Date of Hearing: April 3, 2024

ASSEMBLY COMMITTEE ON UTILITIES AND ENERGY
Cottie Petrie-Norris, Chair
AB 2054 (Bauer-Kahan) – As Amended March 21, 2024

SUBJECT: Energy: employment, gifts, and rates

SUMMARY: Requires the California Public Utilities Commission (CPUC) to conduct a reasonableness review prior to a utility receiving rate recovery for any costs recorded in memorandum or balancing accounts above those authorized in a forecast. Mandates that any costs above the authorized forecast, regardless of reasonableness, shall be allocated between ratepayers and shareholders, with the ratepayers responsible for no more than 50% of the costs. Additionally includes requirements that all proposed public utility spending must include a cost-benefit analysis of at least three alternatives. Finally, prohibits leadership at the CPUC, Public Advocates Office (PAO), and California Energy Commission (CEC) from receiving gifts or employment (for at least 10 years) by any entity subject to regulation by their body.

EXISTING LAW:

1) Establishes the CEC, consisting of five members appointed by the Governor and confirmed by the Senate. (Public Resources Code §§ 25200, et. seq.)

2) Prohibits any CEC commissioner from having received any substantial portion of their income from any electric utility or any energy-affiliated business for the two years prior to their appointment. Also prohibits employment from specified energy businesses for two years following the conclusion of their service. (Public Resources Code § 25205)

3) Establishes the CPUC, consisting of five members appointed by the Governor and confirmed by the Senate for staggered 6-year terms. (California Constitution, Article XII, Section 1)

4) Prohibits any CPUC commissioner from holding an official relation to or financial interest in any person or corporation subject to regulation by the CPUC. Further prohibits public utility executives from CPUC appointments for a period of two years following employment with the utility. (Public Utilities Code § 303)

5) Establishes the PAO as an independent office within the CPUC to advocate for utility customers. Specifies that the PAO director is appointed by and serves at the pleasure of the Governor, subject to Senate confirmation. (Public Utilities Code § 309.5)

6) Mandates the CPUC to require utilities to maintain balancing accounts reflecting the balance between the related costs and revenues whenever the CPUC authorizes a change in rates. Additionally requires the CPUC to take action on any balance remaining during a subsequent rate adjustment. (Public Utilities Code § 792.5 (a))

7) Mandates the CPUC develop a risk-based approach for auditing utility balancing accounts, and to maintain an inventory of the balancing accounts. Permits the CPUC from auditing any balancing account an independent audit has reviewed in the preceding five years. (Public Utilities Code § 792.5 (b)-(f))

8) Requires the CPUC to annually report on the status of its balancing account audit activities, and to share the report publicly, as specified. (Public Utilities Code § 910.7)

9) Establishes revolving door policies for Members of the Legislature, elected state officers, and designated executive branch employees, prohibiting employment that influences their former body for one year after leaving office. (Government Code § 87406)

FISCAL EFFECT: Unknown. This bill is keyed fiscal and will be referred to the Committee on Appropriations for its review.

BACKGROUND:

Cost Recovery Processes: GRCs, Balancing Accounts, and Memorandum Accounts – Utilities employ a number of accounts to track expenses, both anticipated and unanticipated. Anticipated costs are determined through the General Rate Case (GRC) proceedings at the CPUC. The GRCs evaluate both past expenses and utility forecasts of likely future costs. They cover four years of a utility's anticipated costs. The GRC establishes how much money the utilities are allowed to collect, and a fixed escalation rate is applied to expenses for the subsequent three years captured in the GRC cycle. Once the CPUC authorizes the costs, the costs are allocated to different classes of customers and built into future billing.

Balancing accounts are typically used for costs that are expected and occur on a regular basis, but cannot be estimated accurately. For instance, the Energy Resource Recovery Account (ERRA) is a balancing account that tracks, and utilities are pre-approved to collect, costs of fuel and power purchases. These accounts are subject to audit and adjustment, but do not automatically undergo a reasonableness review. Rather the CPUC authorizes a scope of the recorded activity, and maximum level of acceptable expense, before the utility undertakes the activity. However, forecasts are imperfect. If the CPUC authorizes a forecasted amount and also a balancing account for that activity, then when actual costs are higher or lower than the authorized forecast, rates are adjusted up or down to compensate for the forecasting error. For example, in data provided to this committee Southern California Edison reported ERRA overcollections for 2019, 2020, and 2023; these overcollections were returned to customers.[1] However, 2022 ended with a $1.5 billion undercollection, primarily driven by the severe spike in natural gas prices that occurred that winter; customers paid for that undercollection.[2]

