Energy Division

California Public Utilities Commission

DATA REQUEST	
Date:	March 7, 2022
Originator:	Bridget Sieren-Smith
Email:	bridget.sieren-smith@cpuc.ca.gov
Due Date:	March 21, 2022
Subject:	**2022 SB 695 Report IOU Recommendations to Limit Cost and Rate Increases (Electric and Gas IOUs)**
Priority:	**Time-Sensitive**

Please provide the information as requested below. Please submit your response to this data request directly to Bridget Sieren-Smith (bridget.sieren-smith@cpuc.ca.gov). Questions regarding this data request should be immediately directed to the Originator.

This data request is issued regarding proposed recommendations of the investor-owned electric and gas utilities (IOU) to limit cost and rate increases consistent with the state's energy and environmental goals for reducing greenhouse gases, as required by Public Utilities Code Section 913.1. The data provided in the response will be included in its entirety in an appendix to the 2022 SB 695 Report.

In preparing your response, the IOUs are encouraged to be as specific as possible in identifying and quantifying specific potential cost savings initiatives.[1] While recognizing that the utilities generally propose cost savings initiatives in Test Year General Rate Cases (GRC), Public Utilities Code Section 913.1 annually requires that the utilities:

> "…study and report to the commission on measures that they recommend be undertaken to limit costs and rate increases."

In addition to studying and reporting on specific measure that each IOU recommends be undertaken to limit costs and rate increases,[2] please study and report on the following topics, drawn from the Affordability Rulemaking Phase 3 En Banc held February 28th and March 1, 2022:

- Implement an income-based fixed charge with the amount charged progressively increasing for higher income households.
- Implement a percent of income payment plan program at scale, specifically commenting on potential sources of non-ratepayer funds to fund a full-scale program.
- Move wildfire mitigation costs to the General Fund.
- Reduce IOUs' authorized Return on Equity.
- Reduce GRC phase I anchor bias through evaluation of required alternative scenario(s).
- Implement rate or infrastructure planning mechanisms to avoid excessive gas infrastructure costs falling disproportionately on residential customers who cannot electrify.

[1] Data reflecting rates trends, cost recovery mechanisms, types of cost recovery proceedings, and other data non-specific to studying and reporting on measures recommended to limit cost and rate increases should not be included, except to the extent that such data directly supports the recommendations.

[2] For dual-fuel utilities, please include at least one item related to gas.

SCE's Response

Introduction

SCE is focused on minimizing costs for our customers as we provide safe, reliable, and clean electricity service and we look forward to continuing to work with stakeholders in the Affordability Rulemaking proceeding to explore additional opportunities and solutions. However, no solution should inhibit the utilities' ability to maintain safe, reliable service or impede achievement of the state's clean energy goals. Indeed, SCE's Pathway 2045 whitepaper demonstrates that decarbonization can be cost-effectively achieved through powering customers' energy needs with carbon-free electricity, and electrifying transportation and buildings. The analysis finds that while a customer's electricity bill increases over time, the overall energy consumption cost for an average household that adopts decarbonization solutions decreases by one-third by 2045.

One of the ways SCE is attempting to reduce costs and limit customer rate increases is through the deployment of customer-funded self-insurance, which can displace some of SCE's traditional commercial wildfire liability insurance. Both customer-funded self-insurance and commercial liability insurance protect customers from third-party claims for damages when SCE's equipment is alleged to have been associated with a wildfire. However, the premiums for commercial wildfire liability insurance have grown increasingly expensive over recent years, and, like most insurance products, the policies expire after the conclusion of the policy year, whether or not SCE experiences a covered loss. Customer-funded self-insurance, on the other hand, can be "banked" and built up over time if SCE does not experience a loss that must be covered by this self-insurance. The 2021 SCE GRC Final Decision (D.21-08-036) specifically authorized SCE to employ customer-funded self-insurance, and to-date SCE has done so on a limited basis pursuant to that authorization. SCE may seek to increase its use of customer-funded self-insurance when it is less expensive than commercial liability insurance from a forecast actuarial-based perspective.

