**Commission on Catastrophic Wildfire Cost and Recovery**
**Comments of Pacific Gas and Electric Company**
**April 22, 2019**

## Introduction

Pacific Gas & Electric Company ("PG&E") is grateful for the opportunity to respond to the request for comments issued by the Commission on Catastrophic Wildfire Cost and Recovery ("Commission"). Without question, the loss of life, homes and businesses during these devastating wildfires is heartbreaking, and the company remains focused on helping affected communities recover and rebuild. The safety of PG&E's customers and the communities is our most important responsibility, and we are committed to further enhancing safety and helping protect all those we serve from the ever-increasing threat of wildfires. PG&E understands that other commenters will provide comprehensive responses to the questions posed by the Commission. PG&E focuses its comments on three topics: the need to reform the strict liability standard for inverse condemnation (topic 1 in the Commission's questions), the structure of a wildfire fund (topic 3), and community and wildfire victim impacts (topic 4).

## Executive Summary

The Governor's Strike Force Report correctly observes that the strict liability standard for inverse condemnation claims against utilities for property damage resulting from wildfires should be reformed. The existing standard essentially makes utilities the insurers of last resort for property damage resulting from wildfires caused by utility equipment. This exposes utilities to massive liabilities, which in turn jeopardizes their financial stability and directly interferes with the State's goals of providing safe, reliable and clean energy. The strict liability standard should be replaced with a reasonableness standard, which the courts have applied in the context of flood control projects.

The Governor's Strike Force Report also correctly highlights the need for a comprehensive and durable fund, supported by multiple stakeholders, to socialize the costs of property damage resulting from wildfires. This Commission should consider the benefits of expanding the fund to cover all catastrophic wildfires, not just those caused by utilities. A universal, no-fault catastrophic fund would provide a safety net to underinsured and uninsured property owners, as well as provide significant reinsurance to property insurance carriers. Such a fund could be supported by contributions from utilities, premiums from property insurance carriers in exchange for reinsurance for catastrophic wildfire risk (similar to the Florida Hurricane Catastrophe Fund), credit support and direct funding from the State, and potentially also surcharges on policyholders in high fire-risk areas. Property insurers would receive reimbursement for a percentage of their losses after a retention. The fund would also pay property insurers to provide extended coverage to their policyholders for a percentage of their losses in excess of their underlying policy coverage, up to a cap, for a catastrophic wildfire, regardless of cause, thereby reducing the problem of the underinsured. Finally, those without any property insurance would receive a baseline payment amount directly from the fund.

## I. The Current Wildfire Liability Regime Poses Profound Risks to Public Utilities' Ability to Continue to Provide Service to California Consumers

The current application of inverse condemnation allows essentially limitless claims for wildfire property damage to be brought against utilities under a strict liability standard. As described in the Governor's Strike Force Report on "Wildfires and Climate Change: California's Energy Future" (April 12, 2019), the current legal regime is unworkable and calls out for reform, specifically through a shift to a fault-based standard.

The strict liability standard makes little sense as applied to utilities, which are legally required to provide service in all areas of the State. Utilities therefore must operate in areas where

the risk that utility facilities will be involved in ignition of a wildfire is substantially elevated due to factors that the utility cannot control, including climate change, high winds, drought, tree mortality, land-use and development patterns, and building codes. Additionally, proper incentives for safe utility operation can be created without inverse condemnation claims governed by strict liability: If utilities fail to meet safety standards, or if their facilities are involved in fire ignition, utilities can face financial liability for personal injury claims or government claims for fire-fighting costs, and, in the case of investor-owned utilities (IOUs), regulatory action. This approach has a proven track record in other States, and there is nothing unique about utility operations in California that prevents its application here.

