

BEFORE THE PUBLIC UTILITIES COMMISSION  
OF THE STATE OF CALIFORNIA



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Application of San Diego Gas & Electric Company (U 902-M), Southern California Edison Company (U 338-E), Southern California Gas Company (U 904-G) and Pacific Gas and Electric Company (U 39-M) for Authority To Establish A Wildfire Expense Balancing Account to Record for Future Recovery Wildfire-Related Costs

Application No. 09-08-020  
(Filed August 31, 2009)

**SAN DIEGO GAS & ELECTRIC COMPANY (U 902-M), SOUTHERN CALIFORNIA EDISON COMPANY (U 338-E), SOUTHERN CALIFORNIA GAS COMPANY (U 904-G) AND PACIFIC GAS AND ELECTRIC COMPANY'S (U 39-M) REPLY TO PROTESTS**

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OF THE STATE OF CALIFORNIA**

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Pursuant to Rule 2.6(e) of the Rules of Practice and Procedure of the California Public Utilities Commission (“Commission”), Applicants San Diego Gas & Electric Company (“SDG&E”), Southern California Edison Company (“SCE” or “Edison”), Southern California Gas Company (“SoCalGas”), and Pacific Gas and Electric Company (“PG&E”) (collectively, the “Utilities” and individually a “Utility”) respond to the protests filed by the Division of Ratepayer Advocates (“DRA”), the Consumer Protection and Safety Division (“CPSD”), Disability Rights Advocates (“DisabRA”), and Mussey Grade Road Alliance (“Mussey”).

**I. INTRODUCTION.**

The Application and supporting testimony explain why the Commission should authorize the Utilities to recover costs arising from wildfires. An insurance crisis has prevented the Utilities from obtaining sufficient insurance at reasonable cost against third-party claims arising from wildfires.<sup>1</sup> The Application proposes to continue the Commission’s traditional approach to cost recovery: just as the Commission has authorized rate recovery for premiums for liability insurance and for forecasted claims costs, and has likewise authorized the Utilities to recover the costs of other natural

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<sup>1</sup> Testimony In Support Of Joint Application For Authority To Establish A Wildfire Expense Balancing Account To Record For Future Recovery Wildfire-Related Costs (“Utility Testimony”) at 2, 51-75.

disasters, so too should it authorize the Utilities to recover the costs of uninsured claims and related expenses arising from wildfires.<sup>2</sup>

The protests do not dispute that the Utilities face an insurance crisis, nor do they contest that the Commission should act promptly to respond to this crisis. Instead, the protests raise issues about the allocation of responsibility for such costs, the standard for their recovery, and other matters. As discussed below, some of these issues are outside the scope of this proceeding. Others, while within the scope, raise policy questions that can be resolved on the basis of written submissions, and the protests do not justify evidentiary hearings.

The Utilities urge the Commission to establish a procedural schedule that leads to a final decision by the Spring of 2010, before the next fire season begins.

## **II. THE COMMISSION SHOULD REJECT PROPOSALS TO REQUIRE SHAREHOLDERS TO BEAR WILDFIRE COSTS.**

Each of the protests asserts that the Utilities' shareholders should bear some or all of the costs arising from wildfires.<sup>3</sup> The protests suggest that a shareholder payment is needed to create an "incentive" for the Utilities' management to take steps to mitigate the risk of fires and to minimize the costs of claims.<sup>4</sup> Although these policy arguments are within the scope of the proceeding, they are incorrect.

### **A. The Utilities Have Strong Incentives To Operate Their Systems Safely.**

The protests' assumption that a shareholder payment is needed to create an "incentive" to mitigate wildfire risks and claims costs is seriously mistaken. The protests seem to assume that the Utilities' management would ignore safety considerations and

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<sup>2</sup> Id. at 10-13.