In addition to customer-funded self-insurance and exploring the further development of fixed charges as discussed in Part 2, SCE also referenced the following recommendations to limit cost and rate increases at the Commission's En Banc:

- Securitization of certain O&M Costs
- Funding certain public purpose program costs, such as CARE/FERA, from the California State General Fund

These initial recommendations are summarized in part 1 below, and will be described further as part of the Affordability Rulemaking's Phase 3 process for party proposal submissions.

Finally, as requested, in part 2 below, SCE is including initial comments and analysis regarding six identified proposals from the February 28 and March 1, 2022 Affordability Rulemaking Phase 3 En Banc. As indicated below, for some of these proposals, further planning, study and analysis are needed

for SCE to develop comprehensive, fully informed positions. SCE looks forward to working with stakeholders to further consider and develop proposals in Phase 3 of the Affordability Rulemaking.

1. SCE's Initial Recommendations to Limit Cost and Rate Increases

a. Securitization of Certain O&M Costs

Under normal circumstances, SCE would seek recovery of all O&M expenses in rates in the period they are incurred or immediately upon a determination that they are just, reasonable, and consistent with long-standing cost of service ratemaking principles. However, the current need to take additional critical measures to protect customers from catastrophic wildfires coupled with challenging economic conditions resulting in part from the COVID-19 pandemic warrant a different approach. Securitization, for certain exceptional O&M expenses and/or during periods of economic uncertainty, is an important tool that supports both customer affordability by reducing near-term rate increases and utility financial health by maintaining compensatory cost-of-service ratemaking.

Existing authorizing legislation (*i.e.,* Assembly Bill (AB) 1054 and AB 913) allows for the securitization of wildfire mitigation-related O&M expenses, wildfire-related claims payouts above insurance, wildfire-related restoration expenses and 2020 incremental uncollectibles expense. Additionally, in Decision (D.) 21-10-025, the Commission determined that AB 1054 does not preclude the Commission from considering securitization of wildfire mitigation expenses that provide both short-term and long-term economic benefits to customers.[3] However, the Commission has not yet used this existing authority to approve securitization for wildfire-related O&M. Utilizing this securitization authority would aid in supporting critical near-term utility grid hardening activities while also minimizing bill increases, particularly for SCE's most economically vulnerable customers. This is because, under the current statute, SCE's income-qualified customers are exempt from the Fixed Recovery Charges (FRCs) used to recover securitized costs.[4] If SCE had been allowed to securitize approximately $478 million of 2018-2019 wildfire mitigation O&M and a portion of its 2020 incremental uncollectibles as proposed in its June 2021 Application for Authority to Issue Recovery Bonds, CARE customers would have seen an average monthly bill reduction of $3.13 compared to traditional financing.[5] There are also near-term rate reductions for customers who are responsible for securitized costs because these amounts go into rate levels at a significantly lower amount compared to traditional compensatory recovery of O&M expenses (e.g., in the prior example, instead of increasing rate levels by $478 million in a single year, the rate increase in the first year related to the securitized costs would have been approximately $25 million). These near-term rate reductions are particularly important at a time when rate pressures on these vulnerable customers can be significant and economic circumstances are uncertain.

[3] *See* D.21-10-025. p. 15.

[4] Public Utilities Code Section 850.1(i) requires that utilities exclude the Fixed Recovery Charge from the utility bills of customers who participate in the CARE and FERA programs.

[5] *See* SCE's Opening Brief in A.21-06-016, pp. 2-3.