Ultimately, as explained in the Governor's Strike Force Report, the application of a strict liability regime—paired with uncertainty about IOUs' ability to recover wildfire-related costs in rates—harms customers and the State. IOUs (through their investors) are left to shoulder all costs of property damage from catastrophic wildfires, as well as all attorneys' fees and expert costs from litigation, if their facilities were involved in ignition of a fire. That result compromises utilities' ability to raise the capital needed to maintain adequate and safe service, to invest in safety improvements, to fund the State's renewable energy goals, and to continue to provide high-quality jobs and benefits to thousands of Californians. (See Strike Force Report, pp. 28-33.) With no backstop or limitations, the astronomical costs of wildfire liability can create, and has created, a massive "threat of insolvency for California's utilities." (*Id.*, p. 1.)

Accordingly, as the Governor's Strike Force Report recognizes, a new approach is needed to preserve the financial solvency of California's utilities by "allocat[ing] costs resulting from wildfires in a manner that shares the burden broadly among stakeholders, including utilities (ratepayers and investors), insurance companies, local governments, and attorneys." (Strike Force

Report, pp. 2-3.) The Report proposes changing strict liability to a fault-based standard under which utilities would pay for property damage only if caused by their misconduct. That would equitably "shift the risk of property loss to insurance companies and uninsured or underinsured property owners" only "in cases where the utility was not a bad actor." (*Id.*, p. 36.)

In developing the Strike Force's suggestion, the Commission should consider the application of a reasonableness standard like that which is already applied by the California courts in inverse condemnation actions involving flood control projects. The standard would impose liability only if the utility's conduct posed an unreasonable risk of the damage to the plaintiff's property *and* the conduct posing the unreasonable risk was a substantial cause of the damage to the plaintiff's property. It would look to the following factors: (a) the overall purpose of the project; (b) the benefits of the project to the plaintiff; (c) whether the utility could have chosen another, less risky approach, given budgetary and other constraints; (d) how much damage the plaintiff suffered, and the extent to which it could have protected itself against the risk of such damage; (e) whether the damage is a normal risk of land ownership; and (f) whether the failure of the project damaged a large number of property owners, or instead singled out the plaintiff.

The reasonableness standard is appropriate for inverse claims against utilities based on wildfire damage because the Supreme Court's reasons for adopting the standard in flood control cases are applicable. (See *Bunch v. Coachella Valley Water Dist.* (1997) 15 Cal.4th 432, 436-437.) *First*, the Court explained that decisions about where to place flood control projects, how to design them, and how to construct them necessarily involve a complex balancing of interests and risks. The government cannot ensure that a flood control project will be perfect, and it has to take into account the trade-off between higher costs and risks. *Second*, if a flood control project fails, the damage to private property could be enormous. Exposing the government to automatic liability

for all such damage, even if the government acted reasonably, would be unfair and could have the effect of discouraging the government from installing flood control projects in the first place.

The same reasons apply in the context of inverse condemnation claims arising from wildfires. *First,* as with flood control projects, decisions about placement, design, maintenance, and operation of utility facilities, including issues concerning how to maintain surrounding vegetation and under what circumstances to shut off power, involve complex balancing of risks and costs. For example, changing the design of those facilities often involves significant increased costs, which in turn leads to higher rates; similarly, shutting off power in high-wind conditions can reduce the risk that a downed wire will start a fire, but can also leave vulnerable customers without power. These trade-offs are difficult, and it is inequitable to make utilities strictly liable for reasonable choices that can be second-guessed in hindsight. *Second*, also like flood control projects, the property damage that can result from a wildfire is potentially enormous. A spark from a single downed wire or failed tower can start a fire that quickly spreads over thousands of acres when the weather is hot and the winds are strong—circumstances that the utilities cannot control, and that, unfortunately, are becoming more common. Making utilities strictly liable for all resulting damage, even when they acted reasonably, threatens the utilities' ability to carry out their mission of providing essential services to Californians. Thus the "reasonableness" standard strikes the right balance in wildfire cases, just as it does in the flood control context. Utilities would not be immunized from liability, but would continue to have the obligation to act reasonably, maintaining proper incentives for safe utility operation.

