
**SENATE COMMITTEE ON ENERGY, UTILITIES AND
COMMUNICATIONS**
Senator Ben Hueso, Chair
2019 - 2020 Regular

Bill No: SB 549 **Hearing Date:** 4/24/2019
Author: Hill
Version: 4/3/2019 As Amended
Urgency: No **Fiscal:** Yes
Consultant: Nidia Bautista

SUBJECT: Public Utilities Commission: rates: capital structure changes

DIGEST: This bill requires the Legislature to approve a capital change structure or increase in rates for the energy utility, Pacific Gas and Electric (PG&E) Company.

ANALYSIS:

Existing law:

- 1) Establishes the California Public Utilities Commission (CPUC) has regulatory authority over public utilities, including electrical corporations. (California Constitution, Article XII)
- 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) Requires that any governmental regulatory commission with jurisdiction, after confirmation of the reorganization plan of a debtor in bankruptcy protection, over the rates of the debtor has approved any rate change provided for in the plan, or such rate change is expressly conditioned on such approval. (U.S. Bankruptcy Code §1129)

This bill:

- 1) Authorizes the CPUC to approve a capital structure change or increase in rates for PG&E only upon the Legislature, by statute, approving the capital structure change or increase in rates.
- 2) Makes legislative findings and declarations as to the necessity of a special statute for PG&E.

Background

PG&E files for Chapter 11 Bankruptcy protection. On January 29, 2019, PG&E Corp., the holding company of the state's largest utility, voluntarily filed for bankruptcy protection under Chapter 11 of the United States Bankruptcy Code. PG&E filed their case in the Northern California District Court San Francisco Division (Case No. 19-30088-DM). The case has been assigned to the same judge, Honorable Dennis Montali, who handled PG&E's previous reorganization bankruptcy case in connection with the 2001 energy crisis. According to the PG&E's first day filings, in a declaration filed by the PG&E's Senior Vice President and Chief Financial Officer Jason Wells, PG&E's decision to seek relief under Chapter 11 "were necessitated by a confluence of factors resulting from the catastrophic and tragic wildfires that occurred in Northern California in 2017 and 2018, and PG&E's potential liabilities arising therefrom." The declaration specifically cites PG&E's potential liability related to the fires could exceed \$30 billion. PG&E's decision to voluntarily file for bankruptcy protection has raised numerous questions about the process entailed under a Chapter 11 reorganization and the potential implications for the numerous stakeholders that could be affected, including wildfire victims, ratepayers, the utility workforce, energy and other suppliers, local governments, and many others.

Cost of capital. A utility's Rate of Return (ROR), or Cost of Capital (CoC), is the weighted average cost of debt, preferred equity, and common equity a utility has issued to finance its investments. Return on Equity (ROE) is the ratio of a utility's net income over its rate base common equity. The CPUC attempts to set the authorized ROR at a level that is adequate to enable the utility to attract investors to finance the replacement and expansion of its facilities so it can fulfill its public utility service obligation. In practice, this level is determined by comparing market returns on investments for other companies with similar levels of risk. The debt and equity percentages are determined by the CPUC during the CoC proceeding, and together are known as the authorized capital structure. Since equity is more expensive than debt and increasing debt ratio beyond certain point increases the likelihood of default, the authorized equity ratio should be as low as possible consistent with maintaining the utility's financial strength. A decline in the equity ratio below the optimum equity ratio may impact the company's credit rating and thus could expose the ratepayers to additional default risk. CoC is determined by the CPUC for the large utilities – PG&E, Southern California Edison (SCE), Southern California Gas Company (SoCalGas), and San Diego Gas & Electric (SDG&E) – in a single proceeding. The last CoC adjustment occurred in 2017 (D. 17-07-005), in that decision the CPUC extended the next filing date for a CoC application to April 22, 2019.

General Rate Case (GRC). All utilities regulated by the CPUC are required to undergo a GRC whereby the utility requests funding for distribution, generation and operation costs associated with their service. The GRCs are major regulatory proceedings and provide the CPUC an opportunity to perform an exhaustive examination of a utility's operations and costs with input from all stakeholders, representing consumers, business and other interests, including the formerly known, Office of Ratepayer Advocates (ORA) whose accountants and analysts closely exam the requests of the utilities. Usually performed every three years and conducted over roughly 18 months, the GRC allows the CPUC to conduct a broad and detailed review of a utility's revenues, expenses, and investments in plant and equipment to establish an approved revenue requirement. Through the GRC, a utility forecasts how they will structure their operations and make investments for the next three years. Within the adopted GRC decision, a utility may be allocated funds by broad categories, although specific projects are not detailed-out or monitored.

Comments. This bill would require the Legislature to approve any change to PG&E's capital structure or any increase in rates before the CPUC can approve these changes. While mechanically unclear in this bill, it could be that the author intends for the Legislature to approve any change in the cost of capital proceeding and in the utility's GRC. The author is accurate to note a number of bills whereby the Legislature weighed in on the specifics of a CPUC rate-related case, including SB 1090 (Monning, Chapter 561, Statutes of 2018) where the Legislature overturned a CPUC decision related to the decommissioning process and employee bonus and school district compensation for the PG&E Diablo Canyon nuclear generating facility. Nonetheless, the proposal to have the Legislature approve a CPUC CoC or GRC proposed decision seems to be unprecedented. Whereas the CPUC is authorized with plenary power to oversee the operations of an investor-owned utility, including PG&E, and the CPUC has hundreds of staff available to assist with such a review, it is questionable whether the Legislature has the staffing capacity to thoroughly review such a proposal. Moreover, it raises questions as to the appropriateness of regulating rates at the Legislature, when the CPUC has been established for this very purpose. As an extension of the Legislature's authority, the CPUC has a number of tools at its disposal to review the PG&E proceedings, including the bankruptcy reorganization plan that will be proposed at some point in PG&E's bankruptcy court process. Requiring the Legislature to approve such plan before it is approved by the CPUC may be useful to ensure the priorities of the Legislature are reflected in the plan. However, it is very likely there will be aggrieved parties – be they energy generators, wildfire victims, or employees- it will likely be difficult, at best, for the Legislature to manage the complexity of the plan. The Legislature would be wise to enter into such an approach with caution

so as not to create a situation that could prevent the utility from exiting from bankruptcy in as expeditious of a time as possible.

Prior/Related Legislation

SB 550 (Hill, 2019) would require specified safety-related actions before the CPUC can authorize a merger or sale of an investor-owned utility.

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

SUPPORT:

None received

OPPOSITION:

None received

ARGUMENTS IN SUPPORT: According to the author:

“SB 549 prohibits the CPUC from approving changes in rates of PG&E without Legislative authorization. SB 549 ensures Legislators have more oversight of PG&E ratemaking, ensuring PG&E ratepayers are protected – both financially and with safe service. Currently, the Legislature has few explicit constraints on the CPUC’s ratemaking authority. PG&E rate changes can manifest during the approval of a bankruptcy reorganization, an updated cost of capital proceeding, or in PG&E’s next general rate case. SB 549 acknowledges the unique financial and legal circumstance of PG&E, and the difficulty posed by the large liabilities the company faces to adequately balance safe and reliable electric service, by providing oversight of both PG&E and the CPUC.”

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