Liberty Utilities (CalPeco Electric) LLC
933 Eloise Avenue
South Lake Tahoe, CA 96150
Tel: 800-782-2506
Fax: 530-544-4811

April 26, 2019

VIA EMAIL ONLY

Commission on Catastrophic Wildfire Cost and Recovery
Governor's Office of Planning and Research
1400 10th Street
Sacramento, CA 95814

Dear Commissioners:

Liberty Utilities (CalPeco Electric) LLC ("Liberty CalPeco") appreciates this opportunity to provide input on important wildfire-related issues in response to the Commission's Request for Comments. The impact of wildfires in California is a major issue in which we are keenly interested. We generally concur with the recommendations made by Edison Electric Institute ("EEI") and in its April 22, 2019 Comments.[1]

Background on Liberty CalPeco

Liberty CalPeco serves approximately 49,000 electric customers in California in and around the Lake Tahoe Basin. We provide electric distribution service in portions of the counties of Nevada, Placer, Sierra, Plumas, Eldorado, Mono, and Alpine in the State of California, with almost 80 percent of customers located in the Lake Tahoe Basin.

In addition to the considerably smaller customer base, the location, climate and terrain of Liberty CalPeco's California service territory pose special challenges and differentiate Liberty CalPeco greatly from the three major California electric utilities (Pacific Gas and Electric Company ("PG&E"), Southern California Edison Company ("SCE"), and San Diego Gas & Electric Company ("SDG&E")). Liberty CalPeco's service territory extends from Portola in the north to Markleeville and Topaz Lake in the south. The terrain throughout is mountainous and heavily forested. Consequently, the threat of wildfires has been a focus for a very long time.

---

[1] *Comments of the Edison Electric Institute to the on Catastrophic Wildfire Recovery* (April 22, 2019) ("EEI Comments").

California's Wildfire Liability Regime and the Regulatory Compact

As EEI outlined in its comments, "Financially healthy investor-owned utilities have been and will be critical to ensuring continued and increased investments in clean energy and wildfire hazard mitigation for the benefit of all Californians."[2] However, as explained below, the current wildfire liability regime in the State is inconsistent with the cost-recovery framework set forth by the California Public Utilities Commission ("CPUC"). This has led to a breakdown of the regulatory compact that the State has leveraged in the past to accomplish its ambitious clean energy and other policy goals.

This regulatory compact held that, in exchange for serving all customers, the investor-owned utilities ("IOUs") would be allowed to charge rates that reflect their costs of providing service to their customers plus a regulated return on their investments. These "cost-of-service" rates provide investors the confidence that their investments will be repaid and that there will be a return on their equity. This ability to attract investors to supply capital is crucial to enabling IOUs to promote important State policy objectives and to engage in the extensive wildfire mitigation and resilience efforts.

However, California's IOUs are currently under significant financial stress because of the State's unique inverse condemnation doctrine that effectively holds utilities strictly liable for all catastrophic wildfire damages, regardless of fault or foreseeability. In California, therefore, the costs to serve all electricity customers include third-party damages relate to wildfires. For Liberty CalPeco, whose customer base is largely located in the high wildfire hazard wildland-urban interface, the need to incorporate third-party wildfire damages into its cost-of-service rates is of vital importance. Yet, as discussed below, the current cost recovery framework before the CPUC is fundamentally inconsistent with wildfire liability regime, leading to an unsustainable situation effectively requiring IOUs to act as the de facto backstop insurer for all property owners in the State.

Any successful comprehensive solution addressing wildfire risk therefore will necessarily require the restoration of the regulatory compact. This requires a solution that addresses both fronts: we must both shrink the overall size of the liabilities to which the utilities are exposed for catastrophic wildfires (except in the case of fault) and provide IOUs with access to a broad range of insurance and other funding options.

---

[2] *Id.,* p. 1.

The Current Wildfire Liability Regime Must Be Reformed

As mentioned above, California courts have held that IOUs are strictly liable for any wildfire damage caused by their equipment under the inverse condemnation doctrine, regardless of fault or foreseeability. In extending inverse condemnation liability to IOUs, the California courts reasoned that, because all customers share in the benefits of the electric system, they should also share in the risks posed by that system, including the increasing risk of wildfire.[3] Under the structure envisioned by the courts, wildfire claims would similarly function as a form of social insurance: individual property owner claims would be paid by the electric company and recovered in rates, ultimately socializing those costs across the entire customer base. Critical to this reasoning is the courts' assumption that the IOUs would be able to spread costs by raising electricity rates through future rate recovery proceedings.[4] However, the CPUC's recent actions have proven this key assumption incorrect.

