



**TABLE OF CONTENTS**

**I. INTRODUCTION.....1**

**II. RESPONSE TO SPECIFIC INTERVENOR CONCERNS.....2**

**A. NEED FOR A WILDFIRE COST RECOVERY MECHANISM.....2**

**B. REASONABLENESS REVIEW .....4**

**C. EFFECT ON SAFETY .....5**

**D. THIRD PARTY RECOVERIES .....7**

**E. WIPBA .....8**

**F. SHAREHOLDER COMPENSATION .....11**

**G. OTHER ISSUES .....11**

**III. ALTERNATIVE SDG&E AND SOCALGAS WILDFIRE COST  
RECOVERY PROPOSAL .....14**

**A. SUMMARY OF ALTERNATIVE WEBA PROPOSAL .....15**

**B. RATIONALE FOR ALTERNATIVE PROPOSAL .....16**

**ATTACHMENT A.....A-1**

**REBUTTAL TESTIMONY  
(LEE SCHAVRIEN)**

**I. INTRODUCTION**

San Diego Gas & Electric Company (SDG&E) and Southern California Gas Company (SoCalGas) continue to support the Joint Amended Application (Amended Application) originally submitted in this proceeding on August 10, 2010 by SDG&E, SoCalGas, Southern California Edison Company (SCE), and Pacific Gas and Electric Company (PG&E). SCE and PG&E have sought to withdraw from this proceeding based on their concern that negotiations in this proceeding have not led to a settlement, and that “several related proceedings before the Commission have considerably constrained party and Commission resources, thus making it difficult to devote appropriate attention to the progress of the proceeding.”<sup>1</sup> SDG&E and SoCalGas do not have the same concerns. We continue to believe that the issues presented by the Amended Application are important, timely, and worthy of the time of both the Commission and interested parties.

Accordingly, SDG&E and SoCalGas will present the Amended Application on our own, and request Wildfire Expense Balancing Accounts (WEBAs) and related wildfire cost recovery procedures cost for SDG&E and SoCalGas. Our proposals in this proceeding now apply only to SDG&E and SoCalGas, and not to SCE or PG&E. To that end, the SDG&E and SoCalGas will continue to present the following Amended and Restated Direct Testimony, originally served on August 10, 2010:

<b><u>Direct Testimony</u></b>	<b><u>Witness</u></b>
Policy	Lee Schavrien
Cost Recovery	Lee Schavrien
Jonathan Ball on Insurance	Jonathan Ball
SDG&E and SoCalGas Insurance	Maury De Bont
Insurance Procurement Consultative Process	Maury De Bont

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<sup>1</sup> SCE and PG&E Motion to Withdraw dated November 9, 2011, at 2.

1 Ratemaking-Financing

Ken Deremer

2 SDG&E Spending Metrics

Norm Kohls<sup>2</sup>

3 SoCalGas Spending Metrics

Gina Orozco-Mejia

4 SDG&E and SoCalGas will not sponsor SCE or PG&E insurance and spending metrics  
5 testimony, since this information is specific to SCE and PG&E, and not necessary to SDG&E's and  
6 SoCalGas' WEBA proposals. In addition, the direct testimony listed above will need certain limited  
7 cleanup prior to submission to the Commission in order to make it clear that SCE and PG&E are no  
8 longer applicants (e.g., deletion of SCE and PG&E from the definition of Utilities; replacement of the  
9 draft exemplary SCE tariffs in Chapter 5 with draft exemplary tariffs for SDG&E). To facilitate this  
10 limited cleanup, SDG&E and SoCalGas propose supplying parties with redlined and clean corrected  
11 direct testimony at least two weeks prior to the start of evidentiary hearings.

## 12 **II. RESPONSE TO SPECIFIC INTERVENOR CONCERNS**

### 13 **A. NEED FOR A WILDFIRE COST RECOVERY MECHANISM**

14 Several intervenors assert that there is no need for a wildfire recovery mechanism. According to  
15 DRA, "[t]he Commission should retain the 'case-by-case' perspective through a memorandum account,  
16 or other regulatory mechanism, to deal with unusual circumstances such as excessive wildfire costs."<sup>3</sup>  
17 CPSD states that:

18 Existing processes already afford the Utilities the ability to recover the  
19 reasonable costs associated with wildfires. These include general rate cases  
20 (GRCs), Z-factors and the Utilities' ability to submit at any time applications  
21 for recovery of other costs.<sup>4</sup>

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<sup>2</sup> Mike Hale, SDG&E's original witness on this topic, retired in June of 2011.

<sup>3</sup> DRA Testimony at 2.

<sup>4</sup> CPSD Testimony at 2.

1 SDG&E and SoCalGas agree that there are existing processes such as Z-Factor applications or  
2 emergency applications that give them the ability to seek recovery of wildfire costs.<sup>5</sup> But we do not  
3 agree that these existing processes are a reasonable substitute for the WEBA mechanism that we have  
4 proposed in this proceeding. Intervenors who make these arguments would leave the Utilities exposed  
5 to massive wildfire costs with no established provisions for recovery. As explained in our direct  
6 testimony, this uncertainty threatens the financial health of the Utilities, both now and in the future.  
7 Moreover, lack of an established cost recovery mechanism may create an incentive for the Utilities to  
8 take fire prevention efforts that are not cost effective, while causing interested parties to argue against  
9 funding for proposed fire prevention activities because they view wildfires and wildfire prevention as  
10 just the Utilities' problem.

11 With Assembly Bill (AB) 57, the state Legislature recognized that it was in the public interest to  
12 establish an up-front framework for utilities to recover the large costs of energy procurement, rather than  
13 leaving utilities exposed to "case-by-case" applications for recovery of such costs after they are  
14 incurred. Similarly, the Commission should establish a framework and criteria now for recovery of  
15 large wildfire costs. The Legislature does not need to authorize the establishment of a framework for  
16 cost recovery;<sup>6</sup> the Commission can adopt one as a policy. Although there are differences between  
17 energy procurement and wildfire costs, the principle that utilities should not be forced to carry large  
18 costs on their books without a clear framework and standards for recovery applies equally in both  
19 contexts.

