (Public Advocates Office) & National (U.S. Energy Information Administration)
Note: A kilowatt-hour is a common unit of electricity, about the amount used to run a microwave for one hour.

Figure 2. 2021 Major California Investor-Owned Utility Rates by Components

Source: California Public Utilities Commission. Energy Division analysis. *2022 Senate Bill 695 Report*.
Note: The graph displays total system costs, which include the costs covered by all customer types (residential, industrial, agricultural, and commercial)

Winter natural gas prices skyrocket.

As numerous news stories have noted, natural gas prices have surged this winter, beginning in late November and continuing through January. According the Energy Information Administration's (EIA's) *December 22, 2022 Natural Gas Weekly Update*, the daily spot market prices reached their highest levels in over two decades at major trading hubs that deliver natural gas into California, including over $50.00 per million British thermal units (MMBtu) at Pacific Gas & Electric (PG&E) City Gate and Malin, Oregon, as well as, a four-year record for SoCal CityGate of nearly $50 per MMBtu on December 13. These prices compare to the national benchmark price at Henry Hub which was declining to $6.60 MMBtu – a staggering over $40 per MMBtu price difference between the West Coast and other trading hubs in the nation. According to the CPUC's fact sheets regarding utility rates, January 2023 natural gas procurement rate is over 300 percent more than the procurement rate in January 2022. These costs are passed through directly to utility customers – as utilities are prohibited from marking up the price of the commodity. As such, these higher prices are affecting customers' utility bills beginning in January's billing cycle.

A rise in global demand for natural gas (especially liquefied natural gas due to the impacts of the Russian invasion of Ukraine) and the regional effects of colder-than-normal temperatures this winter are likely contributing to higher prices, however, these causes alone do not fully explain the differences between West Coast/Pacific natural gas prices and those in other parts of the nation. According to the EIA, additional factors for West Coast/Pacific higher prices include: reduced natural gas flows, pipeline constraints (including maintenance in West Texas), and low regional natural gas storage inventories, including those that may have been impacted by CPUC rules related to operational flow orders or (as alluded to by the EIA) changes to the accounting of operational gas are inadvertently contributing to price surges.

Calls to investigate causes and help customers with costs. Chair Bradford sent a letter to the CPUC and California Energy Commission (CEC) calling on the agencies to support PAO's request for an investigation into the causes. The Chair's letter also called on the need to help customers buffer these costs. The CPUC and CEC have responded organizing a hearing on the issue on earlier this month. Governor Newsom has also requested the FERC to consider investigation into the causes given their role in overseeing natural gas markets. The CPUC has also approved advancing the annual climate credit, typically issued in the spring or later in the year, to help reduce customers' bills. For SoCalGas customers, the credit is

$50 and is being rolled out this month. At today's hearing, the CPUC will provide an update on the next step.

Available customer assistance.

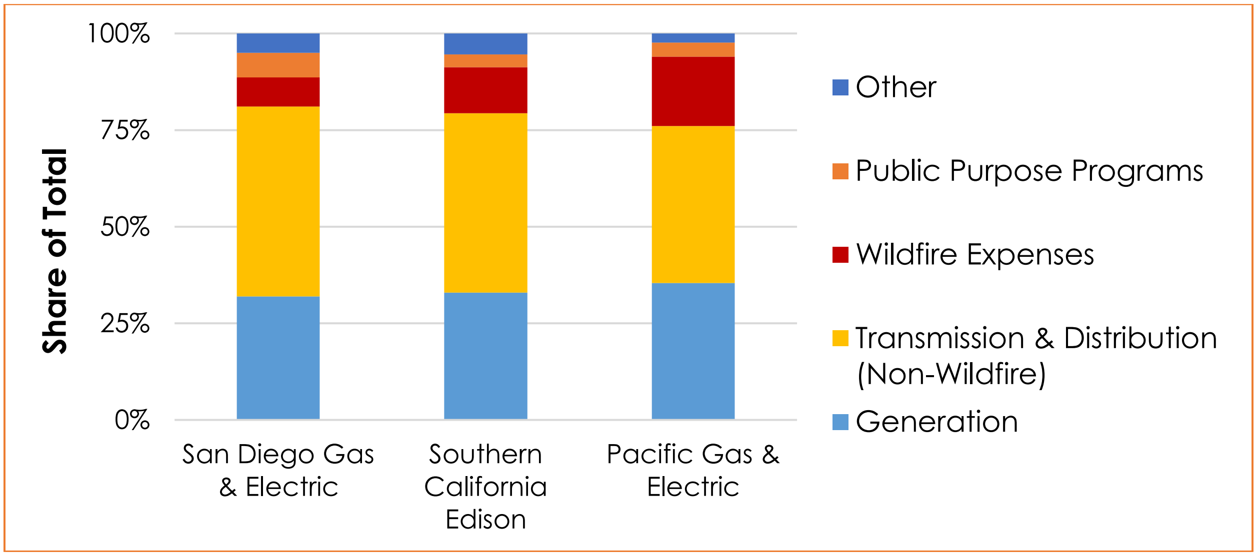
Utility bills, unlike credit card bills, can be more forgiving. The Legislature and the CPUC have adopted numerous rules to provide customer assistance, as well as, disconnection processes to protect customers from loss of essential services. –The programs include the California Alternate Rates for Energy (CARE) program which provides a 30-35 percent discount on electric IOU bills and 20 percent on natural gas IOU bills for income qualified households. Additionally, the Family Electric Rate Assistance (FERA) program provides an 18 percent discount on electric bills for families whose household income slightly exceeds the CARE allowances. FERA is available for customers of Southern California Edison (SCE), San Diego Gas and Electric Company (SDG&E), and PG&E Company. Additional assistance programs provide greater energy allowance for customers who require energy for medical reasons. Low-cost energy efficiency and weatherization services are also available to CARE and FERA customers.