As described below, the CPUC's current cost recovery standard's post-hoc analysis—which essentially holds that the occurrence of fire means that any actions taken by the IOU were imprudent—breaks the regulatory compact, pushing these costs onto shareholders, whose resources will quickly be depleted by billion-dollar damages. Instead, IOUs incur substantial wildfire costs on a strict liability basis under the doctrine of inverse condemnation, but are left saddled with those costs when cost recovery is denied. Effectively, California has shifted from using the utilities as a tool to administer social insurance with costs collectively borne by all residents to a system in which the companies act as *de facto* private insurers.

This status quo is not sustainable. The current wildfire liability regime fails to align risks with those who are best-positioned to mitigate them and then holds the electric companies strictly liable for others' failure to act reasonably.[5] There are several stakeholders driving wildfire risks aside from the electric IOUs alone. Moreover, the substantial costs associated with wildfire inverse condemnation liability jeopardizes the ability of utilities to provide safe, reliable, and affordable power. The terrain of Liberty CalPeco's service territory already presents several challenges in providing safe and reliable power in an affordable manner. Holding a utility strictly liable even when it is not at fault takes funds away that could otherwise be spent toward efforts and programs aimed at keeping rates affordable.

---

[3] *Barham v. Southern California Edison*, 74 Cal.App.4th at 754 (1999).

[4] *Pacific Bell v. Southern California Edison*, 208 Cal.App.4th 1400 (2012); *Barham*, 74 Cal.App.4th at 752.

[5] *See* EEI Comments, pp. 4-5.

Therefore, Liberty CalPeco supports the recommendation of EEI that the current regulatory regime must be reformed: (1) an IOUs should only be held liable for wildfire damages when they are at fault; and (2) IOUs should be guaranteed cost recovery for wildfire damages when they have engaged in prudent mitigation activity. [6] Reform of the strict liability regime under inverse condemnation would reduce third-party damages that electric utilities have to pay, help restore some investor confidence in California's regulatory compact, and create incentives for others to mitigate the risks over which they have control to reduce wildfires. This may be accomplished in the manner detailed in EEI's whitepaper Legislative Options to Reform Inverse Condemnation in California, which it submitted as an exhibit to its Comments.[7]

<u>The CPUC Cost Recovery Framework Should Provide Greater Certainty for Recovery of Costs of Service</u>

The CPUC's current cost recovery standard is inconsistent with the cost-spreading rationale upon which the inverse condemnation wildfire liability regime is based. In November 2017, the CPUC denied an application by SDG&E to recover $379 million of inverse condemnation wildfire costs.[8] As outlined by EEI, this CPUC decision severely undermined investors' confidence in IOUs' stock because it raised concerns in the capital markets that investors in California utilities were more exposed to wildfire liabilities than previously thought.[9]

Under current law, IOUs may only recover non-routine costs, such as wildfire damages, through rates if the CPUC finds that the electric company acted reasonably and prudently in incurring such costs.[10] This "prudent manager" standard requires that the "practices, methods, and acts engaged in by [the] utility follow the exercise of reasonable judgment in light of facts known or which should have been known at the time the decision was made."[11] In a joint concurrence to the November 2017 decision, CPUC President Michael Picker and Commissioner Martha Guzman-Aceves recognized the inconsistency between the inverse condemnation strict liability framework and this cost recovery analysis before the CPUC, expressly urging "the California Courts of Appeal to carefully consider the rationale for

---

6 *Id.,* p. 5.
7 *Id.,* Exhibit A.
8 *See In re: San Diego Gas & Electric Co.,* Order Denying Application, D.17-11-033 (Cal. Pub. Util. Comm'n) (Nov. 30, 2017) ("CPUC Decision 17-11-033").
9 EEI Comments, p. 6.
10 CPUC Decision 17-11-033, p. 9.
11 *Id.*

applying inverse condemnation in these types of cases."[12] They also "respectfully urge[d] the California Legislature to affirmatively address the issues of liability calculation and cost allocation in instances when utility infrastructure is implicated in private property loss."[13]

More concerning is that, in practice, past decisions indicate the CPUC is very unlikely to allow IOUs to recover wildfire costs, even under circumstances in which the electric company took reasonable steps to prevent and respond to wildfires. As a consequence of essentially what is a perfection standard, IOUs and potential investors have read the 2017 CPUC decision for SDG&E to indicate that there is very little that utilities can do operationally to ensure, with certainty, that they will meet the prudent manager standard in the event of a wildfire and be allowed to recover costs. While recent changes in the law have set forth new standards for recovery of wildfire costs,[14] there remains great uncertainty regarding the recovery of wildfire inverse condemnation costs before the CPUC.