<sup>3</sup> DRA Protest at 4-5 (ratepayers should not pay for premium increases that are due to a utility's negligent, grossly negligent or reckless conduct, or a failure to comply with applicable rules or statutes); DRA Protest at 5 (shareholders should pay for a portion of costs); CPSD Protest at 2 (shareholders should pay 20% of the cost); DisabRA Protest at 3 (Commission should consider alternative funding mechanisms, such as requiring some portion of the costs to be borne by shareholders); Mussey Protest at 17 (utilities should not be allowed to recover a portion of costs, characterized as co-pays and deductibles).

<sup>4</sup> DRA Protest at 5; CPSD Protest at 2; DisabRA Protest at 4; Mussey Protest at 17.

cut spending to maximize short-term profits without regard for their continuing obligation to provide safe and reliable service. Nothing could be further from the truth. The Utilities take extremely seriously their duty to mitigate the risk of fire, and they take significant steps to do so through their extensive vegetation management programs and investments in infrastructure. But the Utilities' ability to prevent wildfires is limited, particularly given that the Commission would not authorize the Utilities to spend an unlimited amount on risk management projects,<sup>5</sup> and the consequences of those fires that do start are in the hands of others, such as local fire fighting resources, rather than the Utilities. Accordingly, the risk of fires is inherent and unavoidable and the results are outside the Utilities' control.

The Utilities have always had an incentive to mitigate the risk of wildfires and to contest frivolous claims. They had such an incentive when their insurance coverage was adequate, and they will continue to have such an incentive under the approach set forth in the Application. The provision of safe and reliable service is the Utilities' core mission, and they do not need a shareholder penalty to provide an "incentive" to continue to pursue that goal. In addition, the Utilities have a strong incentive to keep rates low and to preserve and enhance their reputations; both considerations create a powerful motivation to mitigate fire risk and to minimize costs for unfounded claims. The Utilities look forward to working cooperatively with DRA, CPSD, and other interested stakeholders in Phase 2 of the Commission's ongoing rulemaking (R.08-11-005) to develop additional measures to further reduce fire hazards associated with electric and communication facilities. Finally, the Utilities will continue to be subject to penalties for violations of General Order 95, although any such penalties would be separate from recovery of the costs arising from wildfires.<sup>6</sup>

Contrary to DRA's belief, the insurance carriers will continue to play an important role in responding to claims, notwithstanding the reductions in coverage. DRA argues

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<sup>5</sup> Utility Testimony at 14.

<sup>6</sup> Id. at 19.

that, because the Utilities have purchased less insurance, the “insurers will only provide those [claims] services for the relatively small portion of claims for which they are liable.”<sup>7</sup> On the contrary, insurance carriers have a duty to respond to all claims unless and until policy limits are exhausted. As a result, there is no reason to expect that insurance carriers will be less involved than they have been in the past in process of defending claims.

**B. Imposing Costs On Shareholders Would Contravene The Commission’s Long-Standing Policies.**

The protests fail to recognize that the Application proposes to *continue* the Commission’s existing policy of permitting the Utilities to recover the costs of third-party claims, as reflected in the Commission’s regular authorization of rate recovery of insurance premiums and forecasted claims costs.<sup>8</sup> The protests do not explain why the Commission should reverse this long-standing policy simply because insurance carriers have decided to offer less insurance to the Utilities at a substantially higher price. The Commission’s traditional policy is correct and should be followed: the cost of third-party claims arising from wildfires is an ordinary cost of fulfilling the Utilities’ public service obligations, and as such should be recovered in rates.<sup>9</sup>

Imposing costs of providing utility service on shareholders would be unprecedented and unfair. The Commission has a constitutional and statutory duty to give the Utilities the reasonable opportunity to recover their costs *in full*.<sup>10</sup> The suggestion that shareholders should pay a portion of wildfire-related costs, regardless of the limits on the Utilities’ ability to control such costs, and regardless of the legal mandate that the Utilities provide service to fire-prone areas, would contravene this fundamental tenet of the regulatory compact. Costs arising from wildfires are an inherent

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<sup>7</sup> DRA Protest at 5.

