

STATE OF CALIFORNIA

Public Utilities Commission
San Francisco

M e m o r a n d u m

Date: June 4, 2003

To: The Commission
(Meeting of June 5, 2003)

From: Alan LoFaso, Director
Office of Governmental Affairs (OGA) — Sacramento

Subject: **SB 429 (Morrow) Public utilities: acquisition or control.**
As Amended April 30, 3003

Legislative Subcommittee Recommendation: Support with Amendment

Summary: This bill would codify the Commission's "first priority" rules regarding public utility holding companies.

Digest: Existing law, the "Public Utilities Act" (P.U. Code sec. 201 et. seq., most recently codified by Chapter 764, Statutes of 1951), provides that electrical and gas corporations are public utilities, conferring jurisdiction upon the Commission to regulate these entities, as specified.

Existing law, P.U. Code sec. 818, prohibits any public utility from issuing stock or other evidence of ownership or specified bonds, notes, or other evidence of indebtedness without prior authorization from the Commission.

Existing law, P.U. Code sec. 854, prohibits any person or corporation from merging, acquiring, or controlling any public utility without prior authorization from the Commission.

This bill would authorize the Commission to enforce any condition agreed to by a public utility as part of an application pursuant to one of the above statutes. This bill would further provide that the Commission's power to enforce these provisions extends to any person or corporation holding a controlling interest in the public utility.

This bill would provide that any authorization to hold a controlling interest in an electrical or gas corporation includes the following conditions:

- a) The capital requirements of the utility necessary to meet its obligation to serve shall be given first priority, as determined by the Commission;

- b) A balanced capital structure shall be maintained as determined in a utility's most recent general rate case; and
- c) The dividend policy shall continue to be set by the utility's board of directors as though the utility were a comparable, stand-alone entity.

This bill would prohibit any electrical or gas corporation from permitting any retained earnings from being transferred to its holding company where doing so would decrease the utility's net equity ratio below that adopted in the utility's last general rate case.

This bill would further require the Commission to order any person or corporation holding a controlling interest in an electrical or gas corporation to infuse sufficient capital to enable the utility to fulfill its obligation to serve.

This bill would provide that its provisions are declaratory of existing law.

Analysis: SB 429 would codify in statute the "first priority condition" that the Commission imposed when it approved the holding company structure for the electric and gas utilities, and provide an explicit requirement that the Commission to require holding companies to "infuse sufficient capital" of any type deemed necessary by the Commission to enable their utility subsidiaries to meet their obligation to serve (the "first priority" condition).

Each of the decisions approving holding company structures for Southern California Edison (SCE), Sempra Energy, and Pacific Gas and Electric (PG&E) contains a "first priority" condition. (See D. 88-01-063 (SCE); D.98-03-073 (Sempra); D. 96-11-017 (PG&E).)

In 2001, the Commission commenced an investigation (I.) 01-04-002 to determine whether transfer of money to the utilities' holding companies during the period of utility financial distress of 2000-2001 and investigate the holding companies' failure to assist the utilities financially. As of its last published decision in this proceeding, the Commission had made no final determination that any utility or holding company had violated the first priority condition, or that any particular remedy should follow (D. 02-07-043, ordering paragraph 1).

SB 429 also contains specific requirements preventing utilities from reducing their net equity ratios and requires their boards of directors to set dividend policy, independent from the holding company. These requirements are consistent with the Commission's holding company decisions to maintain utilities' financial strength and protect ratepayers from the potential risks of a holding company structure.

AMENDMENT

To further these goals, the Legislative Subcommittee discussed an additional safeguard to protect subsidiary utilities in holding company structures as well as their ratepayers. This additional safeguard would require that no more than 20 percent of the

membership of the boards of directors of the holding company and the subsidiary utility comprise the same individuals as directors. This safeguard would further the intent of SB 429 that dividend policies shall continue to be set by the utility's board of directors, as if the utility were an independent, stand-alone entity. Moreover, this amendment would provide for additional independence to promote the requirement that earnings not be transferred from the subsidiary utility to its holding company where doing so would decrease the utility's net equity ratio.