Therefore, Liberty CalPeco respectfully urges this Commission to take steps to ensure cost recovery for wildfire damages if California continues to require that electric companies serve as the de facto wildfire insurer for the entire State. As proposed by EEI, one way to accomplish this would be for the Commission and legislature to create a distinct standard by which the CPUC will review requests for cost recovery for wildfire damages.[15] The legislature has the ability to simply and clearly direct the CPUC to grant rate recovery to electric companies for a particular class of costs and issue such a directive outlining the circumstances in which catastrophic wildfire losses should be automatically recoverable.[16]

The Commission Should Explore Additional Tools to Address Financial Risks From Wildfires

It is undisputed that the legal liabilities associated with catastrophic wildfires can be enormous. In light of the recent bankruptcy filing by PG&E, it is easy to see that wildfire-related liabilities could present an existential crisis for much smaller electrical operations like Liberty CalPeco. This is not only a problem for electrical utilities, but also for customers who depend on safe, reliable, and affordable service and for wildfire victims who need timely compensation and assistance. Even with reform of the liability regime and more

[12] Concurrence to CPUC Decision 17-11-033, p. 1.
[13] *Id.*
[14] *See*, *e.g.*, Senate Bill 901 (Dodd, 2018).
[15] EEI Comments, p. 7.
[16] *See*, *e.g.,* Cal. Pub. Util. Code § 8386(h)(3) ("The commission shall authorize the electric corporation to recover in rates the costs of the independent evaluator.").

certain cost recovery for potential wildfire damages, utilities will need a broad variety of insurance or other risk-shifting options to cover different tranches of wildfire risk and ensure that sufficient capital resources will be available to compensate wildfire victims in the event of a catastrophic loss.

In past decades, the traditional insurance market provided sufficient and affordable protection for wildfire liability for California's IOUs because wildfire liabilities were smaller. But, with the rise in frequency and severity of wildfires and the current liability regime, this is no longer the case. The traditional insurance market alone cannot provide a solution for wildfire funding for at least three reasons. First, over the past few years, insurance premiums for California's IOUs have skyrocketed. Second, it also is becoming increasingly untenable to find an ideal solution to fit those major insurance premiums into the ratemaking framework. Lastly, the current traditional insurance market does not have sufficient capacity to accommodate the scale of risks that wildfires present, particularly if wildfires continue to occur year over year without any changes to the liability regime.

As the Commission continues to analyze insurance issues, Liberty CalPeco provides its comments echoing those of EEI on the two insurance-related concepts included in the Governor's recent Strike Force Report on Wildfires (issued April 12, 2019) ("Strike Force Report").[17]

The first insurance concept in the Strike Force Report is for a "Liquidity-Only Fund" that would provide liquidity for utilities to pay wildfire damage claims pending CPUC determination of cost recovery potentially coupled with modification of cost recovery standards.[18] However, without significant changes to the application of inverse condemnation or to the cost recovery framework before the CPUC discussed above, the proposed Liquidity Fund is unlikely to provide certainty to the market. Instead, customers and IOUs would be better served if the utilities are permitted to recover self-insurance layers that are included in their general rate case. With a self-insurance layer in addition to any commercially reasonable wildfire damage insurance, each IOU can direct the funds to either investments that return income to enhance liquidity and keep sufficient cash on hand to respond to wildfire expenses.

---

17 *Wildfires and Climate Change: California's Energy Future* (April 12, 2019) ("Strike Force Report").

18 *Id.,* p. 35.