<sup>8</sup> Application at 3 & nn. 4-5; Utility Testimony at 12, 17-18.

<sup>9</sup> Application at 4; Utility Testimony at 14-15, 18.

<sup>10</sup> Utility Testimony at 14-15.

cost of fulfilling the Utilities' duty to serve, and as such they must be fully recoverable in rates.

**III. THE COMMISSION SHOULD REJECT PROPOSALS TO CONDITION COST RECOVERY ON A REVIEW OF REASONABLENESS OR COMPLIANCE WITH RULES.**

DRA argues that costs recorded in the Wildfire Expense Balancing Account (“WEBA”) should not be recovered in rates until the Commission has determined such costs are reasonable.<sup>11</sup> DRA further argues that the Utilities should not be permitted to recover costs that arise from their negligence, gross negligence, violation of a general order, or violation of a state or federal law.<sup>12</sup> Mussey argues that cost recovery should be denied when the Utility is “responsible” for a fire.<sup>13</sup> Mussey does not clearly define what it means by “responsible,” but it appears to contend that cost recovery should be denied whenever the Utility is at “fault,” which Mussey seems to believe covers all situations in which the Utility is out of compliance with Commission’s rules or other “standards.”<sup>14</sup>

Once again, the protests do not acknowledge that they are asking the Commission to deny cost recovery it has traditionally authorized. The Application proposes to continue the approach the Commission has used with respect to recovery of the costs of insurance and of forecasted claims costs. Just as the Utilities have recovered the costs of insurance and the forecasted costs of claims, even though such costs may involve claims based on alleged negligence or violations of regulations or other laws, so too should the Utilities recover the costs of such claims when insurance is no longer available on reasonable terms.<sup>15</sup>

Although the Utilities are strongly committed to actions that mitigate the risk of fires, the Utilities act through their employees, who are fallible. Accidents involving

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<sup>11</sup> DRA Protest at 6.

<sup>12</sup> Id.

<sup>13</sup> Mussey Protest at 15-16.

<sup>14</sup> Id. at 15. DisabRA also implies that cost recovery is inappropriate for “the costs of fires for which the utilities are partially at fault.” DisabRA Protest at 4.

<sup>15</sup> Utility Testimony at 12-13, 18,

negligence are unavoidable, which is why the Utilities—and, indeed, nearly every commercial enterprise, individual, and even the Commission itself—purchase insurance against claims based on negligence or violation of “rules.”<sup>16</sup> The cost of claims arising from wildfires, including wildfires that allegedly result from the negligent actions of the Utilities’ employees, are an inherent cost of providing service, which is properly recovered in rates.

The same reasoning applies to wildfire costs associated with alleged violations of the Commission’s rules. As the Commission has recognized, 100% compliance with Commission rules at all times “is not realistic,” and it would be unreasonable to punish utilities for every event of non-compliance.<sup>17</sup> It would be even more unreasonable to preclude the Utilities from recovering the costs of fires that may be associated with such non-compliance. If a Utility violates a rule or statute, the Commission can investigate and, if appropriate, impose penalties. But penalties serve a different purpose, and cost recovery should not be linked to a determination of whether the Utility complied with every rule.<sup>18</sup>

The protests also fail to address the financial risk to which the Utilities would be exposed if the Commission does not grant the Application. The protests do not dispute that the magnitude of a fire is beyond the Utilities’ control.<sup>19</sup> Thus, even a single act of negligence by a single employee, or a single violation of a Commission rule, can lead to a massive fire resulting in vast claims. Prohibiting Utilities from recovering such costs would create a unique threat to their financial integrity, which would ultimately cause even more harm to ratepayers than the short-term benefit from a denial of cost recovery.<sup>20</sup>

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<sup>16</sup> Utility Testimony at 12, 42-43.

<sup>17</sup> D. 04-04-065, p. 31.