20 Likewise, the Commission's adoption of Catastrophic Event Memorandum Accounts (CEMAs)  
21 for the Utilities supports the establishment of the WEBAs we have proposed. Yes, CEMAs do not  
22 directly apply to the wildfire costs that are at issue in this proceeding because we are dealing with third

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<sup>5</sup> It is not certain, however, that the existing Z-Factor process will continue after SDG&E's and SoCalGas' 2012 GRCs.

<sup>6</sup> CPSD Testimony at 9.

1 party claims costs and not wildfire-related damage to Utility infrastructure. But the underlying principle  
2 behind both CEMA and WEBA – that the Utilities should recover costs resulting from natural disasters,  
3 so that they can continue to provide service -- is the same.

4 Mussey Grade argues that major wildfires involving power lines are rare events.<sup>7</sup> Even so, no  
5 party denies the risk of wildfires in Southern California. The fact that major wildfires involving power  
6 lines do not take place often is not a good reason to put off adoption of a wildfire cost recovery  
7 mechanism. Events covered by CEMA do not happen often either, yet the Commission has determined  
8 that the CEMA cost recovery process is both reasonable and necessary. Moreover, a September 2011  
9 wildfire in Texas that killed two people and destroyed more than 1,500 homes is a grim reminder that  
10 major wildfires are not as uncommon as we would like them to be.<sup>8</sup> Likewise, a November 2011  
11 wildfire in Reno that destroyed 15 homes and damaged at least 40 more demonstrates that the ongoing  
12 risk of wildfires involving power lines is not confined to other states.<sup>9</sup>

### 13 **B. REASONABLENESS REVIEW**

14 CPSD suggests that wildfire claims costs should be subject to reasonableness review.<sup>10</sup> SDG&E  
15 and SoCalGas do not agree. Reasonableness review has historically applied to expenditure decisions for  
16 the costs of utility-supplied services, and the standard of review has traditionally been based upon an  
17 assessment of the information available to the utility at the time the expenditure decision was made.  
18 Wildfire claims costs do not fit this framework. There is no deliberate decision by a utility to incur  
19 wildfire costs. Moreover, it is impossible to control most of the circumstances that lead to wildfires, and  
20 it is often very difficult, or even impossible, for a Utility to control the extent of any particular fire.

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<sup>7</sup> Mussey Grade Testimony at 3.

<sup>8</sup> See the following Insurance Journal article: <http://www.insurancejournal.com/news/southcentral/2011/09/22/216979.htm>.

<sup>9</sup> See the following Washington Post article: [http://www.washingtonpost.com/national/reno-fire-officials-point-to-power-lines-as-likely-cause-of-2000-acre-fire/2011/11/19/gIQAh1mwbN\\_story.html](http://www.washingtonpost.com/national/reno-fire-officials-point-to-power-lines-as-likely-cause-of-2000-acre-fire/2011/11/19/gIQAh1mwbN_story.html).

<sup>10</sup> CPSD Testimony at 9.

1           Supplying customers with natural gas or electricity brings with it an inherent risk of fire,  
2 particularly customers located in extreme or very high fire threat zones. The Utilities can and do take  
3 measures to reduce this risk, but they cannot eliminate it. Measures to mitigate the risk of fires have  
4 both financial and physical limits. Unlike ordinary businesses that can choose whether to take on the  
5 risks associated with selling a product, the Utilities are obligated to provide service to all customers  
6 throughout their service territories, including customers who choose to live in fire-prone areas. When  
7 utilities are held liable for wildfire-related claims, the resulting payments are an unavoidable cost of  
8 providing utility service. As such, the Utilities should be allowed to recover costs falling within  
9 Categories A and B under our proposed WEBA mechanism, without any additional review of the factors  
10 that led to such costs.

### 11           **C.     EFFECT ON SAFETY**

12           Certain intervenors claim that a wildfire cost recovery mechanism will have a negative effect on  
13 safety. For example, CPSD asserts that “the WEBA proposal would so thoroughly insulate the Utilities  
14 from the potentially catastrophic results of unsafely operating their systems, that it will diminish the  
15 Utilities’ focus, such as it is, on operating their systems safely.”<sup>11</sup> Likewise, DRA asserts that:  
16 [b]alancing account treatment could have a deleterious impact on the utility’s safety practices because  
17 the risk for cost recovery may be significantly reduced.”<sup>12</sup> These claims are unfounded, and badly off  
18 target.

19           The Utilities take their responsibility to provide safe and reliable service very seriously, and we  
20 do so day in and day out, every day. Wildfires threaten the lives and livelihoods of our customers, our  
21 employees (most of whom live with their families in our service territories), our infrastructure and  
22 equipment, and our reputations. The Utilities will never ignore fire safety, and the adoption of a

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<sup>11</sup> CPSD Testimony at 3.

<sup>12</sup> DRA Testimony at 6; see also Center for Accessible Technology (CAT) Testimony at 4.

