

The Basics: Converting PG&E to a Customer-Owned Utility

Our Current Challenge

The crisis in California's electric utility industry has placed our region's health, safety, and prosperity at serious risk.

- The Governor and the Legislature have taken important steps in response, through the creation of a Wildfire Fund, to reduce the statewide financial risk of wildfire-based losses to its utilities. While very helpful, PG&E suffers from more systemic and extraordinary problems than the Fund can solve.
- PG&E's January 2019 bankruptcy filing has opened the door to completely new solutions to deal with the Company's failure. However, the two proposals before the bankruptcy court— one from PG&E and the other from a group of its creditors —do little to resolve this crisis, while proposing to compensate wildfire victims with a dubious package of cash and new PG&E stock, and to use high interest rate junk bonds as part of its pay-off for other debts. This crisis requires much more, however: substantive reform, and better alignment of PG&E's financial interests with the public interest.
- As an investor-owned utility, PG&E currently operates for the benefit of its shareholders, which may be appropriate in many contexts. In these grave circumstances, however, the short-term, shareholder-first financial focus of the Company has prompted a series of decisions that have severely undermined the safety and reliability of its service, to the great detriment of its 16 million customers.
- A broad coalition of mayors and other local leaders, representing millions of PG&E customers, has proposed a totally new approach: converting PG&E into a customer-owned utility.
- A customer-owned business will have a simple focus: serving its ratepayers safely, reliably, and cost-effectively. This business model has a proven track record: nearly 900 customer-owned cooperatives all across our country already furnish electric power to more than 40 million Americans.
- Even without the poor decisions that have put PG&E back into Chapter 11 for the second time in 20 years, the utility would face an enormous financial burden to make the grid resilient to the challenges of climate change. Tens of billions of dollars will be required for hardening, cyber-security, and wildfire protection, threatening customers with significant rate increases. A customer-owned utility will have both greater and lower-cost access to capital to address those financial needs, which means lower rates for customers.

PG&E's Future Cannot Rest In the Hands of the Hedge Funds Currently Competing in Bankruptcy Court

Chapter 11 reorganization has two functions: to repay what the company owes, and to create a financially viable successor business that will not have to seek further court protection. Neither group now competing for ownership of PG&E offers a long-term path for creating a viable, sustainable utility.

- PG&E has accrued indebtedness exceeding \$25 billion to financial institutions and trade creditors, and also faces a rapidly growing mountain of tort claims arising from 2017, 2018 and 2019 wildfires that have crippled the company.

- Both groups of hedge funds have proposed deeply flawed plans of reorganization: The Company plan unduly protects the shareholders represented in its group, while the competing plan predictably benefits bondholders that dominate its interests.
- While competing claimants have consumed all the attention in bankruptcy court, the Bankruptcy Code also requires the creation of a new reorganized utility to emerge from bankruptcy as a financially sustainable company. The two groups fighting over PG&E's assets have presented plans demonstrating little regard for the future viability for the company, and particularly for its need to raise the tens of billions of dollars to rebuild and repair an unsafe power grid.
- The current competing plans are something of a shell game, variously using - depending on the plan - an ever-changing combination of some cash, some investment-grade debt, some high-cost junk bonds, and some new stock of speculative value in a reorganized PG&E to pay claims and/or reward shareholders. Both approaches pay only lip service to the massive future challenge of rebuilding the grid and protecting customers from wildfire risk.
- Both plans emphasize immediate payment of their financial backers, leaving a fundamentally weakened PG&E vulnerable to a return to bankruptcy for a third time. The CPUC should disapprove both deeply flawed plans of reorganization that have been proposed.

A Customer-Owned Utility Best Serves Ratepayers and Our Communities

We seek to repay wildfire victims and other creditors, as fully and fairly as possible— and even compensate equity owners of PG&E, if the Bankruptcy Court determines that to be appropriate — while creating a new utility that will serve our citizens safely, reliably, and cost-effectively. A customer-owned utility provides the best vehicle to accomplish these objectives, particularly where it must acquire and continually operate *all* of PG&E's electric and gas businesses.

- Two reasons support a customer-owned utility as the best path forward: (1) it provides access to capital at the lowest cost to pay creditor claims to exit bankruptcy, rebuild the company, and operate the utility, and (2) it re-aligns PG&E's financial interests with the public interest.
- A customer-owned utility can avail itself of less expensive access to capital for several reasons. By law, a customer-owned utility sets its own rates and determines how to recover its costs. Avoiding the uncertainties of governmental regulatory control over rates enables a customer-owned utility to have access to public market financing, eschewing much more expensive equity and conventional debt. An investor-owned utility's imperative to pay dividends to shareholders alone places much more burdensome capital costs on the company. As a result, a customer-owned entity may save as much as 50% in lower capital costs, translating to billions of dollars of savings in interest payments.
- Further, going forward a customer-owned utility will be exempt from federal taxation (we expect it will need to make whole its obligations on state and local taxes through in lieu payments, however), enabling the company to refocus save dollars for investment on critical maintenance and capital infrastructure.
- The magnitude of these savings becomes apparent when we consider that PG&E has projected that it will have to spend—and borrow—\$28 billion on system hardening and upgrades in the next four years. The financing savings unleashed by a cooperative model run in the billions of

dollars, and if properly reinvested in grid resiliency, these savings will have a multiplier effect by reducing losses, mitigating claims, and dampening customer rate increases.