<sup>18</sup> Utility Testimony at 19.

<sup>19</sup> Mussey asserts that the Utilities have some control over the number of fires, in the sense that Mussey believes the Utilities can harden their systems to reduce the likelihood that their facilities will start a fire. Mussey Protest at 5. But Mussey does not contend that, once a fire is started, the Utilities can control its magnitude.

<sup>20</sup> Utility Testimony at 15-16.

**IV. THE COMMISSION SHOULD REJECT CERTAIN OTHER PROPOSALS SET FORTH IN THE PROTESTS.**

**A. The Commission Should Reject DRA's Proposal To Limit Cost Recovery To Historical Insurance Levels.**

DRA argues that the WEBA should be capped at the amount of insurance coverage the Utilities previously purchased, i.e., \$650 million to \$1.2 billion.<sup>21</sup> The Commission should reject this proposal.

There is no principled reason to limit recovery to the amounts of insurance coverage the Utilities purchased in the past. The reasons that justify cost recovery apply to all wildfire-related claims costs, including costs that may exceed the insurance levels the Utilities obtained in the past.

To the contrary, it would be arbitrary to set in stone a particular year's insurance levels as the limit on cost recovery. Absent the insurance crisis, the Utilities would have altered their coverage to the extent warranted by their evaluation of risks and insurance market conditions. The Commission's ratemaking mechanism should mirror this flexibility.

**B. The Commission Should Reject DRA's Proposal To Require The Commission To Revisit The WEBA Mechanism In Three Years.**

DRA also recommends that the Commission review the WEBA mechanism within three years.<sup>22</sup> DRA notes that insurers may be willing to reenter the market in the future based on changed circumstances.<sup>23</sup>

The Commission has the discretion to revisit the WEBA mechanism at any time, but there is no need for the Commission to obligate itself to conduct a new proceeding to review the WEBA mechanism in three years. The WEBA would record claims costs that are *not* covered by insurance (as well as other costs identified in the testimony).<sup>24</sup> If

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<sup>21</sup> DRA Protest at 2-3.

<sup>22</sup> Id. at 3.

<sup>23</sup> Id.

<sup>24</sup> Utility Testimony at 76.

insurance companies offer additional coverage at reasonable rates in the future—which the Utilities sincerely hope will be the case—the claims costs to be recovered through the WEBA will automatically be reduced. This possibility does not require the Commission to commit itself to a review of the mechanism at a particular date.

**C. The Commission Should Reject DRA’s Proposal To Prohibit Recovery Of Costs Allocated To The Transmission Function.**

DRA argues that costs allocated to the transmission function should not be recovered through the WEBA.<sup>25</sup> The costs to be recorded into the WEBA would not be assigned to the transmission function based on the jurisdictional status of the facilities that may be involved in the fire. Rather, claims costs, legal expenses, insurance proceeds, and related financing costs are classified as Administrative & General costs. Instead of separating these costs between jurisdictions, the Utilities propose to recover the costs fully through rates set by the Commission. This simplifies and rationalizes the cost-recovery procedure. At the same time, the Utilities would record as a credit to the WEBA any amounts FERC authorizes for recovery through transmission rates.<sup>26</sup>

**D. The WEBA Will Not Result In Double Recovery Of Legal Expenses.**

DRA contends that legal expenses should not be recorded in the WEBA. DRA claims that when such costs are forecast in the Utilities’ General Rate Cases, they are not reserved for specific types of lawsuits. DRA concludes that balancing account treatment of legal expenses would create the potential for double recovery.<sup>27</sup>

The Utilities agree that they should not double recover legal costs (or any other type of cost) through the WEBA.<sup>28</sup> Accordingly, each Utility will need to establish an accounting mechanism with respect to legal expenses to prevent double recovery. Provided they do so, there is no reason to preclude the Utilities from recovering these costs.

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<sup>25</sup> DRA Protest at 7.