1 recovery mechanism for wildfire costs will not change our approach to fire safety one bit. The safety-  
2 related arguments by intervenors ignore the fact that SDG&E in particular has been a leader with respect  
3 to fire safety, hardening its system aggressively, and being a strong advocate for safety-related changes  
4 in the Commission's ongoing fire safety rulemaking, R.08-11-005. In fact, in the current second phase  
5 of this rulemaking, SDG&E has sponsored a number of fire safety proposals that are more aggressive  
6 than proposals by CPSD.<sup>13</sup>

7 The intervenors do not mention that the Utilities are required to meet stringent safety  
8 requirements, including General Order 165 inspection standards and General Order 95 design and  
9 maintenance standards. The Utilities could not ignore these requirements even if we wanted to (and we  
10 do not). The Commission inspects our compliance with its standards on a regular basis. If the Utilities  
11 chose to ignore fire safety, we would hear about it very soon, and face substantial penalties as a result.  
12 As demonstrated by the \$38 million penalty recently imposed upon PG&E relating to the Rancho  
13 Cordova explosion in I.10-11-013, and the \$100 million of penalties that have been proposed for the  
14 2007 Malibu Canyon wildfire in I.09-01-018, the penalties that the Commission can impose for  
15 violations of its fire safety rules are substantial, and a strong financial deterrent to the Utilities if they  
16 should ever consider ignoring fire safety (which they would not).<sup>14</sup>

17 Likewise, the 95/5 sharing proposed in the Utilities' Amended Application WEBA proposal (up  
18 to a \$20 million 12-month cap), together with the potential for up to \$10 million of Tier 1 access fees in  
19 any 12-month period, provide an additional financial incentive for the Utilities to pursue fire safety  
20 activities such as system hardening, and to design, maintain, and operate their systems in a safe manner.  
21 These potential sharing amounts are substantial. Combined with the potential for penalties of the sort

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<sup>13</sup> For example, SDG&E's Rule 18A proposal, SDG&E's Rule 31.2 and 80.1A proposal, and SDG&E's new Rule 91.5 proposal that would require communication companies to mark their overhead facilities.

<sup>14</sup> In addition, Resolution ALJ-274 adopted by the Commission on December 1, 2011, gives CPSD broad authority to penalize gas corporations for safety violations.

1 proposed for the Malibu canyon wildfire, it is simply not credible for intervenors to argue that the  
2 Utilities' WEBA proposal would somehow create a financial incentive to compromise safety.

3 **D. THIRD PARTY RECOVERIES**

4 Under the WEBA proposal in the Amended Application, recoveries from third parties, net of  
5 legal expenses, will be shared 90/10 between a Utility and its customers until the Utility has been fully  
6 reimbursed for costs it has absorbed for that wildfire; thereafter, the Utility and its customers will share  
7 any remaining recovery on a 10/90 basis.<sup>15</sup> AT&T expresses concern about this provision, claiming that  
8 it would encourage the Utilities to pursue "tort claims litigation beyond the economic costs of their  
9 losses."<sup>16</sup> According to AT&T, this provision "would encourage the Utilities to expand this segment of  
10 their 'business' beyond what is economically efficient for the provision of gas or electric service . . ."<sup>17</sup>  
11 TURN believes that the Commission should retain the right to allocate recoveries from third parties  
12 more heavily to ratepayers than the Utilities have proposed.<sup>18</sup>

13 These concerns are unfounded. This third party recovery provision simply provides the Utilities  
14 with a strong incentive to pursue wildfire-related claims against third parties. Any recovery from third  
15 parties benefits both the Utilities and our customers -- and any sizable recovery (i.e., one above \$30  
16 million annual wildfire risk taken on by the Utilities) primarily benefits our customers. This incentive to  
17 pursue wildfire-related claims against potentially responsible third parties will not create a new line of  
18 business for the utilities, or cause us to take actions that are economically inefficient. Large wildfires do  
19 not take place often, and there are a limited and defined number of parties responsible for any particular  
20 fire. The Utilities will not engage in frivolous litigation against third parties because of this sharing  
21 mechanism. In fact, if additional profits through frivolous litigation were our goal (and it is definitely

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<sup>15</sup> Utilities' Direct Testimony at 28.

<sup>16</sup> AT&T Testimony at 2.

<sup>17</sup> AT&T Testimony at 2.

<sup>18</sup> TURN Testimony at 4.

1 not), the Utilities would actually be better off pursuing such actions under the standard test-year  
2 ratemaking regime (under which we would generally keep 100% of any unforecasted third party  
3 recovery).

4 The third party recovery sharing we have proposed is similar in nature and intent to the insurance  
5 recovery provisions found in the hazardous waste recovery mechanism adopted by the Commission in  
6 D.94-05-020.<sup>19</sup> This aspect of the hazwaste recovery mechanism is designed to give utilities a strong  
7 incentive to pursue hazwaste coverage claims against their insurers -- such claims may involve policies  
8 that are decades old, and are often heavily contested by the insurers. A similar incentive does not appear  
9 to be necessary for wildfire insurance since such coverage claims are generally pretty cut and dried –  
10 i.e., a wildfire either occurs during the policy period or it does not; there are no questions regarding  
11 statutes of limitations, or whether the contamination in question took place during the relevant policy  
12 period. At least in our experience, however, wildfire-related claims against potentially responsible third  
13 parties are generally vigorously contested by the third parties and their insurers, and so the sharing  
14 percentages we have proposed make sense.

#### 15 **E. WIPBA**

16 The Amended Application asks the Commission to authorize the Utilities to establish Wildfire  
17 Insurance Premium Balancing Accounts (WIPBAs) to record all increases or decreases from the  
18 amounts adopted in their GRCs for insurance premiums attributable to coverage for wildfire-related  
19 claims, and to consolidate and recover WIPBA balances annually.<sup>20</sup> DRA opposes this proposal,  
20 arguing that balancing account treatment “could remove any incentive for the utility to balance the risk

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<sup>19</sup> In this hazwaste recovery mechanism, insurance litigation costs are shared 70/30 between customers and shareholders; insurance recoveries are shared 70/30 until the utility and its customers have both been fully reimbursed for insurance litigation costs to date; the remaining recovery is shared 10/90 between customers and shareholders until the utility has been made whole for all hazardous substance cleanup costs to date; and any remainder is shared 60/40 over the next five years. See D.94-05-020, mimeo., at 6, and pp. 8-9 of Appendix A.