Importantly, the Legislature could effectuate a reform of the strict liability standard to a reasonableness standard via statute. A constitutional amendment is not required. Under California law, there is a "strong presumption" in favor of the Legislature's interpretation of a Constitutional

provision unless it is directly contrary to the Constitution's unambiguous language. (*See, e.g.*, *Property Reserve, Inc. v. Superior Court* (2016) 1 Cal.5th 151, 198-199.) In adopting strict liability for inverse condemnation claims (outside the flood control context), the California Supreme Court explained that prior decisions had applied two different interpretations of the operative constitutional provision (Cal. Const., art. I, § 19): Under one interpretation, government liability was limited to that which a private party would incur if it had caused the damage; under the other interpretation, the government was strictly liable. As a matter of "interpretation and policy," the Court elected the strict liability standard. (*Albers v. Los Angeles County* (1965) 62 Cal.2d 250, 261-262.) But in light of different policy considerations, the Court also adopted the reasonableness standard for flood control projects as described above. (*E.g.*, *Belair v. Riverside County Flood Control Dist.* (1988) 47 Cal.3d 550.) Read together, these decisions show that a strict liability standard is not mandated by the language of the Constitution itself and that a reasonableness standard is also consistent with the Constitution. Accordingly, the Legislature has the authority to change the strict liability standard currently applied to inverse condemnation claims in the gas and electric utility context, such as those that involve wildfire damages, to one that requires a showing that a utility acted unreasonably.

## II. The Creation of a Wildfire Fund that Provides Compensation for the Collective Causes and Costs of Catastrophic Wildfires is Imperative

A wildfire fund would socialize the costs of wildfires and provide assistance to those whose property is damaged and who may not have sufficient insurance coverage. The Strike Force Report suggested the establishment of a "well-capitalized wildfire fund that would create a buffer to absorb a significant portion of the wildfire liability costs that might otherwise be passed on to ratepayers" and "provide…utilities a source of immediate funding for the claims asserted against them for catastrophic wildfire damages." (Strike Force Report, p. 37.)

The Report sketches a general vision for a fund to which IOUs would be required to contribute, and which municipally owned utilities could elect to join as well. It envisions the creation of a trust to pay "all subrogation claims and reimburse utilities for the costs of judgments on or settlements of uninsured and underinsured victims' claims." (Strike Force Report, p. 38.) Insurance carriers might receive only "settlements at a stated percentage of the validated amount of their claim" from the fund, and would be barred from pursuing subrogation claims against any entity other than the trust. (*Ibid.*) With respect to uninsured and underinsured victims, the Governor's Strike Force proposed that utilities could be responsible for "litigating or settling" claims brought by these individuals and then seek reimbursement from the trust. (*Ibid.*) This reimbursement would provide certain unspecified incentives for utilities to swiftly and fairly settle with uninsured and underinsured property owners. Once the wildfire trust's funds are depleted, "ratepayers will be responsible for costs [arising out of catastrophic wildfires] thereafter." (*Id.*, pp. 37-38.)

The Strike Force fund concept is an important step towards the creation of a sustainable regulatory system that adequately addresses the needs of wildfire victims while still ensuring that utilities are not forced to bear potentially crippling costs in the wake of wildfires. The fund concept should be further developed and expanded, with the overarching goal of providing a durable and comprehensive mechanism to address the climate change-driven risks to the State of all catastrophic wildfires. While the Strike Force Report references contributions by utilities and limitations on subrogated claims, the Commission should also consider the benefits of contributions from property insurance carriers in the form of premiums in exchange for reinsurance for catastrophic wildfire risk. This is similar to the model used successfully by the Florida Hurricane Catastrophe Fund. In addition, because catastrophic wildfires can occur without any

involvement by utilities, and because the consequences of such wildfires affect the entire State, a financial contribution by the State should be evaluated. Finally, the possibility of raising revenues via a surcharge on property insurance premiums on policyholders in high fire-risk areas should be considered as well. With these sources of funds, a well-capitalized fund could be established that would provide universal no-fault coverage for all catastrophic wildfires, whether or not caused by utilities.