<sup>26</sup> Utility Testimony at 76-77.

<sup>27</sup> DRA Protest at 7.

<sup>28</sup> Utility Testimony at 76.

**V. THE COMMISSION SHOULD DECLARE THAT CERTAIN OTHER ISSUES ARE OUTSIDE THE SCOPE OF THIS PROCEEDING.**

A number of other issues raised by the protests are outside the scope of the proceeding.

CPSD argues that, if the Application is granted, the Commission should reduce the Utilities' authorized return on equity by at least 100 basis points. CPSD argues that such a reduction is appropriate because "ratepayer funding would drastically reduce the Utilities' risk."<sup>29</sup> CPSD's position is incorrect: the Utilities traditionally did not face a significant risk of non-recovery of costs associated with wildfires. But in any case, CPSD's suggestion is outside the scope of this proceeding and should be considered, if at all, in the Utilities' cost of capital proceedings.

DisabRA argues that the recovery of costs to be recorded in the WEBA will have an "asymmetrical" impact on the disabled.<sup>30</sup> This Application is limited to the types of costs that will be recorded in the WEBA and the standard for the recovery of such costs. *How* the costs are recovered is a cost allocation issue that is outside the scope of this proceeding. Electric rate design issues are traditionally addressed in the Utilities' General Rate Cases. Rate Design Windows and gas rate design issues similarly are the subject of their own proceedings. In those contexts, the Commission considers the proper means of recovering all authorized costs. That issue should remain separate from the recoverability of particular categories of cost, all that is involved in this proceeding.

DisabRA also encourages the Commission to consider whether it can exert "influence" over the insurance market.<sup>31</sup> Although the Utilities welcome any actions that could lead to the greater availability of insurance at reasonable rates, they are doubtful the Commission can influence that outcome. In any case, such efforts would be beyond the scope of this proceeding, and can occur independent of it.

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<sup>29</sup> CPSD Protest at 2.

<sup>30</sup> DisabRA Protest at 2-3.

<sup>31</sup> Id. at 5.

Mussey's primary argument is that the Utilities should spend more money to harden their systems and thereby reduce the risk of fires.<sup>32</sup> This is also an underlying theme of the DisabRA protest.<sup>33</sup> The Utilities agree with the general concept that the Commission must balance the cost of additional measures to reduce the risk of wildfires against the potential costs of claims in the event wildfires occur. In other words, the Commission should make a considered judgment about how much ratepayers should pay for the Utilities to harden their systems, given the costs and benefits of such actions. But these considerations are outside the scope of this proceeding and should instead be examined in Phase 2 of the Safety OIR<sup>34</sup> and the Utilities' General Rate Cases. The Utilities will comply with any decision the Commission makes with respect to the level of expenditures they should undertake to mitigate wildfire risk, but there will always be a risk that a wildfire will nevertheless occur. The Commission should decide in this proceeding that the costs related to such wildfires are recoverable through the WEBA. The Commission should not delay or condition cost recovery on the extent of actions the Commission may authorize the Utilities to take to mitigate the risk of such wildfires, which are properly considered in other proceedings.

Mussey also states that the "regulators have asserted" that SDG&E was at fault in the Witch and Rice fires. Mussey relies on CPSD's initial report in I.08-11-006. The Commission, however, has made no finding with respect to SDG&E's conduct in connection with those fires, which are the subject of another pending proceeding.<sup>35</sup> Any retrospective review of SDG&E's conduct in connection with the Witch and Rice fires is beyond the scope of this proceeding.

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<sup>32</sup> Mussey Protest at 4-8.

<sup>33</sup> DisabRA Protest at 4.

<sup>34</sup> *Order Instituting Rulemaking to Revise and Clarify Commission Regulations Relating to the Safety of Electric Utility and Communications Infrastructure Provider Facilities*, R.08-11-005.

<sup>35</sup> I. 08-11-006.