<sup>20</sup> See the Utilities’ Direct Testimony at 1-2 and 32.

1 of liability exposure against the implementation of safety measures in a cost-effective manner.”<sup>21</sup> CPSD  
2 opposes balancing account treatment on the grounds that utility insurance procurement decisions should  
3 be reviewed for reasonableness.<sup>22</sup> TURN does not oppose the Utilities’ WIPBA proposal, but suggests  
4 that the WIPBA balances be shared 95/5 between customers and shareholders.<sup>23</sup> TURN also supports an  
5 advisory mechanism so that interested parties can understand and comment on insurance coverage levels  
6 and costs.<sup>24</sup>

7           SDG&E and SoCalGas believe that the concerns expressed by DRA and CPSD regarding the  
8 proposed WIPBAs are unfounded. Balancing account treatment for wildfire insurance premiums will  
9 not remove incentives for the Utilities to implement fire-related safety measures. In fact, there is no  
10 potential connection between these two concepts unless the Utilities could somehow obtain enough  
11 wildfire insurance to eliminate all potential risk of wildfire costs in excess of insurance. As explained in  
12 detail in our direct testimony, this is simply not possible; the market for wildfire insurance is limited,  
13 and the Utilities will never be able to obtain enough wildfire insurance to cover all potential risk of  
14 wildfires.

15           The WIPBA is simply intended to protect the Utilities and their customers from fluctuations in  
16 the insurance market, while reinforcing Utility incentives to maintain the highest level of insurance  
17 coverage that can be obtained at a reasonable cost. CPSD’s after-the-fact prudence review concept  
18 creates too much risk for the Utilities, and would create a built-in disincentive against spending any  
19 more for wildfire insurance than amounts adopted in the Utilities’ most recent GRCs. In an environment  
20 of rising insurance costs, this would mean less wildfire insurance, which SDG&E and SoCalGas do not  
21 believe is a good thing. And in an environment of decreasing wildfire insurance premiums -- which may

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<sup>21</sup> DRA Testimony at 7.

<sup>22</sup> CPSD Testimony at 8.

<sup>23</sup> TURN Testimony at 5.

<sup>24</sup> TURN Testimony at 5.

1 very well be possible if we experience several years without utility-related wildfires in California --  
2 customers would not share in the decreases. Wildfire insurance premiums are so unpredictable these  
3 days that it simply makes good sense to subject these particular costs to two-way balancing.

4 TURN's proposal for 95/5 sharing of WIPBA balances is interesting, but it could still discourage  
5 the Utilities from spending more for wildfire insurance than amounts adopted in our most recent GRCs.  
6 Moreover, TURN's proposal is based upon the premise that the Utilities have a degree of control over  
7 both coverage levels and insurance carriers.<sup>25</sup> Yes, the Utilities have some degree of control over  
8 coverage levels because we propose coverage levels in our GRCs. But we are price takers in the  
9 insurance market, and obtain insurance from whichever qualified carriers are able to provide it at the  
10 most reasonable cost. TURN's WIPBA proposal contains an additional thoughtful element:

11 Because additional coverage is in the public interest if cost-effective, costs of  
12 increased coverage over forecast coverage levels would also be recoverable  
13 from ratepayers on a 100-0 basis between rate cases if the forecast average cost  
14 per unit of new coverage is less than 95% of the forecast average cost per unit of  
15 existing coverage.<sup>26</sup>

16 SDG&E and SoCalGas agree with the premise behind this particular element -- if the Utilities  
17 have an opportunity to obtain coverage above forecast levels, at a reasonable cost, we should not be  
18 penalized for doing so. But this possibility can be handled more simply by standard two-way balancing  
19 account treatment, combined with a wildfire insurance procurement consultative process. SDG&E and  
20 SoCalGas agree with TURN's suggestion of an insurance advisory mechanism so that interested parties  
21 can understand and comment on insurance coverage levels and costs. We believe that the wildfire  
22 insurance procurement consultative process we have presented in our Amended Application (and our  
23 alternative proposal below, as well) satisfies this suggestion.

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<sup>25</sup> TURN Testimony at 5.

<sup>26</sup> TURN Testimony at 5.

1           **F.     SHAREHOLDER COMPENSATION**

2           Certain intervenors oppose the shareholder compensation element of the Utilities’ Amended  
3 Application proposal.<sup>27</sup> Under this aspect of the Amended Application proposal, the Utilities would  
4 receive an annual revenue requirement to compensate them for the financial risk they would bear under  
5 the proposal. This annual revenue requirement would be calculated based upon the financial risk  
6 undertaken by the Utilities each year (\$30 million) multiplied by the average premium rate paid by the  
7 Utilities for liability insurance that year.<sup>28</sup>

8           SDG&E and SoCalGas believe that the shareholder compensation element of the Amended  
9 Application proposal has merit. However, we understand that this particular element of our proposal  
10 elicits a very strong negative reaction from intervenors, and there are other ways of compensating the  
11 Utilities for the risks we undertake to provide service to our customers. Accordingly, SDG&E and  
12 SoCalGas are dropping this particular element of the Amended Application proposal. This deletion will  
13 be reflected in the corrected direct testimony that we provide to parties and the Commission at least two  
14 weeks prior to the start of evidentiary hearings.

15           **G.     OTHER ISSUES**

16           CPSD argues that the Utilities’ WEBA proposal, “if approved, would need to be modified to  
17 provide for a significant reduction in the Utilities’ authorized ROE to reflect the reduced risks borne by  
18 the Utilities and to offset the additional profits created by the proposed WEBA mechanism.”<sup>29</sup> SDG&E  
19 and SoCalGas strongly disagree. The risk of non-recovery of uninsured wildfire costs has not been  
20 identified in our cost of capital proceedings, and is not a risk that either SDG&E or SoCalGas have been  
21 compensated for in our ROEs. To the extent that the Utilities shoulder any risk of non-recovery of

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<sup>27</sup> See, e.g., DRA Testimony at 5-6; TURN Testimony at 3.