Memorandum accounts are used for activities that are likely to be a reasonable use of ratepayer funds. The CPUC does not decide on the reasonableness of the costs recorded in the

---

[1] Southern California Edison,"ERRA Analysis 2019-2023," March 28, 2024.
[2] *Ibid.*

memorandum accounts; rather they authorize the tracking of costs that *may* be reasonable. Costs recorded in memorandum accounts are subject to a later reasonableness review, with the potential inclusion in rates, but such recovery is not guaranteed. Memorandum accounts are meant to address expenditures that are much less certain than balancing accounts. For example, per statute,[3] utilities record costs incurred in responding to emergencies in Catastrophic Event Memorandum Accounts.

The differences in the account types lie in the timing and certainty of cost recovery. Memorandum accounts require a review of reasonableness before cost recovery is approved. Balancing accounts pre-approve the scope of activities and their associated costs because they are believed to be both certain and reasonable. This allows IOUs to incorporate the costs incurred in balancing accounts into rates as soon as it is practicable for them to do so.
Before the regular use of memorandum and balancing accounts, utilities were at risk of absorbing the cost of unforeseen activities until the next GRC is authorized, a process years in the making. The CPUC has noted to this committee that prior to the use of these accounts utilities were hesitant to engage in activities unforeseen during the GRC, leading to unnecessary delays. In the current era of decarbonizing our electric and gas sector and mitigating and responding to climate events, such delays might carry dire consequences.

COMMENTS:

1) *Author's Statement.* According to the author, "Energy prices are skyrocketing, and Californians deserve to know their regulators are fully independent of industry influence. Our energy system is unique because it does not function based on a competitive market. The ability of utilities to make money is determined by the Public Utilities Commission. Any conflict of interest at the commissioner endangers the well-being of ratepayers and trust in the system. AB 2054 protects ratepayers by extending the cooling-off period for Public Utilities Commissioners and Energy Commissioners to 10 years. The bill also requires stricter oversight of memorandum accounts that have ballooned in recent years, all costs covered by ratepayers. AB 2054 takes a two-pronged approach to address the root-cause and the impact of a monopolized industry. We must keep our utilities accountable and spending under control if Californians are to maintain trust in our system."

2) *Ballooning Costs, Perverse Incentives.* PAO, in their role of reviewing utility finances, has noted a growing trend of more utility expenses being recorded outside the GRC in memorandum and balancing accounts. They note over $14 billion in wildfire-related expenses alone have been requested through these accounts since 2020.[4] As noted in a

---

[3] PUC § 454.9
[4] Slide 7, presentation of Linda Serizawa, "Affordability Concerns in the Electric Sector," March 6, 2024; Assembly Utilities and Energy Committee hearing, State Capitol Room 437; https://autl.assembly.ca.gov/system/files/2024-03/2-linda-serizawa-pao-assembly-utilities-energy-hearing-final.pdf

recent State Auditor report, PAO only reviews a fraction of utility accounts.[5] Many utility accounts carry high balances, and typically do not receive scrutiny until a utility requests recovery for costs in the account.[6] In other words, that $14 billion PAO tracked may be the tip of the financial iceberg. This bill seeks cost containment by requiring any costs in these accounts above those forecasts to be split between ratepayers and shareholders, with ratepayers responsible for no more than 50%.

The sponsors of this measure cite utilities' smart-meter deployment as an example of the CPUC establishing such cost-sharing arrangements. For instance, Pacific Gas and Electric's (PG&E) smart-meter program had an approved financial structure of:

- $1.6 billion deemed reasonable and recovered in rates without any after-the-fact reasonableness review.
- 90% of up to $100 million in costs beyond the $1.6 billion would also be deemed reasonable without any after-the-fact review to cover project overruns. The remaining 10% would be absorbed by PG&E's shareholders.
- Costs in excess of the $100 million over the $1.6 billion would be recoverable only if approved by the CPUC in a reasonableness review.[7]

It is unclear to the committee how common such financial arrangements might be for utility projects – with both a cost-sharing arrangement and an overall project cap. However, the CPUC commented in the decision adopting this arrangement that the $10 million exposure to the shareholders would provide an "incentive to minimize and mitigate [project] overruns."[8] Given the ballooning costs – and subsequent increasing bills – characteristic of electric utilities of late, it may be prudent for the CPUC to again consider such arrangements.

