Pacific Gas and Electric Company®

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January 3, 2022

Ms. Caroline Thomas Jacobs
Director, Office of Energy Infrastructure Safety
715 P Street, 20th Floor
Sacramento, California 95814

Re: Comments on Draft 2022 Executive Compensation Guidelines

Dear Ms. Thomas Jacobs:

Pacific Gas and Electric Company ("PG&E") respectfully submits the following comments on the Office of Energy Infrastructure Safety's ("OEIS") Draft 2022 Executive Compensation Guidelines (the "Draft Guidelines"). PG&E's executive compensation structure is an important component of its multi-faceted commitment to safety and operational excellence, and PG&E appreciates the opportunity to comment prior to OEIS's issuance of final guidelines.

PG&E generally supports the Draft Guidelines as consistent with the requirements of Assembly Bill ("AB") 1054. As set forth below, however, PG&E believes that certain limited aspects of the Draft Guidelines are problematic, and PG&E urges OEIS to refrain from adopting, or to modify, those aspects. PG&E also finds some portions to be ambiguous, and respectfully asks OEIS to clarify those portions before finalizing them.

A. Inclusion of Supplemental Retirement Benefits in the Definition of "Perquisites"

AB 1054 seeks to ensure that an electrical corporation's executive compensation program is "structured to promote safety as a priority and to ensure public safety and utility financial stability."[1] The statute accomplishes this in part by requiring that "a compensation structure for any new or amended contracts for executive officers" be "based on" certain "principles," including basing the "primary portion of the executive officers' compensation . . . on achievement of objective performance metrics," and basing "a significant portion of compensation . . . on the electrical corporation's long-term performance and value."[2] The statute's "primary portion" and "significant portion" principles arguably connote ratios, or fractions, but without specifying what should be included in the denominator.

The Draft Guidelines appropriately recognize that not everything that might be called "compensation" appropriately fits within the denominator. Page 43 contemplates using Total

[1] Pub. Util. Code § 8389(e)(4).

[2] *Id.* § 8389(e)(6)(A), (e)(6)(A)(i)(I), (e)(6)(A)(iii).

Direct Compensation ("TDC") as the denominator, and page 57 defines TDC as "Base Salary + Short-Term Incentive Program compensation + Long-Term Incentive Program compensation + Perquisite compensation." Notably, this excludes "Benefit Programs," which page 55 defines to include programs that "[p]rovide financial security in the case of death, disability, sickness, or retirement," as well as "severance pay, life insurance, and medical insurance."

PG&E agrees that it is appropriate—indeed, important—to exclude retirement and other benefit programs from the denominator when assessing compliance with the statute's "primary portion" and "significant portion" principles. There are many reason for this:

- Goals of AB 1054: Excluding such items is consistent with AB 1054's goal of ensuring that executive compensation programs appropriately promote safety and financial stability. It makes sense to focus that inquiry on executive officers' most direct and immediate compensation (base pay and incentive compensation), because that is the compensation that is designed to have the most significant tie to individual and company performance. That is also what employees and executive compensation professionals tend to regard as TDC.[3] It makes little sense, and would contravene common understandings of TDC, to include benefit programs whose monetary value is less determinable, or programs that provide deferred compensation for when the executive is retired and no longer able to influence the utility's operations.

- Recruitment and Retention: Not excluding retirement and other benefit programs would undercut the purpose of AB 1054 by making it harder to recruit and retain the talented executives that are necessary for operational excellence, and thus, for safety and financial stability. Not excluding such items from the denominator would make it mathematically harder to comply with the "primary portion" and "significant portion" principles, and would require either reducing base salaries (which would make it harder to recruit and retain), or increasing incentive compensation (which would turn AB 1054 on its head by giving utility executive officers the windfall of greater overall compensation). Notably, the California Public Utilities Commission ("CPUC") has emphasized that implementation of executive compensation requirements "should take into account PG&E's need to attract and retain highly qualified executive officers."[4] PG&E's Federal Monitor also recently observed that "it is important that PG&E's Board of Directors focus on hiring and retaining the right set of leaders to move PG&E forward," and that

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[3] *See, e.g.*, Economic Research Institute, Inc., *Glossary* (defining "Total Direct Compensation" as "total annual cash compensation plus the annualized value of long-term incentives"), *available at* https://www.erieri.com/glossary/term/total-direct-compensation; Society for Human Resource Management, *What Should Be Included in a Total Compensation Statement* ("Direct compensation can be defined as 'all compensation (base salary and/or incentive pay) that is paid directly to an employee.'"), *available at* https://www.shrm.org/resourcesandtools/tools-and-samples/hr-qa/pages/totalcompensationstatement.aspx.