LEGISLATIVE HISTORY

Senate E.U.&C.: 7-0 (do pass) (4//22/03)

Sen. Approps.: Ordered to Senate Floor per Rule 28.8 (no fiscal impact) (May 19, 2003)

SUPPORT/OPPOSITION

Support: California Utility Employees, Office of Ratepayer Advocate, Utility Consumer Action Network, The Utility Reform Network.

Opposition: Pacific Gas & Electric, Sempra Energy, Southern California Edison.

LEGISLATIVE STAFF CONTACT

Alan LoFaso, Legislative Director
CPUC-OGA

alo@cpuc.ca.gov
(916) 327-7788

Date: June 4, 2003

BILL LANGUAGE:

BILL NUMBER: SB 429 AMENDED
 BILL TEXT

AMENDED IN SENATE APRIL 30, 2003

INTRODUCED BY Senator Morrow

FEBRUARY 20, 2003

An act to add Section 854.5 to the Public Utilities Code, relating to public utilities.

LEGISLATIVE COUNSEL'S DIGEST

SB 429, as amended, Morrow. Public utilities: acquisition or control ~~of electrical corporations and gas corporations~~

(1) The California Constitution establishes the Public Utilities Commission, with jurisdiction over all public utilities. The Constitution grants the commission certain general powers over all public utilities, subject to control by the Legislature, and authorizes the Legislature, unlimited by the other provisions of the Constitution, to confer additional authority and jurisdiction upon the commission, that is cognate and germane to the regulation of public utilities.

The existing Public Utilities Act, prohibits any person or corporation from acquiring or controlling, directly or indirectly, any public utility organized and doing business in this state, ~~including electrical corporations and gas corporations,~~ without first securing authorization to do so from the commission. Existing law requires the commission, before authorizing the acquisition or control of an electric, gas, or telephone utility having revenues in excess of a specified amount, to consider, among other things, that the proposal provides short-term and long-term economic benefits to ratepayers, and equitably allocates the short-term and long-term forecasted economic benefits of the proposed merger, acquisition, or control, as determined by the commission, between shareholders and ratepayers, where the commission has ratemaking authority. *The act prohibits a public utility from issuing stocks and stock certificates, or other evidence of interest or ownership, or bonds, notes, or other evidences of indebtedness payable at periods of more than 12 months, without first securing authorization to do so from the commission.*

Pursuant to the act, the commission has authorized the formation of holding companies holding a controlling interest in certain ~~electrical corporations and gas corporations~~ *public utilities*. The commission has conditioned authorization upon the capital requirements of the ~~electrical corporation or gas corporation~~ *utility* being given first priority by the board of directors of the parent holding company, as determined by the commission as being necessary to meet the obligation to serve ~~the electrical corporation or gas corporation~~.

This bill would ~~provide that any corporation or person holding a controlling interest in an electrical corporation or gas corporation organized and doing business under the laws of this~~

~~state, is subject to the continuing jurisdiction and power of the commission to enforce a condition placed upon any authorization obtained to acquire or control, directly or indirectly, the public utility. The bill would require that it be a condition of any authorization given a corporation or person holding a controlling interest in an electrical corporation or gas corporation, that the capital requirements of the utility, as determined by the commission to be necessary to meet the utility's obligations to serve, be given first priority. The bill would further require, when the commission determines it necessary to meet the obligation of the utility to serve, that the commission order the corporation or person holding a controlling interest in the utility, to infuse sufficient capital into the utility subsidiary, of any type deemed necessary by the commission, to enable the utility to fulfill the obligation to serve.~~

~~authorize the commission to enforce any condition agreed to by a public utility as part of an application to merge, acquire, or control a public utility or an application to issue stocks and stock certificates, or other evidence of interest or ownership, or bonds, notes, or other evidence of indebtedness. The power to enforce would apply to the utility and the corporation or person holding a controlling interest in the utility. The bill would require that whenever the commission authorizes a corporation or person to hold a controlling interest in an electrical or gas corporation, that it be a condition that the capital requirements of the utility necessary to meet the utility's obligation to serve be given first priority. The bill would declare that these provisions state existing law.~~