SCE's customers further benefit from this type of financing because unlike lengthy and non-compensatory amortization periods, targeted securitization is excluded from SCE's credit metrics. Better credit metrics represent improved financial health and support lower costs of traditional financing, which benefit current and future customers. That said, there is a limit to how much of SCE's revenue can be securitized while still receiving a AAA rating that allows for low interest rates.[6] As such, SCE intends to assess any broader use of securitization based on the then-current environment and does not consider it to be the default tool for financing business-as-usual investments. However, given the benefits to customer affordability and corresponding utility financial health, securitization is a tool that should be authorized when conditions warrant such action. The opportunity already exists today for the Commission to approve greater use of securitization to the benefit of customers, particularly for wildfire O&M expenses.

b. Accessing State General Funds for CARE/FERA Costs

SCE supports using state or federal funding for extraordinary costs or costs not directly linked to cost-of-service and is assessing components of customers' electric bills appropriate for accessing state general funds to offset costs. SCE is also evaluating opportunities to pursue federal funding under the Infrastructure Investment and Jobs Act.

In addition to the criteria the Commission laid out at this year's Affordability En Banc, there are additional key criteria to evaluate when considering which costs currently funded through utility bills are more appropriately funded using state funds.

First, any proposals to utilize non-ratepayer funding must not impede or impact a utility's ability to provide safe and reliable electric service. As a result, any adjustments to programs and funding need to maintain or exceed current levels of safety and reliability. Second, it is necessary to consider whether accessing state general funds will improve, or at the very least not inhibit achievement of California's climate and clean air objectives, given that achieving those goals through mass electrification will result in lower total energy burden for customers. Third, the operational complexity of accessing the state's general fund to offset customer costs for certain programs should be considered to ensure that any adjustments to existing programs and costs do not create new risks or points of failure, or amplify levels of administrative burden, any of which could ultimately result in less efficient and more costly services. As such, the most effective approach would be to leverage existing approval processes and cost recovery mechanisms through the CPUC and other state agencies to access general funds and offset customer costs where appropriate. For example, the Commission could approve an offset to SCE's already-authorized funding for any amounts made available by the California legislature. In addition, for any funding SCE receives, the existing cost recovery mechanisms are already designed to allow for state funding to offset authorized revenue to be collected from customers (e.g., through a credit to a balancing account, reducing the amount recovered through customers' rates). This approach maintains existing review and approval processes, reducing delays and operational

[6] Fitch's limit on AAA-rated securitization debt allows for the fixed recovery charge from securitization to rise only as high as 20 percent of the amounts otherwise in rates.

complexity, and would in turn benefit customers by minimizing potential disruptions or fluctuations in program funding and approval.

Against this backdrop, SCE is supportive of continuing to seek opportunities to utilize non-ratepayer funding for certain public purpose programs and other activities that are not specifically related to a utility's cost of service but are paid today through electric rates. For example, the program costs and subsides associated with SCE's income-qualified CARE and FERA programs would be appropriate to fund with state funds, given that they provide valuable assistance for income-constrained customers, reflecting a beneficial public good beyond the utilities' operations and services. This action satisfies the evaluation criteria outlined above (i.e., would not negatively impact SCE's safety and reliability, would not jeopardize the state's climate goals, and would not likely add unreasonable operational complexity if administered by crediting a balancing account as referenced above). Fully funding CARE / FERA subsidy costs with state funds would result in a meaningful rate reduction for non-participating customers, improving the affordability of electric bills. The benefit could be even more significant if the state chooses to not only fund the costs through the general fund, but also were to expand the eligibility criteria or the size of the subsidy as well.

2. Affordability Rulemaking Phase 3 En Banc Proposals

a. Potential frameworks for an income-based fixed charge

SCE is encouraged by the suite of fixed charge proposals discussed at the 2022 Affordability En Banc. Residential graduated fixed charges that vary as a function of income, or a proxy thereof, can advance affordability and bring greater cost recovery equity to the residential class. A graduated fixed charge structure addresses affordability concerns across the spectrum of residential customers. The broad application of fixed charges reduces volumetric charges for everyone within the class relative to the current structure, which improves equity of cost recovery across the class. The income-graduation provides a more progressive overall pricing structure for income-qualified customers, and the lower volumetric charges improve affordability of electrification technologies by facilitating rate structures that can reduce energy burdens for high volume customers.

