BEFORE THE PUBLIC UTILITIES COMMISSION

OF THE STATE OF CALIFORNIA

Order Instituting Rulemaking to Implement Public Utilities Code Section 451.2 Regarding Criteria and Methodology for Wildfire Cost Recovery Pursuant to Senate Bill 901 (2018).	Rulemaking 19-01-006 (Filed January 10, 2019)

COMMENTS OF THE COUNTIES OF MENDOCINO, NAPA, AND SONOMA ON R.19-01-006

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In accordance with Rule 6.2 of the Commission's Rules of Practice and Procedure, and the schedule set forth in the Order Instituting Rulemaking, the County of Mendocino, the County of Napa, and the County of Sonoma submit these comments on the OIR.

I. COMMENTS ON R.19-01-006

The OIR presents three overarching questions regarding the factors the Commission might take into account when assessing a utility's financial status under Public Utilities Code Section 451.2(b), how the Commission might define "material impact" on a utility's ability to provide safe and adequate service, and how the Commission should define harm to ratepayers. The Counties address these questions in turn. Because Section 451.2 is specific to costs and expenses arising from the 2017 wildfires, the Counties' comments are focused on future cost recovery by PG&E.

At the outset, the Counties note that the financial balancing test contemplated by SB 901, which directs the Commission to weigh harm to ratepayers and material impacts to the utility's ability to provide safe and adequate service, is out of date. SB 901 was drafted, amended, and signed into law before the devastating Camp Fire in November 2018 and before PG&E suffered its final credit downgrades and filed for Chapter 11 bankruptcy protection. PG&E's customers have therefore already been harmed by the increased cost of borrowing, the looming prospect of post-bankruptcy rate increases, the utility's poor credit rating, and the bankruptcy proceeding; these same factors have also materially impacted PG&E's ability to provide service, as discussed in Section B below. The question, then, is how to prevent further harm to ratepayers and further impacts to PG&E's ability to provide safe and adequate service.

A. What factors or financial metrics should the Commission consider when examining an electrical corporation's "financial status"?

1. Debt/Equity ratios and changes to capital structure

The capital structure set for a utility by the Commission determines the authorized cost of capital and rate of return. The utility's authorized capital structure may differ from its actual capital structure, which depends on how the utility manages its capital needs. Significant changes in a utility's use of existing authority to issue equity or assume debt, however, should be examined when determining the utility's financial status. New debt or equity may be an indication of financial distress, or it may simply be a reflection of market conditions.

2. Net income

The amount of net income incremental to the utility's authorized revenue requirement should be considered in assessing the company's financial status and should be used to mitigate ratepayer cost responsibility. Income in excess of the revenue requirement is not collected in exchange for providing, or in order to provide, utility service. This income would ordinarily inure to the benefit of shareholders or be treated as retained earnings, and should be considered funds available to the utility for satisfying wildfire-related financial obligations. Funds recorded in memorandum or balancing accounts, while accounted for differently than funds collected as a straightforward revenue-requirement item, should not be included in the incremental net income calculation.

3. Retained earnings

Retained earnings should be treated in the same manner as incremental net income.

4. Credit ratings

The lower the utility's credit rating, the higher the cost of borrowing for the utility's ratepayers. In the case of the 2017 wildfires, PG&E's credit rating is at junk status because of harm already inflicted by PG&E on its customers and the significant potential liability arising from that harm. The Commission might consider allowing customer recovery of any borrowing that is deemed prudent, but at an imputed interest rate that would be available to a financially healthy utility. For instance, PG&E's customers might be responsible for the costs of borrowing at the interest rate that would have been available to PG&E with its pre-2017-fire credit rating. The shareholders/utility will bear the cost of the difference between the lower imputed rate and the actual interest rate.

5. Changes to the ability of the electrical corporation to pay dividends

This should not be taken into consideration. PG&E suspended dividends in anticipation of significant wildfire-related liability more than a year before filing for Chapter 11 bankruptcy protection. Even at the time it decided to file for reorganization, PG&E had funds available to it. Whether the utility chooses not to issue dividends, or says it is unable to, is subjective and should not be considered.