Instead of a uniform percentage reduction in recovery on subrogation claims, the Commission should consider a structure that is more consistent with a true reinsurance product. For example, property insurers could be required to have a retention for first-dollar losses up to an actuarially-based amount; this retention could be lower for utility-caused wildfires than others. Above the retention, property insurers would receive reimbursement for a percentage of loss elected in advance based on the premium paid (e.g., 45%, 75%, 90%). However, there should be a tranche of coverage for utility-caused fires for which the insurers receive a fixed percentage of recovery, which may be lower than the percentage for higher losses.

The initial capitalization of the fund could come from a combination of utility contributions, as well as State funding and credit in support of revenue bonds. The utilities and insurance carriers could make ongoing contributions to support the fund's own reinsurance and bonds, and both utilities and insurance carriers could recover those ongoing costs from their customers. In the event a utility causes a fire that results in payments by the fund, that utility would pay the fund a percentage of the losses up to a cap, with the remainder replenished by the other utilities, the State, and potentially policyholders in high fire-risk areas via a surcharge, depending on the magnitude of the loss.

Finally, the fund could be structured to provide a "safety net" for uninsured and underinsured wildfire victims. The fund could address the underinsured by requiring property insurers to offer (at no cost to the policyholder) extended coverage that would pay policyholders a percentage of their loss not covered by the underlying policy, up to a cap, for any catastrophic wildfire. In return, the fund would pay the property insurers a premium based on an actuarial evaluation of the cost of this additional coverage. The property insurers would then be responsible for adjusting these losses, along with the losses covered by the underlying policy. Policyholders would have the option to decline the extended coverage at the time the policy is written, in which case they would retain the right to sue a utility that caused the wildfire. The fund could also provide a mechanism for property owners who lack any insurance to seek compensation from the fund for a percentage of their actual uninsured property losses, up to a cap. Any property owner who suffered property damage should also have the opportunity to seek an interim payment from the fund if they faced near-term economic hardship as a result of a wildfire. Recovery would be limited to the resources made available by the fund. Property owners would, however, have the ability to opt out of the fund's coverage on an annual basis in order to preserve the right to sue a utility. For those who decline the extended coverage or opt out of baseline coverage or interim payments, the fees paid to the property owner's attorney should be capped.

PG&E perceives a number of benefits to the Strike Force wildfire fund, if further developed as suggested above. It serves to socialize the costs of property damage caused by wildfires while still maintaining reasonable financial incentives for property owners to purchase insurance and utilities to take prudent steps to avert wildfires. It also provides insurance carriers and public utilities, and their prospective investors, with greater certainty regarding the likely costs they would be required to bear in the event of a catastrophic wildfire. Finally, it envisions a role for

the State in this process commensurate with the public interest in ensuring that property owners receive compensation for the damages they may suffer as a result of a catastrophic wildfire and in safeguarding public utilities and insurance carriers' ability to continue to serve California's communities.

## III. The Creation of a Wildfire Fund Will Assist in Addressing the Financial Needs of Communities and Wildfire Victims

The current regulatory regime has failed to adequately socialize the costs associated with the increased severity and frequency of wildfires, such that IOUs have become the sole recourse for property owners and insurance carriers that have been impacted by a wildfire. When these costs are so high that a utility must file for bankruptcy, as PG&E did earlier this year, the utility becomes subject to a highly restrictive set of requirements set forth in the Bankruptcy Code which effectively preclude it from paying any individual creditors—including property owners and others impacted by a wildfire—until approval is received from a bankruptcy judge. To emerge from bankruptcy, an IOU must raise large amounts of new capital to fund those claims and to support future investments. Until that time, creditors, including wildfire victims, are left in limbo. Unless and until a clear and durable system for socializing wildfire costs is established that provides clarity regarding utilities' financial exposure to future wildfire events, PG&E will be unable to attract the capital it needs to emerge from Chapter 11 and the State's other IOUs may remain on negative credit watch per the rating agencies. This Commission's work is critical to developing policy recommendations that can bring that needed clarity, particularly in the areas of inverse condemnation reform and a comprehensive wildfire fund.

## IV. Conclusion

PG&E is grateful for the opportunity to provide these comments and stands ready to provide the Commission with any additional information that may be useful to it at its request.