Creating a purely income-graduated fixed charge using tax information, or other sources of income information, may prove complex for a utility's customer service and billing operations. The use of third-party income data would necessitate that the utility performs periodic review and assessments of the various provisions of the tax code and third-party sources related to a customer's income. The utilities would also be required to develop a methodology to account for low-income customers who may not show up in taxing authority data. These are just a few of the complexities. Developing workable solutions to these considerations will take time. Given the Commission's immediate priorities around affordability and electrification, graduated fixed charge approaches that rely primarily on a utility's current suite of tools should be explored in the near-term. As experience with graduated fixed charges grows and associated systems and processes are developed, it may be appropriate to explore other approaches to graduating residential fixed charges that are more reliant on tax authority information.

As an initial step, the Commission should consider an approach that uses the income gradation currently existing in rates. For SCE, CARE customers receive an effective 32.5 percent bill discount and FERA customers receive an effective 18.2 percent discount. When taken together with a non-CARE fixed charge, this structure represents a basic 3-level income-based fixed charge approach. Additional low-income policy adjustments informed by Commission policy, academic research, or utility cost studies can be considered if appropriate.

SCE performed a high-level calculation of graduated fixed charges at various levels (i.e., fixed charge steps) based on current rate levels, the current equal percentage of marginal costs (EPMC) scalar representing the amount of revenue recovered above the marginal cost level reflected in the retail rate, and a stepped distribution similar to the "As Progressive as Income" example presented in the Energy Institute at Haas study regarding income-based fixed charges[7]. In this illustrative example, SCE's average monthly non-CARE graduated fixed charge is $53/mo. When this average is normalized to the income-based fixed charge distribution in the Haas Institute paper[8], an income-based fixed charge range of $24/mo. to $153/mo. is produced. SCE is evaluating further potential details associated with the Haas structure and will include recommendations as part of forthcoming party proposals in Phase 3 of the rulemaking, in accordance with the framework requested by the Commission for participant proposals.

In addition to income-based fixed charges, SCE intends to explore the potential of designing fixed charges that are based on the inherent consumption and load characteristics of the class and which can then be complemented by a sliding scale of discounts that align with the existing framework of income distribution across the class, namely CARE and FERA programs. By designing fixed charges using these different approaches, SCE will be able to test the efficacy of these designs using data and systems that are already in its inventory, such as the approach discussed in Shaun McRae and Frank Wolak's[9] study regarding income-based fixed charges in Colombia.

It also bears noting that existing statutory requirements in Public Utilities Code Section 739.9 limit the ability of the described graduated fixed charge framework to fully address affordability concerns and facilitate GHG reductions, and thus those limitations will likely need to be addressed through future legislative action. For example, the statute sets a $10 per month cap on default rate fixed charges. As fixed charge proposals are evaluated further, stakeholders and the Commission will need to consider and recommend corresponding legislative action that would facilitate appropriate and effective fixed charges to benefit customers.

b. Implement a percent of income payment plan program at scale, specifically commenting on potential sources of non-ratepayer funds to fund a full-scale program.

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[7] Borenstein, Severin, Meredith Fowlie, and James Sallee. "Designing electricity rates for an equitable energy transition." *Energy Institute at Haas working paper* 314 (2021).
[8] Fig. 9b on page 41 of the Energy Institute at Haas paper Designing Electricity Rates for An Equitable Energy Transition.
[9] McRae, Shaun D., and Frank A. Wolak. *Retail pricing in Colombia to support the efficient deployment of distributed generation and electric vehicles.* No. IDB-WP-01021. IDB Working Paper Series, 2020.

