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Exhibit No.:	SCE-01
Witnesses:	M. Sheriff

(U 338-E)

Rebuttal Testimony of Southern California Edison Company (U 338-E) on Application of Pacific Gas and Electric Company for Approval of Zonal Electrification

Before the

Public Utilities Commission of the State of California

Rosemead, California
March 17, 2023

SCE-01: Rebuttal Testimony of Southern California Edison Company (U 338-E) on Application of Pacific Gas and Electric Company for Approval of Zonal Electrification

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I.

INTRODUCTION

Pursuant to the *Assigned Commissioner's Scoping Memo and Ruling Requiring the Service and Filing of Amended Application*, dated November 22, 2022 (Ruling), Southern California Edison Company (SCE) submits this Rebuttal Testimony, which responds, in part, to Pacific Gas and Electric Company's (PG&E) Application for Approval of Zonal Electrification Pilot Project and Request for Expedited Schedule and its supporting Testimony, filed August 10, 2022 (Application). SCE supports the Application's request for regulatory asset recovery as set forth therein.

II.

THE COMMISSION SHOULD REJECT CAL ADVOCATES' DEBT ONLY PROPOSAL BECAUSE IT IS CONTRARY TO COST-OF-SERVICE RATEMAKING

Cal Advocates claims that PG&E's return on Phase 2 costs "should be reduced to reflect the cost of debt only, not the full weighted cost of capital (rate of return)," because "the project will not incur capital expenditures like traditional capital projects, and there will be no shareholder risk." Because PG&E estimates that Phase 2 of the project is not cost effective, Cal Advocates then concludes that "the return [on Phase 2] should be adjusted down to the cost of debt only."[1]

SCE opposes Cal Advocates' proposal that PG&E provide financing at a debt-only rate of return as it is unsupported and inconsistent with PG&E's Cost of Capital proceeding. Tellingly, Cal Advocates devotes just ten lines of testimony to its suggestion above and offers no facts or evidence for why its request is just and reasonable, let alone consistent with PG&E's Cost of Capital proceeding. More specifically, Cal Advocates proposes that PG&E's "non-cost effective" Phase 2 project expenditures, estimated at $7.13 million, should receive debt rate of return of 4.31 percent on the regulatory asset[2] rather than its authorized weighted cost of debt and equity of 7.81 percent.[3] Cal Advocates' proposal effectively requires that PG&E

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[1] Public Advocates Office at the California Public Utilities Commission (Cal Advocates) Direct Testimony filed on February 17, 2023, page 4.

[2] *Ibid*, page 4.

[3] D.22-12-031. Corrected version issued 1/10/2023, page 3.

finance customer-side electrification of appliances and infrastructure, but only allows PG&E to recover a portion of its authorized cost of financing. This proposal arbitrarily departs from both long-standing cost-of-service principles and the Commission's recent determination of PG&E's cost of capital in Decision (D.)22-12-031 and is non-compensatory.

Cal Advocates' proposal is inconsistent with well-established cost-of-service principles. Commission precedent dictates that investor-owned utilities (IOUs) finance long-term asset recovery through a Commission-approved capital structure of debt and equity and earn a Commission-approved rate of return based on the resulting cost of capital. A utility's authorized capital structure and authorized rate of return are determined in cost-of-service proceedings, referred to as "Cost of Capital" proceedings.[4] PG&E's most recent Cost of Capital proceeding filed on April 20, 2022 and concluded with a decision issued on December 19, 2022.

The costs that comprise PG&E's regulatory asset request in this proceeding must be financed the same any other long-term investment, *i.e.*, PG&E will use capital raised in accordance with the utility's approved capital structure, at a cost of capital equal to the cost of capital for other long-term investments. The rate of return on the regulatory asset must therefore be the same as PG&E's rate of return for other long-term investments. In other words, the actual cost to PG&E to finance these customer-side infrastructure investments is the same cost to finance all other investments and, moreover, this cost has been determined by the Commission in D.22-12-031.[5]

Cal Advocates fails to justify why the Commission should deviate from established cost-of-service principles. It is not reasonable to expect PG&E to finance the regulatory asset entirely with debt rather than the mix of capital as prescribed by the Commission-approved capital structure.[6] PG&E does not finance each regulatory asset separately. Therefore, Cal Advocates' unsupported claim that these assets are less risky is irrelevant. Rather, the company finances assets at an enterprise-wide level, and the company does

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4 *Ibid.*

5 *Ibid,* Ordering Paragraph (OP) 1.

6 *Ibid*, OP 1 presents PG&E's authorized capital structure of: Long Term Debt of 47.50%, Preferred Equity of 0.50%, and Common Equity of 52.00%.

so with a mix of debt and equity that the Commission approved in PG&E's most Cost of Capital proceeding. By modifying the rate of return on the regulatory asset to equal the cost of debt, Cal Advocates proposes that PG&E shareholders be compensated about half the rate return.[7] Therefore, the proposed debt-only return on the long-term regulatory asset is non-compensatory and violates the principles of cost-of-service ratemaking. Fundamentally, Cal Advocates' suggestion ignores the fact that PG&E is required to maintain its respective authorized capital structure and, therefore, financing the regulatory asset entirely via debt is unsustainable for utility to provide safe, reliable service given that cost-of-service principles are no longer be utilized.

Finally, the Commission-authorized capital structure is intended to maintain credit ratings. The proportion of debt to equity is critical to PG&E's (and other IOUs') credit quality, which would deteriorate with additional debt impacting both the cost of future financings as well as its ability to maintain liquidity. Financing investments solely with debt would lead to unreasonable financial risk. The capital structure, and importantly the ratio of total debt to capital, is a key metric used by rating agencies to quantitatively assess credit quality. All else being equal, as the proportion of debt increases, credit quality decreases, financial risk increases, and the cost of equity increases. In short, a debt-only return will harm PG&E's customers by indirectly increasing costs.

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[7] *Ibid,* Conclusion of Law 20, "A test year 2023 ROE of 10.00% and ROR of 7.32% is just and reasonable for PG&E."