6. Equity issuances by the electrical corporation

Because equity issuances are a source of non-revenue requirement income for the utility, and are a measure of the utility's financial health, the Commission should consider new equity issuances by the utility since the 2017 fires, including the number and price of the shares. Any revenues from new equity that are not used to fund the provision of utility service to customers should reduce ratepayer cost responsibility.

7. Current outstanding debt and terms of debt issuances

As with the utility's credit rating, current outstanding debt should be considered when assessing the utility's financial status. Customers' interests are best served when the utility can borrow at a reasonable interest rate; the terms of any outstanding debt will show whether the utility was able to obtain a reasonable rate, when compared to pre-wildfire borrowing. The Commission should also review whether the borrowed funds are being used to provide safe and reliable utility service.

8. Current insurance costs and coverage amounts

Assuming the Commission continues to find that liability insurance, even if drastically more expensive, is an expense appropriately borne by the ratepayers, the cost of insurance should not be taken into consideration as part of the utility's financial status. The level of coverage should be considered only in terms of the funds available to pay claims. These funds will affect the utility's financial status, but the funds are not paid by the utility. To the extent coverage is available to reimburse the utility for wildfire-related losses, those amounts should reduce ratepayer cost responsibility.

9. Outstanding liabilities and assets

From a wildfire damages point of view, outstanding liabilities should be considered in assessing the utility's financial situation if they are not speculative. Treating potential future liabilities as real obligations will improperly diminish the funds available to pay existing obligations. If the liability was incurred as a result of utility negligence, actions or decisions determined by the Commission to be unreasonable, or under inverse condemnation, the liability should be borne by the shareholders.

From a day-to-day bookkeeping point of view, outstanding liabilities (such as accounts payable) and assets should not be a significant factor in the utility's financial situation, unless the utility is significantly in arrears on its obligations or has a significant under-collection issue or failure to maintain its assets.

10. Borrowing ability and ability to raise equity

As discussed above, the ability to borrow and raise equity are indications of overall financial health and should be considered.

B. How should the Commission define a "material impact" on a utility's ability to provide safe and adequate service under Section 451.2(b)?

As the Counties noted at the outset of these comments, the financial balancing test contemplated by SB 901 has been essentially rendered moot by the Camp Fire, PG&E credit downgrades, and PG&E's bankruptcy filing. The traditional metrics that have been used to determine if a utility's ability to provide safe and adequate service—such as changes to costs of debt or capital, inability to fully recover costs, reduced ability to raise capital for investment or issue equity—are not useful to measure potential harms to utility service and customers from costs arising from the 2017 wildfires because these events have already transpired. The two most significant financial events in PG&E's recent history illustrate the limited usefulness of the available measures to address the current situation. When determining whether imposing a penalty of over $2 billion on PG&E for its conduct related to the San Bruno natural gas pipeline tragedy, the Commission found that PG&E, which retained its investment-grade rating, could issue $2.45 billion of non-revenue producing equity without unfavorably impacting ratepayers or the utility's ability to issue dividends.[1] PG&E's credit rating is now hovering near "junk" status. During its bankruptcy after the energy crisis, PG&E's credit rating was as poor as it is today,[2] which is why restoring the utility to an investment-grade rating was the cornerstone of the settlement agreement the Commission adopted to bring PG&E out of bankruptcy. But the Commission had no reason in 2003 to contemplate the financial effects of significant future cost disallowances due to catastrophic harm caused by the utility.[3] Now, the question posed by Section 451.2 is how to measure a material impact on PG&E's ability to provide safe and adequate service where it is facing substantial cost disallowances from wildfires started by its equipment, while it has no credit rating to speak of and is at the start of Chapter 11 reorganization.