The Percentage of Income Payment Plan (PIPP) pilot, authorized in Decision (D.)21-10-012, will cap a customer's monthly bill amount based on a percentage of the customer's household monthly income. The goals for the four-year pilot are to determine whether a PIPP program can (i) reduce the number of low-income households at risk of disconnection, (ii) encourage participation in energy saving and energy management programs, (iii) increase access to essential levels of energy service, and (iv) control program costs.[10]

An integral component of the PIPP pilot is the evaluation report, which will use at least the first 18 months of data based on the statewide 15,000-customer participation cap. This report will 1) determine whether modifications to the pilot should be made to meet the goals established in D.21-10-012, and 2) inform the design and consideration of a potential long-term PIPP program. D.21-10-012 also ordered the recovery of electric costs through the Public Purpose Programs Charge (PPPC) but noted that this cost recovery mechanism would not set a precedent for potential program expansion. Furthermore, the Decision orders that incremental administrative costs be recorded in a new PIPP memorandum account that is subject to a reasonableness review by the Commission.[11]

On February 4, 2022, SCE submitted Advice 4710-E to implement its PIPP pilot. The pilot is to begin within 45 days of the advice letter approval, which is still pending.[12] Given the forthcoming pilot, consideration of any long-term, full-scale PIPP program, including comments about program viability and feasibility, should take place only after the pilot and subsequent evaluation report address the various questions outlined in D.21-10-012, such as how much did the pilot subsidies cost, net of CARE subsidies, how the PIPP pilot administration cost compared with estimates, understanding the "net benefit" to a CARE customer when enrolling in the PIPP pilot versus what they would have received under CARE alone, and how the pilot affected participants' energy usage behavior. In comments preceding D.21-10-012, SCE recommended that a balancing account be used to record the PIPP pilot bill subsidies and that these subsidies be recovered through the PPPC from all customers.[13] Outside of this construct, SCE is supportive of accessing external sources of funding, such as California's general fund, to support any future iterations of PIPP.

c. Move wildfire mitigation costs to the General Fund

Cost recovery for approved IOU wildfire mitigation activities should be covered by the most stable funding source possible. "Moving" wildfire mitigation funding to California's general fund could introduce an unnecessary and unpredictable level of volatility for this critical utility infrastructure-based safety work. Any reduction of IOU control and oversight of IOU wildfire mitigation activities may introduce unnecessary safety and reliability risks to critical infrastructure. Furthermore, unlike the CARE and FERA costs discussed above, these wildfire mitigation activities are a core part of delivering safe, reliable electric service, and should be treated as such.

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[10] D.21-10-012, Attachment A, p. 1.
[11] D.21-10-012, p. 66.
[12] D.21-10-012, OP 4.
[13] *See* SCE's Opening Comments ALJ's E-mail Ruling Requesting Comments on Four Questions Concerning the Percentage of Income Payment Plan in R.18-07-005, issued on January 28, 2021, p. 4

In Part 1 of SCE's 2022 SB 695 response, SCE estimated its total 2022 wildfire mitigation costs in rates to be approximately $2.2 billion and its total wildfire insurance and response costs (CEMA) in rates to be approximately $1.4 billion. All wildfire-related forecast spend is approved in the GRC, while planned activities are approved in the WMP. SCE also has the authority to record over-authorized amounts in various memorandum accounts for later recovery from customers upon a finding from the Commission that the costs were reasonable. Given the magnitude of this spend and the importance of this work to protect public safety, SCE is not supportive of proposals that would delay or introduce uncertainty into SCE's ability to mitigate and respond to catastrophic wildfires. In terms of safety and reliability, SCE's wildfire mitigation measures from 2018 – 2021 resulted in more than 2,900 miles of covered conductor installed, over 890,000 inspections performed on our transmission and distribution assets, nearly 360,000 hazard trees assessed adjacent to SCE's power lines, more than 1,460 weather stations and 166 high-definition cameras installed for improved situational awareness, over 6,700 critical care back-up batteries provided to customers to minimize the impacts of PSPS, and more. Anything that impacts our ability to expeditiously mitigate and respond to wildfire risk through activities like these would not be in our communities' interest.