**VI. THE COMMISSION SHOULD ADOPT A SCHEDULE THAT LEADS TO A DECISION IN THE SPRING OF 2010.**

As explained in the Application, the Commission should move expeditiously to adopt a final decision in this proceeding by the Spring of 2010.<sup>36</sup> DRA is the only party that argues against this schedule, claiming that it provides insufficient time for discovery.<sup>37</sup> DRA, however, does not identify what discovery it requires or why such discovery cannot be completed in sufficient time to enable intervenors to serve testimony by December 1, as the Application proposes.<sup>38</sup>

No party has demonstrated a need for evidentiary hearings. DRA is the only party requesting an evidentiary hearing. The Commission's rules require a party who requests a hearing to "state the facts the protestant would present at an evidentiary hearing."<sup>39</sup> DRA has not met this standard. DRA states that hearings will be necessary because "there will likely be disputed issues of fact concerning insurance procurement practices and the propriety of the Utilities' requested relief."<sup>40</sup> DRA's protest, however, does not suggest that the Utilities have failed to procure insurance available at reasonable rates. Nor has DRA explained what facts must be presented at an evidentiary hearing that would bear on the propriety of the relief sought.

The issues raised by the protests that are within the scope of this proceeding are primarily matters of policy. The Commission can resolve these matters based on consideration of written testimony, without evidentiary hearings. The Commission has elected to use a similar "paper hearing" process when faced with similar policy judgments,<sup>41</sup> and should do so again here.

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<sup>36</sup> Application at 8-9.

<sup>37</sup> DRA Protest at 8.

<sup>38</sup> Since filing its protest, DRA has served the Utilities with a single set of data requests. The Utilities expect to respond within the 10 business days requested by DRA.

<sup>39</sup> Rules of Practice and Procedure, Rule 2.6(b).

<sup>40</sup> DRA Protest at 8.

<sup>41</sup> See, e.g., D.07-12-056, p. 16-17 ("The Commission is not required to hold evidentiary hearings in every proceeding. Section 1701.1 states that '[t]he Commission, consistent with due process, public policy, and statutory requirements, shall determine whether a proceeding requires a hearing.' In this instance, the Resolution noted that formal hearings were not required as there were no disputed issues of material fact. Rehearing

**VII. CONCLUSION.**

The Commission should declare certain issues identified above to be outside the scope of this proceeding, should adopt a procedural schedule that leads to a final decision by the Spring of 2010, and should not convene evidentiary hearings.

Dated, this 15th day of October, 2009.

Respectfully submitted,

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Applications fail to explain why formal hearings are required in this instance. The examples of factual issues offered by Rehearing Applications do not demonstrate that there are disputed issues of material fact that must be addressed in formal hearings. Rather, these examples raise matters of policy and law.” (citations and footnote omitted); D.06-04-070, p. 13 (“[T]he record provides no persuasive reason to depart from our preliminary conclusion that there is no need for evidentiary hearings. The issues in this proceeding, for the most part, involve policy and legal conclusions that have been addressed in briefs. Also no party has demonstrated a disputed material issue of fact that would affect our deliberations.”)

**CERTIFICATE OF SERVICE**

I hereby certify that, pursuant to the Commission's Rules of Practice and Procedure, I have this day served a true copy of **SAN DIEGO GAS & ELECTRIC COMPANY (U 902-M), SOUTHERN CALIFORNIA EDISON COMPANY (U 338-E), SOUTHERN CALIFORNIA GAS COMPANY (U 904-G) AND PACIFIC GAS AND ELECTRIC COMPANY'S (U 39-M) REPLY TO PROTESTS** on all parties identified on the attached service list(s). Service was effected by one or more means indicated below:

Transmitting the copies via e-mail to all parties who have provided an e-mail address. First class mail will be used if electronic service cannot be effectuated.

Executed this **15th day of October, 2009**, at Rosemead, California.

/s/ JENNIFER ALDERETE  
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## California Public Utilities Commission

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