<sup>28</sup> See the Utilities’ Direct Testimony at 33.

<sup>29</sup> CPSD Testimony at 7.

1 wildfire costs, our ROEs should be increased, not decreased. But this is a matter that can be addressed  
2 in our cost of capital proceedings.

3           TURN expresses concern that the Utilities’ WEBA proposal could require customers to pay  
4 billions of dollars in wildfire claims within 12 months, and TURN asserts that the Commission “should  
5 retain the flexibility to spread any recovery of large amounts over more time than a typical balancing  
6 account undercollection period (possibly with carrying costs above a balancing account rate together  
7 with an offset for deferred income taxes) or even to pursue securitization if costs are large enough.”<sup>30</sup>  
8 SDG&E and SoCalGas agree with TURN’s position; the recovery of large WEBA balances may need to  
9 take place over longer than 12 months, and may even require securitization under extreme  
10 circumstances. As the Utilities explained in their Direct Testimony:

11           The Utilities propose that the time frame for recovery of WEBA balances vary  
12 depending on the amount of any undercollection in the WEBA, and that prior to  
13 implementing a WEBA undercollection in rates a Utility would inform the  
14 Commission of its plan for amortizing the undercollection after analyzing the  
15 magnitude of all of the pending revenue requirement and rate changes for the  
16 subsequent year. . . .

17           . . .

18           The size of wildfire liabilities could range from modest to extremely large, and  
19 WEBA financing will vary accordingly. Balances that remain small may be  
20 accommodated within a Utility’s existing short-term borrowing program. . . .

21  
22           However, the Utilities’ short-term borrowing capacity is limited, and much of  
23 that capacity is needed to meet day-to-day operational needs, other balancing  
24 account under-collections and collateral to support energy procurement. Thus, a  
25 Utility may need to resort to financing with long-term debt and/or equity to  
26 support sizeable WEBA balances. If such circumstances occur and a Utility  
27 proposes that correspondingly higher financing costs be recorded in its WEBA,

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<sup>30</sup> TURN Testimony at 4.

1 the Utility will present a proposal to that effect in a separate application to the  
2 Commission.<sup>31</sup>

3 TURN states that the Utilities' WEBA proposal raises unanswered questions about whether  
4 certain wildfire costs and wildfire-related insurance costs should be allocated to FERC transmission  
5 rates rather than CPUC-jurisdictional distribution rates.<sup>32</sup> But these particular issues have in fact been  
6 dealt with in our WEBA proposal. As explained in our ratemaking testimony:

7 The Utilities propose that all Wildfire Claims costs be booked to the WEBA  
8 for recovery in CPUC-jurisdictional retail rates. Current regulatory policies  
9 would allocate some portion of these costs to rates under the jurisdiction of  
10 FERC. To the extent that FERC authorizes recovery of a portion of Wildfire  
11 Costs in FERC-jurisdictional rates, the WEBA will be credited by that  
12 amount.<sup>33</sup>

13 Likewise, amounts recorded in our SDG&E's WIPBA would be adjusted for costs recovered through  
14 FERC-jurisdictional rates.<sup>34</sup> In fact, SDG&E sought authorization from FERC to recover through  
15 FERC-jurisdictional rates all excess wildfire costs relating to one of the 2007 wildfires in SDG&E's  
16 service territory (the Witch fire), and was told by FERC that excess wildfire costs should be expensed to  
17 FERC Account 925 pursuant to labor ratios.<sup>35</sup>

18 In its testimony, CAT expresses concern regarding the effect of rate increases on low-income  
19 people with disabilities, and the vulnerability of people with disabilities during emergencies such as  
20 wildfires.<sup>36</sup> The Utilities recognize that these are legitimate concerns, but they do not appear to be  
21 relevant to this particular application. SDG&E and SoCalGas are simply proposing a wildfire cost  
22 recovery mechanism. We are not establishing or changing how we conduct our operations during

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<sup>31</sup> Utilities' Direct Testimony at 93-94.

<sup>32</sup> See TURN Testimony at 4.

<sup>33</sup> Utilities' Direct Testimony at 90. Because SoCalGas does not have FERC-jurisdictional rates, this particular aspect of our proposal only relates to SDG&E.

<sup>34</sup> Utilities' Direct Testimony at 92 and 100.

<sup>35</sup> 137 FERC ¶ 61,041 at 4-5.

<sup>36</sup> CAT Testimony at 6-10.

1 emergencies, and we are not designing rates or rate structures. A more appropriate venue for CAT's  
2 concerns and proposals would be a rate design proceeding (or proceedings), or a proceeding that  
3 considers the Utilities' operational approach during emergencies (SDG&E's recent EPSO application is  
4 an example, and a venue in which CAT's predecessor, Disability Rights Advocates, participated).

5 Ruth Henricks contends that the Commission should involve the California Insurance  
6 Commission and the State Legislature in this proceeding, and craft a solution to the wildfire insurance  
7 "crisis" that is similar to the FAIR insurance plan adopted in 1968 by the California Legislature for  
8 homeowners in high-risk fire areas.<sup>37</sup> SDG&E and SoCalGas believe these proposals are off the mark.  
9 We need a wildfire cost recovery mechanism even if wildfire liability coverage availability and costs  
10 should go back to pre-2009 levels. Plus, this application deals with insurance for utilities, not  
11 homeowners, so the 1968 FAIR plan is not a helpful precedent. Even if the Commission had the ability  
12 to involve either the California Insurance Commissioner or the State Legislature into this proceeding, it  
13 is very questionable whether they could take any actions which would either increase the amount of  
14 wildfire insurance available to the Utilities, or lower its cost. SDG&E and SoCalGas are interested in  
15 obtaining greater wildfire liability coverage at a reasonable cost, but the concepts proposed by Ms.  
16 Henricks do not appear like a viable way to achieve that result.