As discussed above in Part 1(a), existing authorizing legislation (*i.e.,* Assembly Bill (AB) 1054 and AB 913) currently allows for the securitization of wildfire-related O&M expenses, which is an appropriate tool to use as conditions warrant to reduce the near term rate impacts to customers.

d. Reduce IOUs' authorized Return on Equity

Customer and shareholder interests are linked and balanced under California's well-established regulatory framework. Put simply, an IOU cannot make the necessary investments to provide safe and reliable service to customers without a fair return on its capital investments (including wildfire-related investments, resiliency, and clean energy investments to meet state electrification goals). The construct of establishing an IOU's authorized Return on Equity (ROE) in line with its cost of equity is a fundamental tenet of the regulatory framework, and reducing an authorized ROE does not mean that an IOU's cost of equity is thus reduced. A mismatch of these creates incentives for investors to look elsewhere.

Under our state's regulatory framework, customers are provided with universal service and regulated cost-based rates. Reasonableness review and CPUC oversight further incentivize the IOUs to operate cost effectively and to make prudent investments and decisions. Additionally, instead of requiring customers to provide the entire cost of capital investments up front, the IOUs finance the up-front capital costs and then spread the recovery of those costs over many years. In exchange, the IOUs have the opportunity to recover their just and reasonable costs from customers including a fair return on capital investment, as measured by the cost of obtaining capital in a competitive capital market. A fair return opportunity is vital to ensure the IOUs are able to efficiently raise sufficient capital to make improvements to infrastructure and provide safe and reliable service to all customers.

Critically, a Return on Equity that fails to adequately compensate investors for their risk would lead to increased customer costs in the long run by impairing key credit metrics that rating agencies use to evaluate and establish SCE's credit rating, including cash flow to debt ratios. In addition to credit metrics, ratings agencies review the regulatory environment of an entity as part of their ratings process, and actions they view as contrary to the norms of our regulatory framework may be viewed as less credit supportive. Any ratings downgrade would result in higher debt borrowing costs that flow to customers and would require multiple years to reverse. In the long-run, higher embedded debt costs and a lower authorized ROE make it more costly to raise the capital necessary to provide essential electric service to our customers and to support California's policy priorities, and this increased cost for raising capital would result in higher customer rates.

e. Reduce GRC phase I anchor bias through evaluation of required alternative scenario(s)

SCE opposes this proposal, which would require utilities to file a CPI-constrained proposal as an alternative in their General Rate Case (GRC). This proposal is inconsistent with California's longstanding utility regulatory framework based on cost-of-service ratemaking. Moreover, this proposal ignores critical factors that SCE must consider when developing its GRC proposals. SCE's GRC proposals must balance minimizing costs with additional critical factors, which include meeting our customers' electricity service needs, providing safe and reliable service, and supporting state climate change mitigation objectives. A CPI-constrained alternative, even if not proposed as a cap, is unduly artificial and risks creating an alternative "anchor bias" toward a forecast that did not reflect SCE's cost to serve our customers' actual needs (which can exceed CPI at times). Finally, intervenors already have every ability to propose these alternatives, and the CPUC has a robust process to evaluate and determine the outcome. Thus, rather than force utilities to sponsor a case inconsistent with their costs of service and that they do not support, the CPUC should maintain the current GRC process.

f. Implement rate or infrastructure planning mechanisms to avoid excessive gas infrastructure costs falling disproportionately on residential customers who cannot electrify

SCE supports evaluating natural gas rates and affordability within Phase 3 of the Affordability Rulemaking and in coordination with the Gas Transition Rulemaking. SCE also supports the consideration of natural gas costs as they affect total energy affordability - electrification, gas system safety, and customer bill affordability are all linked.

As electrification of transportation and buildings increases, some customer electric bill costs may be offset by decreases in natural gas. Conversely, gas customers who face barriers to electrification may be left with upward pressure on gas rates as gas system costs are spread among a shrinking volume of sales. Exploring rate or infrastructure planning mechanisms to avoid gas infrastructure cost-shifting

would allow the Commission and stakeholders to better evaluate electric affordability issues in the context of fuel switching and the state's decarbonization efforts.