Looking at the traditional metrics, PG&E's ability to borrow at its pre-wildfires interest rate(s) will be negatively impacted, and it is likely that customers will bear the resulting increased costs. SB 901 has decreed that PG&E will not be able to recover all of its 2017 wildfire-related costs. And PG&E's Chapter 11 bankruptcy filing has made it impossible to determine the circumstances under which the utility might be able to raise capital, issue equity, or even what assets it will ultimately retain.[4] PG&E's poor credit rating and the inevitably higher cost of post-bankruptcy borrowing should be taken into account as harms to customers—and should offset customer cost responsibility, as described above—but these financial impacts are not theoretical harms to be warded off by limiting utility shareholder cost responsibility to a certain amount. PG&E's ability to provide safe and adequate service has already been materially

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[1] See D.15-04-024, pp. 62–68.
[2] See, e.g. D.03-12-035, p. 41.
[3] *Id.* at pp. 48, 49–51, Findings of Fact.
[4] The approximately $5.5 billion in Debtor-In-Possession funding PG&E obtained by encumbering all of its assets is not likely to be a useful measure of PG&E's future ability to raise capital, given the unique circumstances of the transaction.

impacted and its customers have already been harmed. Because PG&E's credit rating cannot be downgraded much further, and because PG&E's finances are in stasis until it emerges from bankruptcy, there is not likely to be a significant incremental material impact to service or harm to customers under these criteria. When the Commission finally considers an application for recovery of costs resulting from the 2017 wildfires, there will be no harms left to stave off—other than a diminution in actual utility service.

The practical impacts to PG&E's ability to provide service are easier to quantify: brown- and blackouts; failure of infrastructure and equipment due to lack of maintenance or inspection; reduction in workforce; reduction in the scope of daily operations and maintenance activities; default on Power Purchase Agreements. These events would put customers' safety and health at risk. PG&E's revenue requirement and any equity funds that are necessary to provide utility service should not be reduced. Neither should PG&E's customers pay for the costs of repairing the damage caused by the 2017 wildfires, because they have already been harmed by increased rates, lost homes and personal belongings, and lost loved ones.

The Commission should therefore start its analysis of any 2017 wildfire costs PG&E seeks to recover from the premise that PG&E's customers, having already suffered harm and a diminution in PG&E's ability to provide safe and adequate service, should not be responsible for additional costs beyond those necessary to fund daily utility service. The Commission can examine the potential incremental impacts from shareholder cost responsibility for the wildfire expenses—increased borrowing costs, reduced ability to issue equity to fund utility operations, etc.—and determine how much of the wildfire costs the shareholders can bear in a given calendar year; the balance can be amortized to the shareholders over a reasonable period of time or subject to financing that does not pass costs on to customers.

C. How should the Commission define harm to ratepayers under Section 451.2(b)? What measures or metrics should be used in determining whether ratepayers are harmed?

As discussed in Section B, the downgrade in PG&E's credit rating and its Chapter 11 bankruptcy have harmed ratepayers. The inevitable increased costs associated with PG&E's bankruptcy will also harm its customers. And any actual diminution in the reliability or safety of utility service would be a significant harm.

For purposes of assessing harm to customers under these circumstances, the Commission should look at incremental impacts from wildfire-related costs, whether from further-reduced credit ratings, new debt at interest rates above PG&E's pre-2017 wildfires rates, or reduced ability to issue equity to fund utility operations. These impacts would further increase costs for customers.

Requiring customers to bear the costs of any financing to cover the portion of the disallowed wildfire costs that fall outside the financial "stress test" cutoff would also harm PG&E's customers and would violate the basic principles of utility ratemaking. Any such financing must be non-revenue producing[5] or must otherwise be structured so that customers do not bear any of the costs.

II. OTHER ISSUES

A. Categorization, Need for Hearings, and Schedule

The Counties do not object to the categorization of this proceeding as ratesetting, or the preliminary determination that hearings will not be needed. The Counties also have no objection to the preliminary schedule set forth in the Rulemaking.

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[5] Cf. D.15-04-024, p. 63.

III. <u>CONCLUSION</u>

As the Commission undertakes to develop the methodology by which costs arising from the 2017 wildfires are assigned to shareholders and customers, it must bear in mind that the facts have changed significantly since SB 901 was enacted, and the analysis of what constitutes harm to customers and material impacts to PG&E's ability to provide safe and reliable service must also change. While the Commission will have a number of tools to assess PG&E's financial status, the fact remains that the utility's credit downgrade and bankruptcy filing have already impacted its ability to provide service and caused its customers harm. The financial "stress test" ultimately developed in this proceeding must not increase that harm or diminish safe and reliable service.

Respectfully submitted February 11, 2019, at San Francisco, California.

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