[4] Decision Approving Reorganization Plan, D.20-05-053, at 89 (CPUC June 1, 2020).

"[n]o organization can sustain long-term progress if there is substantial turnover of senior leaders."[5]

- Uncertainties re Valuation: Excluding benefit programs potentially avoids difficult and amorphous questions. When calculating the value of perquisites provided on an annual basis (*e.g.*, health club memberships), valuation can be straightforward. When calculating the value of *deferred* compensation, valuation can be more complex, and difficult questions could be presented about how such valuations should factor into the "primary portion" and "significant portion" calculations.

Although PG&E supports the Draft Guidelines' exclusion of retirement and other benefit programs from TDC, for all the same reasons, PG&E opposes including supplemental retirement benefits in TDC (which the Draft Guidelines would do by defining "Perquisites" to include "supplemental retirement benefits," and defining TDC to include "Perquisite compensation").[6] Including supplemental retirement benefits would be inconsistent with the foregoing considerations, and as noted, would make it harder for a utility to comply with the "primary portion" and "significant portion" principles. This would make it even more challenging than it already is for California utilities to compete for the talent necessary to promote and maintain safety and financial stability.

Including supplemental retirement benefits in TDC by defining such benefits as "Perquisites" also would be inappropriate for additional reasons. Supplemental executive retirement plans spring in part from the fact that the tax laws impose inflexible dollar limits on contributions to certain types of retirement plans, including limits based on the amount of the employee's compensation.[7] This is despite the fact that standard financial planning guidance is that retirees should expect annually to spend not a fixed dollar amount in retirement, but a *percentage* of their "annual income while . . . still working."[8] Thus, without a supplemental plan, executive officers, who tend to be more highly paid than other employees, would suffer a comparative disadvantage in retirement. A supplemental plan thus is not a "perquisite" the way a health club membership or a personal car service is a perquisite; it is a form of deferred compensation to help ensure that executive officers are not penalized in retirement due solely to application of tax laws. Notably, the federal securities laws' proxy disclosure rules do not lump

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[5] Kirkland & Ellis LLP, *PG&E Independent Monitor Report of November 19, 2021*, at 17, 46 (filed in N.D. Cal. Case No. 3:14-CR-00175-WHA on Nov. 23, 2021 at ECF No. 1524-1).

[6] Draft Guidelines at 56-57.

[7] *See* 26 U.S.C. § 415.

[8] *E.g.*, Fidelity Brokerage Services, LLC, *How Much Will You Spend in Retirement?* (Sept. 24, 2021) ("Expect to spend 55%-80% of your current income annually in retirement."), *available at* https://www.fidelity.com/viewpoints/retirement/spending-in-retirement.

supplemental retirement plans into the category of "perquisites," but, to the contrary, expressly distinguish between the two.[9]

In sum, PG&E believes that the Draft Guidelines appropriately exclude retirement plans from TDC, but believes that that exclusion should extend to supplemental retirement plans.

B. Timing of Executive Compensation Approval Process

PG&E has concerns with the Draft Guidelines' timeline for the executive compensation approval process, which would have submissions on March 14, 2022, stakeholder comments 30 days later, reply comments 15 days after that, and an unstated period for review and decision. Specifically, PG&E is concerned that this schedule is likely to result in a decision not being rendered until roughly half the calendar year has gone by, which would represent half the performance period for annual incentive compensation offered under PG&E's Short-Term Incentive Plan ("STIP"). PG&E believes that if its STIP is to be effective in promoting safety and other priorities throughout the year, it must be settled *early* in the year—incentives that are not in place, that are in an uncertain holding pattern, or that might be revoked or modified many months after being implemented as a result of OEIS action would lose their incentive effect.