However, this bill mandates cost-sharing. Such a requirement overlooks the potential for cost overruns to arise from force majeure events outside the utilities' control; or other, similar circumstances where a constitutional taking may result. As such, it is important that the economic regulator be responsible for balancing ratepayer versus shareholder interests; otherwise mandating cost-sharing for all project overruns may lead utilities to inflate their forecasts in order to ensure such arrangements are never reached. *In order to signal to the CPUC that such financial arrangements may be beneficial while retaining needed flexibility for the CPUC to implement, the committee may wish to amend the requirement that the CPUC provide a cost-share, and instead make the cost-share optional. Moreover, the committee may wish to delete prescriptive details allocating*

---

[5] Pg. 53, State Auditor, *Ibid.*
[6] Pg. 54, State Auditor, *Ibid.*
[7] Pg. 14, D. 06-07-027; file:///S:/autl/Legislative%20Session%202023%20to%202024/bill%20analyses/2024/Assembly/AB%202054_RBK_Conflict%20of%20Interest%20+%20rates/D.%20_smartmeter_.pdf
[8] *Ibid.*

responsibility and reasonableness terms of the cost-share, in order to allow the CPUC to establish terms as befits the circumstance.

3) *Strange Mechanics.* This bill requires cost-sharing of utility expenses that are incurred above an authorized forecast. This includes costs recorded in either a memorandum or a balancing account. As noted above, these accounts – while similar – differ in the timing and certainty of cost recovery. Memorandum accounts require a review of reasonableness before cost recovery is approved. Balancing accounts receive pre-approval of the scope of activities and their associated costs. Typically, memorandum accounts are for unforeseen circumstances, such as emergencies; as such, a forecast would be highly uncertain. Balancing accounts by their nature have forecasts and project scopes. Given this, the review structure posed by this bill for both account types may only work in practice for one. *Given the author's stated intent that this measure help alleviate ratepayer costs associated with electric utility wildfire expenses, largely concentrated in balancing accounts, the author and committee may wish to limit this measure to utility balancing accounts.*

4) *A Decade in the Waiting.* This measure also includes prohibitions on receiving gifts and post-service employment for CPUC, CEC, and PAO leadership from any entity subject to regulation or oversight of their respective bodies. Such gift and revolving door clauses are common good governance principles, and exist for members of the Legislature as well as some executive branch positions.[9] However, the degree of the prohibition put forward by this measure is significant. Namely, statute prohibits members of the Legislature from lobbying their colleagues for one year after leaving office.[10] This bill puts a 10-year freeze on any CPUC or CEC commissioner or PAO director from employment with any entity subject to their regulation. While the principle behind such a prohibition may be laudable – namely, ensuring independence between the regulated and regulator – in practice, it may have a chilling effect on the make-up of these bodies.

   While the Legislature is made up of elected officials ranging in background, education, former employment and experience – as well as specialties and areas of focus while in office – leadership at the CEC, CPUC, and PAO are often career specialists in energy and utilities.[11] Such expertise is crucial in properly evaluating regulations and ratemaking. This bill would leave these career specialists unable to return to their areas of expertise for a decade following the conclusion of their service, effectively forcing them into early retirement or the academic or non-profit sector. Such a prohibition may pose a significant barrier to getting a diverse pool of candidates for these appointments. Another unintended consequence may be rendering only out-of-state experts interested in California appointments, as more businesses in their home state are likely to not be subject to

---

[9] GOV § 87406
[10] This period is extended when a lawmaker leaves office earlier in their term.
[11] Exceptions to this observation do, of course, exist; even recently.

regulation by the CEC or CPUC enabling them to more easily return to their careers following their service. As written, this prohibition seems imprudent. *The committee may wish to retain a revolving door policy for these appointees, but reduce the time period to 3 years.*

5) *Related Legislation.*

AB 3256 (Irwin), requires the CPUC to annually determine if each memorandum and balancing account has achieved its intended purpose in the previous year. Requires the CPUC to include the status of utilities' memorandum accounts as part of an existing report. Status: *set for hearing on April 3rd* in this committee.

REGISTERED SUPPORT / OPPOSITION:

Support

California Environmental Justice Alliance Action, a Project of Tides Advocacy
California Solar & Storage Association
Media Alliance
Sonoma County Democratic Party
Sustainable Rossmoor
The Climate Center
The Utility Reform Network (TURN)

Oppose

California State Association of Electrical Workers
California Water Association
Coalition of California Utility Employees
Edison International and Affiliates, Including Southern California Edison
Pacific Gas and Electric Company and Its Affiliated Entities
San Diego Gas and Electric Company
Sempra Energy Utilities/SDG&E/SoCalGas

Analysis Prepared by: Laura Shybut / U. & E. / (916) 319-2083