~~The bill would require the commission to order the corporation or person holding a controlling interest to infuse sufficient capital into the utility to enable it to fulfill its obligation to serve. The bill would require that whenever the commission authorizes a corporation or person to hold a controlling interest in an electrical or gas corporation, that a balanced capital structure be maintained in the utility and that retained earnings not be transferred to the controlling corporation or person where doing so would decrease the utility's net equity below that adopted by the commission in the utility's last general rate proceeding. The bill would require that whenever the commission authorizes a corporation or person to hold a controlling interest in an electrical or gas corporation, that any dividend policy of the utility be set by the utility's board of directors as though the utility is a stand-alone electrical or gas corporation. Because a violation of the Public Utilities Act or an order of the commission is a crime under existing law, the bill would impose a state-mandated local program by creating a new crime.~~

(2) The California Constitution requires the state to reimburse local agencies and school districts for certain costs mandated by the state. Statutory provisions establish procedures for making that reimbursement.

This bill would provide that no reimbursement is required by this act for a specified reason.

Vote: majority. Appropriation: no. Fiscal committee: yes.
State-mandated local program: yes.

THE PEOPLE OF THE STATE OF CALIFORNIA DO ENACT AS FOLLOWS:

SECTION 1. Section 854.5 is added to the Public Utilities Code, to read:

~~854.5. (a) Any corporation or person holding a controlling~~

854.5. (a) The commission may enforce any condition agreed to by a public utility as part of an application to merge, acquire, or control either directly or indirectly any public utility organized and doing business in this state, pursuant to Section 854.

(b) The commission may enforce any condition agreed to by a public utility as part of an application to issue stocks and stock certificates, or other evidence of interest or ownership, or bonds, notes, or other evidences of indebtedness, pursuant to Section 818.

(c) The commission's power to enforce under this section applies to the public utility and any corporation or person holding a controlling interest in the public utility.

(d) Whenever the commission authorizes a corporation or person to hold a controlling interest in an electrical corporation or gas corporation, a condition of that authorization is that the capital requirements of the electrical corporation or gas corporation, as determined by the commission to be necessary to meet the public utility's obligation to serve, shall be given first priority.

(e) The commission shall order a corporation or person holding a controlling interest in an electrical corporation or gas corporation to infuse sufficient capital into the public utility, of any type and quantity deemed necessary by the commission, to enable the public utility to fulfill its obligation to serve.

(f) Whenever the commission authorizes a corporation or person to hold a controlling interest in an electrical corporation or gas corporation, a condition of that authorization is that the corporation or person maintain a balanced capital structure in the public utility, as determined to be reasonable by the commission in the public utility's most recent general rate case. No electrical corporation or gas corporation shall permit retained earnings to be transferred to a corporation or person holding a controlling interest in the public utility where doing so would decrease the public utility's net equity ratio below that adopted in the public utility's last general rate proceeding.

(g) Whenever the commission authorizes a corporation or person to hold a controlling interest in an electrical corporation or gas corporation, a condition of that authorization is that the dividend policy of the public utility shall continue to be set by the public utility's board of directors, as though the public utility were a comparable stand-alone electrical corporation or gas corporation.

SEC. 2. The addition of subdivisions (a), (b), (c) and (d) to Section 854.5 of the Public Utilities Code by Section 1 of this act do not constitute a change in, but are declaratory of, existing law.

~~interest in an electrical corporation or gas corporation organized and doing business under the laws of this state, is subject to the continuing jurisdiction and power of the commission to enforce a condition placed upon any authorization obtained pursuant to Section 854.~~

~~(b) It is a condition of any authorization given to a corporation or person holding a controlling interest in an electrical corporation or gas corporation organized and doing business under the laws of this state, that the capital requirements of the electrical corporation or gas corporation, as determined by the commission to be necessary to meet the corporation's obligations to serve, shall be given first priority. When determined by the commission to be necessary to meet the obligation of an electrical corporation or gas corporation to serve, the commission shall order a corporation or person holding a controlling interest in the electrical corporation~~

~~or gas corporation, to infuse sufficient capital into their
respective utility subsidiaries, of any type deemed necessary by the
commission to enable the electrical corporation or gas corporation to
fulfill the obligation to serve.—~~