- The customer-owned utility's leaner financing model also enables it to undertake essential insurance needs relating to future wildfire risk, including participating in the recently-established \$21 billion state wildfire fund, and other forms of risk management.
- Second, the different financing structure of a utility cooperative liberates it from the constant short-term imperative of maximizing shareholder value through the stock price. This will enable a new culture at the utility, one that can harmonize the goals of management and the workforce with the real needs of their customers and the public.
- The governing board of the utility will ultimately be responsible to customers, not shareholders, and the company will establish a formal process for incorporating ratepayer input into the board election process.
- In a customer-owned utility, the new governing board will determine whether to retain the current operating managers who were recently selected to run PG&E after its bankruptcy, or whether a new executive team should be chosen.
- A publicly-owned utility—as distinguished from the customer-owned model that we propose—has merit, and several municipal utilities have demonstrated strong track records. Conversion of an investor-owned PG&E to a publicly-owned utility, however, faces daunting hurdles. The California Constitution prohibits the state from owning a company. Purchasing the company also poses fiscal risk to the state, as Standard & Poor's recently publicly stated that any state acquisition of PG&E would result in a downgrade of state bonds, increasing future financing costs on taxpayers. Finally, public acquisitions of private assets through eminent domain—and lengthy litigation—very often result in taxpayer payments in excess of the market value of the assets.

Bankruptcy Can Enable PG&E's Transformation to a Customer-Owned Utility

The Chapter 11 process provides a path for the conversion of PG&E to a utility cooperative.

- The Bankruptcy Code confers statutory authority on the Federal Courts to change the corporate form of a company in Chapter 11 as part of the reorganization process. This can be accomplished with or without the consent of the equity owners of the company.
- The cities and counties supporting creation of an electrical cooperative will propose their own Chapter 11 plan (the "Customer Plan"), just as the Company and the bondholders have each proposed a plan. The terms of this Customer Plan will convert PG&E into a customer-owned utility cooperative. It will pay claims in cash instead of using the uncertainties of the payment proposals of the other plans.
- The CPUC must review and approve the structure of whatever company emerges from bankruptcy. The coalition of local leaders submitted a November 4, 2019 letter to CPUC Board President Marlene Batjer, seeking to ensure that the agency's scope of review incorporates consideration of a reorganized structure that will best serve the public. In her November 14, 2019 response, President Batjer observed that the Commission has already begun to discuss "concepts such as mutual benefit corporations and similar models. There are many benefits from such models that warrant further consideration."

- Perhaps most importantly, the Customer Plan will articulate a clear approach for financing the more than \$50 billion in debts and obligations of PG&E.
- If the Customer Plan is approved by the Bankruptcy Court and the CPUC, PG&E will emerge from chapter 11 as a customer-owned cooperative, with a new governing board, new ownership, a new financing structure, and board selection process focused on the best interests of the customers.

A Customer-Owned Model Can Best Meet Our Communities' Expectations and Values

- We have begun discussions with legislators who have expressed an interest in carrying a bill to implement a customer-owned model that meets our collective expectations for transparency and accountability in governance structure, and ensures that such good governance laws as the Brown Act and the Public Records Act apply appropriately to the company's operations.
- We have drafted a set of guiding principles that articulate many of these specific objectives, and we continue to engage with our coalition of local leaders to improve those principles.
- We seek the wholesale transformation of every part of PG&E's service area, so that no parts of the state will suffer disparate impacts from exclusion, and to ensure a geographically equitable governance structure. A customer-owned model will succeed only if it leaves no part of our state behind—particularly those rural regions that bear the burden for the high-voltage transmission infrastructure necessary for the grid's proper functioning.
- In collaboration with the Legislature and Governor, we will aggressively advocate to ensure that in lieu fees are paid to state and local governments for any taxes for which a customer-owned utility might be exempt, to ensure that our local communities are made whole.
- We will insist that positive PG&E efforts to meet State clean energy and energy efficiency mandates, along with other public policy imperatives, will continue under a customer-owned utility structure.
- We will honor PG&E's workforce. Although PG&E's problems have many sources, they do not lie in its highly trained, skilled and motivated workforce. We will insist that the conversion to a customer-owned utility not affect their jobs, benefits, or pay structures, as articulated in existing contracts.

The Opportunity of Change

Widespread hostility toward PG&E has become an unnecessarily regrettable fact of life in Northern California, the Central Coast, and the Central Valley. Anger over the Company's failures and the suffering of our communities will not disappear with the mere emergence of a customer-owned entity. It will take time to rebuild confidence, and to rebuild the system. Nonetheless, a transformation of the company to a customer-owned cooperative opens the door to a more collaborative approach with the public and the state's leadership. We aspire to create a company that fundamentally realigns its interest with the public interest.