### 17 **III. ALTERNATIVE SDG&E AND SOCIALGAS WILDFIRE COST RECOVERY**

#### 18 **PROPOSAL**

19 As explained above, SDG&E and SoCalGas continue to support the WEBA proposal presented  
20 in the Amended Application. In order to address certain concerns raised by DRA, CPSD, and other  
21 intervenors, however, SDG&E and SoCalGas hereby present an alternative WEBA proposal for the  
22 Commission's consideration. This alternative proposal, set forth in Attachment A to my testimony, is in

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<sup>37</sup> Henricks' Testimony at 12-14.

1 large part based upon the hazardous waste recovery mechanism adopted by the Commission in D.94-05-  
2 020.

3 **A. SUMMARY OF ALTERNATIVE WEBA PROPOSAL**

4 SDG&E's and SoCalGas' alternative wildfire cost recovery proposal includes the following  
5 elements:

- 6 • SDG&E and SoCalGas would continue to record all wildfire costs in their respective  
7 WEMAs;
- 8 • SDG&E and SoCalGas would transfer wildfire costs to their new WEBAs once the costs  
9 for any wildfire reach \$10 million;
- 10 • All wildfire costs transferred to the WEBAs would be shared 90/10 between ratepayers  
11 and shareholders, as with existing hazardous waste recovery mechanism;
- 12 • Third party litigation costs and recoveries would be shared 90/10 between ratepayers and  
13 shareholders, as with the existing hazardous waste recovery mechanism;
- 14 • Insurance litigation costs and recoveries would be shared 90/10 between ratepayers and  
15 shareholders;<sup>38</sup>
- 16 • As with the existing hazardous waste recovery mechanism, there would be no  
17 reasonableness review of any costs or recoveries covered by this new mechanism;
- 18 • The new mechanism would apply to all SDG&E and SoCalGas wildfire costs that meet  
19 the criteria for inclusion in the utilities' WEBAs, including costs from the 2007 wildfires  
20 that SDG&E has been recording in its WEMA;

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<sup>38</sup> This treatment is similar to the WEBA proposal in the Amended Application, which simply nets insurance recoveries against wildfire costs, but it differs from the existing hazardous waste recovery mechanism which has a somewhat complex sharing formula for insurance costs and recoveries that reflects issues unique to hazardous waste-related insurance claims.

- 1 • As with the existing hazardous waste recovery mechanism, SDG&E and SoCalGas would  
2 recover WEBA costs in the subsequent proceeding or proceedings that they deem  
3 appropriate;
- 4 • SDG&E and SoCalGas would provide informational notices to the Commission’s Energy  
5 Division within 15 days after costs reach \$10 million for any wildfire;
- 6 • SDG&E and SoCalGas would submit a WEBA annual report to the Commission’s  
7 Energy Division for any calendar year in which they record costs or recoveries in their  
8 respective WEBAs;
- 9 • As with their proposal in the Amended Application, SDG&E and SoCalGas would  
10 establish WIPBAs for changes up/down from the amounts adopted in the utility’s General  
11 Rate Case for insurance premiums attributable to coverage for Wildfire-related claims;  
12 and
- 13 • SDG&E and SoCalGas would also establish a wildfire insurance procurement  
14 consultative process so that customer representatives can better understand and provide  
15 input regarding wildfire insurance coverage levels and costs.

16 **B. RATIONALE FOR ALTERNATIVE PROPOSAL**

17 The Utilities submitted their Amended Application in response to a December 21, 2009 Ruling  
18 of Commissioner Simon and ALJ Bushey Directing Applicants to Amend Application (ACR). The  
19 ACR directed the Utilities to amend their August 2009 application to address concerns raised in various  
20 protests that 100% rate recovery would remove the Utilities’ “financial motivation to defend” third-party  
21 claims for wildfire damages and that “[f]inancial incentives for prudent risk management and safety  
22 regulation compliance are substantially undermined by the presumption of recovery from ratepayers.”<sup>39</sup>

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<sup>39</sup> ACR at 7.

1 The proposed wildfire recovery mechanism described in the Amended Application and  
2 supporting testimony responds to these concerns by requiring the Utilities to absorb up to \$10 million of  
3 Tier 1 Excess Wildfire Costs for all wildfires within any 12-month period, and up to \$20 million of Tier  
4 2 costs. However, several intervenors assert that the wildfire cost recovery mechanism proposed in the  
5 Amended Application still does not appropriately spread the risk of significant wildfire costs between  
6 the Utilities and their customers, and does not provide appropriate incentives for the Utilities to promote  
7 fire safety. As explained above, SDG&E and SoCalGas believe that these concerns are without merit.  
8 The WEBA mechanism described in the Amended Application achieves the goals of the ACR by putting  
9 the Utilities at substantial financial risk for wildfire costs, and by establishing a partnership between the  
10 Utilities and customer representatives for the development of future wildfire mitigation efforts and for  
11 wildfire insurance procurement. Nonetheless, SDG&E and SoCalGas are willing to shoulder even more  
12 shareholder risk in an effort to develop a simple and effective wildfire cost recovery mechanism that  
13 further overcomes the objections of core customer representatives.