More recently, the Legislature and Governor have approved over $3 billion in utility debt-relief assistance for energy and water utility bills, across IOUs and POUs. The program is administered by the Department of Community Services and Development (CSD) with the bulk of the funding already provided to utilities to help customers with arrearages. However, some funding remains and $400 million is proposed to be reverted to the General Fund under the Governor's January budget proposal. In addition, CSD administers federal Low Income Home Energy Assistance (LIHEAP) program that provides one-time emergency safety net assistance to pay for utility bills for income qualified customers. Beyond these programs, the CPUC also imposes various disconnection processes and procedures in order to protect customers from being unfairly disconnected from utility service. The CPUC is also experimenting with a Percentage of Income Payment Plan (PIPP) pilot to allow some CARE customers to receive monthly household income utility bill caps, set at four percent of household incomes. The four-year pilot was only recently been initiated as part of the CPUC's utility disconnections proceeding. Findings from the pilot are still years away.

What's in the rates?

On electric side of the equation, a number of drivers are increasing costs. According to the CPUC's annual SB 695 report, since 2013, bundled residential average rates have increased at an annual average rate of about seven percent for

PG&E, five percent for SCE, and 10 percent for SDG&E. The primary drivers include wildfire mitigation investments, and transmission and distribution costs. The following bar chart is provided by PAO based on CPUC and IOU data regarding the categories of costs in electric rates.



Legislature approves income-graduated fixed charges.

Among the many provisions in AB 205 (Committee on Budget, Chapter 61, Statutes of 2022) was the removal of the existing fixed charge caps established under AB 327 (Perea, Chapter 611, Statutes of 2013) which limited fixed charges to no more than 10 dollars and five dollars for CARE customers. The CPUC has never opted to adopt the ten dollar fixed charge, opting for a minimum bill option, instead. However, with the passage of AB 205 last year, the CPUC is initiating a proceeding to adopt the income graduated fixed charge, with the statutory requirements for "no fewer than three income thresholds so that low-income customers each baseline territory would realize a lower average residential monthly bill without making changes in usage."

Exploring additional options to address affordability.

The CPUC has held two *En Bancs* related to utility bill affordability, one in 2021 and another in 2022. Multiple stakeholders have proposed various strategies to reduce costs on utility bills, including utilizing the General Fund or other State funds for some utility programs. A recent example of this approach beyond the arrearages funding, includes the Governor and Legislature adopting a Strategic Reliability Reserve last year, which authorizes the Department of Water Resources (DWR) to utilize State funds to procure energy resources for electricity procurement. Other proposals include: finding other sources of funding for specified utility activities, including exploring state financing for expenditures such as transmission and other utility operations. Today’s hearing, will provide a small sample of some of the proposals stakeholders are suggesting. As is often the case, each proposal comes with its own set of tradeoffs. The hope is that these discussions can inform how future policy is shaped so that Californians can receive the affordable, reliable, safe, and clean essential utility service.