The second insurance concept in the Strike Force Report is the creation of a "Catastrophic Wildfire Fund" coupled with a revised cost recovery standard to spread the cost of catastrophic wildfires more broadly among stakeholders.[19] If properly designed, the Wildfire Fund has the potential to deliver substantial benefits to electricity consumers, IOUs, insurance companies, homeowner ratepayers, and the State and local governments. Any fund administering property owner claims must recognize that the compensation provided to wildfire victims in California in events in which electric companies are found not to have violated a fault standard is effectively a form of social insurance. Therefore, it is essential that any approach to compensating wildfire victims recognizes the central role that communities play in wildfire hazard reduction and create incentives for individual property owners to mitigate their wildfire hazard exposure. Additionally, Liberty CalPeco concurs with the recommendations of EEI regarding the potential creation of a Wildfire Fund, including the following fund design recommendations:[20]

- Recovery by insurers should be capped at a level that is consistent with the typical settled value of subrogated insurance claims.
- Property owners should be required to present their claims for the underinsured portions of their losses to the fund, allowing for the implementation of a number of mechanisms to encourage property owners to maintain adequate insurance coverage and ensure that Wildfire Fund dollars are distributed in a manner that provides more protections for lower income customers.
- The Commission should revise the Strike Force Report Catastrophic Wildfire Fund concept to develop a framework in which individual claimants with uninsured losses can also present their claims directly to the Wildfire Fund.
- The Commission should adopt a model for the Wildfire Fund based on the flood-specific provisions of the Stafford Act in which property owners are required to maintain insurance after receiving an initial payment under the federal disaster relief programs.

Other Potential Opportunities for More Effective Wildfire Hazard Mitigation

The Strike Force Report correctly recognizes that "All stakeholders must come together to address the cumulative liability of uncontrolled fires."[21] Accordingly, any comprehensive approach to addressing the challenge of catastrophic wildfire events must include efforts by

---

[19] *Id.,* p. 37.
[20] EEI Comments, pp. 10-13.
[21] Strike Force Report, p. 49.

all stakeholders to reduce wildfire hazard exposures. For wildfire hazard mitigation to be most effective, the Commission should evaluate structures that could help all stakeholders use their resources collectively to target the actions that will lead to the most significant reductions in wildfire hazard exposure. Such a structure would require two innovations by the Commission not raised in the Strike Force report. First, the Commission should explore tools to evaluate, rank, and deploy capital to support the most effective measures to reduce hazard exposure. Second, the Commission should evaluate whether an additional pool of capital will be necessary to effectively mitigate hazard exposure.

With respect to hazard mitigation by utilities, the Wildfire Mitigation Plans required by Senate Bill 901 (Dodd, 2018) ("SB 901") will be a centerpiece of utility efforts to mitigate wildfire hazards as they cut across a broad range of initiatives in addressing wildfire risks related to utility infrastructure. Liberty CalPeco submitted its Wildfire Mitigation Plan to the CPUC on February 6, 2019. Liberty CalPeco has applied a thoughtful approach in developing a holistic strategy to mitigate utility-posed wildfire risks pursuant to SB 901. The process included a strategic, risk-based evaluation that resulted in efforts to improve operational practices, fortify existing preventative and response plans, and coordinate responsibilities within the utility to monitor and enhance the plan over time. Reforming the CPUC to provide comprehensive technical evaluation of Wildfire Mitigation Plans and to monitor implementation could provide additional tools to promote wildfire hazard mitigation. The Commission should evaluate the role that new technical experts at the CPUC could play in evaluating emerging best practices and adding any requirements for Wildfire Mitigation Plans that are specified by the legislature.

With respect to hazard mitigation by State and Local Governments, the Commission should evaluate the role that changes to and enforcement of existing state and local government policies could mitigate wildfire risk. The Commission and local governments must grapple with the larger climate adaptation question of how wildfire risks will continue to evolve and how land use practices must change to respond to increased wildfire hazard in the future. State and local governments should also take measures to ensure that they have invested in and provided sufficient infrastructure for emergency response that reflects the land use choices made in their communities. The Commission also should evaluate what mechanisms are available to State and local governments to enforce the defensible space rules and how they could be encouraged to do so.

With respect to hazard mitigation by the insurance industry, Liberty CalPeco supports the Strike Force Report's recommendation that insurance rates be structured to provide

communities or individual homeowners with financial incentives to engage in wildfire hazard mitigation. In order for such incentives to be effective, baseline property insurance rates in the wildland-urban interface should be allowed to increase significantly, with substantial rate discounting offered for risk reduction measures. The Commission should evaluate the types and levels of incentives that would be necessary to encourage property owner hazard mitigation and evaluate what changes, if any, need to be made at the California Department of Insurance to compel the use of such pricing incentives.

Conclusion

Liberty CalPeco thanks the Commission for its efforts thus far to delve into critical issues and develop a recommendation to address wildfire risk in California. We hope that the Commission will consider the perspectives of Liberty CalPeco.

Sincerely,

/s/ Greg Sorensen

Greg Sorensen
President, West Region
Liberty Utilities (CalPeco Electric) LLC