14 SDG&E and SoCalGas still support the proposed WEBA mechanism in the Amended  
15 Application. But we recognize that the mechanism is somewhat complex -- an inevitable offshoot of the  
16 many months of negotiations and mediation sessions that ultimately led to the proposal. By contrast, our  
17 alternative WEBA proposal eliminates the complexity of Tier 1 and Tier 2, Categories A, B, and C, and  
18 WEBA categorization applications, and replaces these elements with a simple and straightforward  
19 proposition – 90/10 sharing of all wildfire costs and recoveries. No reasonableness review of wildfire  
20 costs or recoveries; no WEBA categorization applications; and no continuation of the inevitable clash  
21 between utility arguments for full recovery of wildfire costs and intervenor arguments for less than full  
22 recovery.

1 This approach is essentially the same as the 90/10 sharing of hazardous substance cleanup costs  
2 and related third party recoveries adopted by the Commission in D.94-05-020. This 90/10 sharing of  
3 hazwaste program costs and recoveries has worked well for over 17 years. SDG&E and SoCalGas  
4 believe it can work well for wildfire costs, too. Treating wildfire costs and recoveries in the same  
5 manner as hazwaste program costs and third party recoveries makes sense. As with wildfire costs,  
6 hazardous substance cleanup costs were the subject of much contention between utilities and customer  
7 representatives. Utilities asserted that they should be authorized to recover 100% of all hazardous  
8 substance cleanup costs because such costs were incurred as part of utility provision of service to  
9 customers; customer representatives contended that some or all hazardous substance cleanup costs  
10 should be disallowed because such costs would allegedly not have been incurred in the absence of utility  
11 fault; and the Commission questioned whether the traditional reasonableness review procedure was  
12 appropriate for recovery of hazwaste program expenses.<sup>40</sup> As explained in the hazwaste collaborative  
13 report developed by SDG&E, SoCalGas, DRA, TURN, SCE, PG&E, the California Environmental  
14 Protection Agency, and the United States Environmental Protection Agency:

15 The recommended mechanism recognizes the difficulty associated with  
16 determining the reasonableness of utility efforts to clean up hazardous  
17 substance contamination, utility actions that resulted in responsibility for that  
18 contamination, and utility efforts to secure proceeds from insurance carriers  
19 and other responsible parties. It also recognizes the difficulty associated with  
20 determining who should bear responsibility for cleanup costs – ratepayers or  
21 shareholders. Taking these considerations into account, the recommended  
22 mechanism provides utilities incentives to clean up contaminated sites in a

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<sup>40</sup> See D.94-05-020, mimeo., at 2 (referencing D.92-11-030).

1 cost-effective and timely manner and to pursue claims against insurers and  
2 other responsible parties, as appropriate.<sup>41</sup>

3 The situation faced by the utilities, interested parties, and the Commission with respect to  
4 hazardous substance cleanup costs is very similar to the situation we now face with wildfire costs and  
5 recoveries. In each case the costs have been incurred by utilities as part of their obligation to serve their  
6 customers; in each case customer representatives assert that utilities should not be able to recover costs  
7 when utility fault is involved; and in each case a recovery mechanism that allocates costs between  
8 customers and utilities on a 90/10 basis will provide the following benefits:

- 9 • Provide the Utilities a strong incentive to minimize the costs;
- 10 • Provide the Utilities a strong incentive to pursue recovery from insurance carriers and  
11 potentially responsible third parties, while at the same time providing a disincentive to  
12 pursue litigation where the litigation costs outweigh the expected returns;
- 13 • Allow the Utilities to recover to costs in a more timely manner;
- 14 • Provide the Utilities with a fair opportunity to recover their costs, depending on the  
15 quality of their management efforts; and
- 16 • Lessen the administrative burden on the Commission, intervenors, and Utilities  
17 associated with detailed oversight.<sup>42</sup>

18 The 90/10 approach to sharing hazardous waste cleanup costs and third party recoveries has  
19 worked for the Utilities, their customers, and the Commission for over 17 years. The same approach can  
20 work for the Utilities' wildfire costs and related recoveries as well.<sup>43</sup> This mechanism will provide the

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<sup>41</sup> November 19, 1993 Hazardous Substance Cleanup Cost Recovery Collaborative Report Submitted in Response to Decision No. 92-11-030, at pp. ES-I and ES-II.

<sup>42</sup> See D.94-05-020, mimeo., at 8-9.

<sup>43</sup> As explained above, the hazwaste mechanism has a somewhat complex mechanism for sharing insurance litigation costs and recoveries. This aspect of the hazwaste mechanism is designed to deal with issues specific to environmental insurance

1 financial certainty needed by the Utilities. At the same time, the new mechanism -- combined with the  
2 potential for penalties of the sort proposed for the Malibu canyon wildfire and recently imposed on  
3 PG&E for the Rancho Cordova explosion – will establish a framework that provides strong incentives  
4 for the Utilities to aggressively pursue fire safety.

5 This concludes my prepared rebuttal testimony.

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litigation. Accordingly, SDG&E and SoCalGas are simply proposing that wildfire-related insurance litigation costs and recoveries simply be shared 90/10 like wildfire costs and third party recoveries.

## ATTACHMENT A

### SDG&E/SOCALGAS ALTERNATIVE WILDFIRE COST RECOVERY MECHANISM

#### I. DEFINITIONS

- A. **Utility:** San Diego Gas & Electric Company (SDG&E) or Southern California Gas Company (SoCalGas).
- B. **Wildfire:** A large, destructive fire.
- C. **Wildfire Costs:** Wildfire Costs are Wildfire Claims Costs, Wildfire Litigation Costs, and Wildfire Financing Costs.
- a. **Wildfire Claims Costs:** Wildfire Claims Costs are payments by or on behalf of a Utility to persons or entities not funded through the Utility's base rates to satisfy claims relating to a Wildfire, including without limitation, damage claims by third parties and their insurers, and claims by governmental entities for the reimbursement of fire suppression costs, damages to environmental resources, and other governmental claims against the Utilities arising from a Wildfire. Wildfire Costs do not include costs that qualify for inclusion in a Utility's Catastrophic Event Memorandum Account (CEMA)
  - b. **Wildfire Litigation Costs:** Wildfire Litigation Costs are payments by or on behalf of a Utility to persons or entities not funded through the Utility's base rates, including without limitation, outside attorneys, consultants, and claims administrators, to pursue or defend claims relating to a Wildfire.
  - c. **Wildfire Financing Costs:** Unless otherwise authorized by the Commission, WEMA and WEBA balances will accrue interest at the 3-month commercial paper rate. The Utilities may present alternative financing proposals to the Commission for large WEBA balances via an application.
- D. **Wildfire Recovery:** A Wildfire Recovery is a payment received by a Utility relating to a Wildfire made in response to a claim asserted by the Utility. Wildfire Recoveries include payments from insurers of a Utility pursuant to a policy held by the Utility, as well as payments from other persons or entities. Wildfire Recoveries include amounts paid by a third party pursuant to a claim for indemnity or contribution and amounts paid to

plaintiffs in settlement or following judgment. Payments that must be returned by a Utility to its insurers pursuant to subrogation or other rights are not Wildfire Recoveries and shall not be recorded in WEMA or WEBA.

## **II. WILDFIRE COSTS AND RECOVERIES**

A. The Utilities shall continue to record in their Wildfire Expense Memorandum Accounts (WEMAs) established in 2010 pursuant to Resolution E-4311 all Wildfire Costs as they are paid and Wildfire Recoveries as they are received.

B. The Utilities shall each create a new Wildfire Expense Balancing Account (WEBA) to facilitate recovery of Wildfire Costs pursuant to the cost recovery mechanism described below. Once net Wildfire Costs for a given Wildfire reach \$10 million, a Utility may transfer the WEMA balance for that Wildfire to its WEBA. Thereafter, all costs and recoveries relating to that Wildfire shall be recorded by the Utility in its WEBA when paid and received, and all such costs and recoveries shall be subject to the WEBA cost recovery mechanism described below.

C. Inclusion of Wildfire Costs and Wildfire Recoveries in the WEBA cost recovery mechanism is voluntary. The Utilities may seek full recovery of Wildfire Costs not included in the WEBA mechanism through their GRCs, by application, or by any other procedure approved by the Commission.

D. The Utilities shall recover in rates 90% of all Wildfire Costs recorded in their WEBAs. The Utilities and their shareholders shall be responsible for the remaining 10% of these costs.

E. Ratepayers shall receive 90% of all Wildfire Recoveries recorded in the Utilities WEBAs. The Utilities and their shareholder shall retain the remaining 10% of these recoveries.

F. The new mechanism applies to all Wildfire Costs and Wildfire Recoveries that meet the criteria for inclusion in the Utilities' WEBAs described above, including costs from the 2007 Wildfires that SDG&E has been recording in its WEMA.

G. SDG&E shall credit its WEBA for any Wildfire Costs recovered through revenues authorized by FERC.

H. The Utilities shall credit their WEBA for any Wildfire Costs recovered through their Z-factor mechanisms.

### **III. NO REASONABLENESS REVIEW**

A. There shall be no reasonableness review of any of the Wildfire Costs or Wildfire Recoveries covered by this wildfire cost recovery mechanism.

### **VI. RATE RECOVERY**

A. WEBA balances shall be recovered by the Utilities in the subsequent proceeding or proceedings that each Utility deems appropriate.

B. Each Utility shall allocate and recover WEBA balances in rates in the same manner as liability insurance expenses.

### **V. GRC FORECASTS**

A. The Utilities shall exclude from their General Rate Case forecasts costs and recoveries relating to Wildfires with Wildfire Costs of more than \$10 million.

### **VI. WILDFIRE INSURANCE PREMIUMS**

A. The Utilities shall each create a Wildfire Insurance Premium Balancing Account (WIPBA) to record all increases or decreases from the amounts adopted in the utility's General Rate Case for insurance premiums attributable to coverage for Wildfire-related claims.

B. WIPBA balances should be consolidated and recovered annually, consistent with established procedures for the recovery of similar balancing accounts.

C. Amounts recorded to the WIPBA should be adjusted, as applicable, for costs capitalized to rate base, intercompany billings, and costs recovered through FERC-jurisdictional rates.

### **VI. NOTICES AND REPORTS**

A. The Utilities shall provide informational notices to the Commission's Energy Division within 15 days after costs reach \$10 million for any Wildfire.

B. The Utilities shall submit a WEBA annual report to the Commission's Energy Division for any calendar year in which they record Wildfire Costs or Wildfire

Recoveries in their respective WEBAs. This report shall list: (1) the names, dates, and locations of all relevant Wildfires; (2) the amount of Wildfire Costs and Wildfire Recoveries attributable to each such Wildfire during the calendar year; and (3) the total amount of Wildfire Costs paid and Wildfire Recoveries received during the calendar year. The report shall describe the Wildfire Costs and Wildfire Recoveries in enough detail to allow Energy Division to determine whether the costs and recoveries have been properly accounted for by the Utility, and whether reported Wildfire Costs are already being recovered in rates. The annual report shall also be served upon each of the parties to A.09-08-020.

## **VII. WILDFIRE INSURANCE PROCUREMENT CONSULTATIVE PROCESS**

A. The Utilities shall establish a wildfire insurance procurement consultative process so that customer representatives can better understand and provide input regarding wildfire insurance coverage levels and costs.

B. To facilitate stakeholder input consistent with the realities of the procurement of liability insurance, the Utilities shall meet with interested customer representatives at least two months prior to wildfire insurance renewal to review proposed procurement strategy, including current market conditions and the Utilities' insurance needs.

C. Within 30 days after each wildfire insurance renewal, the Utilities shall submit a report to the Commission's Energy Division describing the process and outcome of the wildfire insurance procurement effort.