At the same time, however, PG&E appreciates that it is not feasible for utilities to make their submissions significantly earlier than March 14 due to the timing of compensation committee meetings, certification of performance results from the prior year, payment of incentive compensation awards for the prior year, submission (in PG&E's case) of a Tier 1 Advice Letter to the CPUC that reports on awards from the prior year,[10] preparation of proxy materials, and so forth. PG&E therefore makes two proposals. First, PG&E proposes tightening up the schedule slightly by having submissions on March 1, 2022, stakeholder comments 14 days later, and reply comments 10 days after that. Although that would not solve the problem, it would mitigate it. Second, PG&E proposes that if OEIS perceives problems with a utility's executive compensation structure, then, absent the most profound of deficiencies, OEIS address the issue only prospectively by including it in OEIS's guidance for the following year. That would avoid pulling the rug out from under a STIP midway through the performance period, and avoid undercutting or negating a utility's efforts to use a STIP to promote safety and other priorities.

C. Requests for Clarification

PG&E respectfully requests that OEIS clarify the following portions of the Draft Guidelines prior to finalization:

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[9] *Compare* 17 C.F.R. § 229.402(c)(1), (c)(2)(viii) (Instructions) (requiring disclosure of "[c]hange in pension value and non-qualified deferred compensation earnings," including under "each plan that provides for the payment of retirement benefits, . . . including but not limited to . . . supplemental executive retirement plans") *with id.* § 229.402(c)(1), (c)(2)(ix)(A) (requiring *separate* disclosure of "[a]ll other compensation," including "[p]erquisites and other personal benefits").

[10] *See* Decision Approving Reorganization Plan, D.20-05-053, at 88 (CPUC June 1, 2020) (requiring PG&E to provide "[a]nnual reporting of awards to the CPUC through a Tier 1 Advice Letter compliance filing").

Definition of "Executive Officer": The Draft Guidelines note that AB 1054 defines "executive officer" by incorporating the definition in Public Utilities Code § 451.5, which is: "any person who performs policy making functions and is employed by the public utility subject to the approval of the board of directors, and includes the president, secretary, treasurer, and any vice president in charge of a principal business unit, division, or function of the public utility." The Draft Guidelines appear to recognize that "policy making functions" and "approval of the board of directors" are irreducible requirements of this definition, and that the specifically enumerated positions, such as the corporate secretary and treasurer, would not qualify if, in the circumstances, such positions do not involve "policy making functions" or such individuals' employment is not subject to board approval.[11] PG&E agrees with this, for reasons previously explained by Southern California Edison Company ("SCE").[12] PG&E notes, however, that some of the relevant text in the Draft Guidelines appears in a hypothetical table, and PG&E believes it would be helpful to the California utilities if OEIS clarified more explicitly that the secretary and treasurer only qualify as "executive officers" if they perform policy making functions and if their employment is subject to board approval.

Metric Categorizations: The Draft Guidelines ask utilities to place performance metrics into specified categories and sub-categories. PG&E appreciates that this can be useful, but as with any categorization effort, it may have the unintended effect of eliding nuances and skewing analyses. Some metrics defy simplistic categorization, in that they appropriately fit into more than one category. But if a metric that crosses categories has to be shunted into only one category, there is a risk it would not be "counted" when assessing compliance with AB 1054's various requirements. For example, if a metric that promotes both customer service and safety were placed solely in the "Customer Service" category, there is a risk it would not be counted when assessing compliance with the requirement that an executive compensation program be "structured to promote safety."[13]

PG&E does not advocate doing away with categories. PG&E instead urges OEIS to clarify that, notwithstanding categorizations, OEIS will look to the substance of the metrics, and the manner in which they operate, in determining whether a utility's executive compensation structure complies with AB 1054.

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[11] *See* Draft Guidelines at 15 (noting that it may be appropriate to "exclude[] the Secretary [if] this individual does not perform policy making functions and is not subject to approval of the board of directors").

[12] *See* October 15, 2021 Letter from SCE to OEIS ("The three positions listed in Pub. Util. Code 451.5 reflect repealed corporate law provisions that previously required California corporations to have as officers at least a president, a secretary, a treasurer, and a vice president. With only four officer positions, each one would have a policy-making function. . . . Secretary and Treasurer . . . officers who do not have policy-making functions . . . are not executive officers for purposes of Pub. Util. Codes 451.5 or 8983(e) . . . . Secretary and Treasurer [positions] are also not executive officers [if] they are not employed by the public utility subject to the approval of the board of directors.") (internal quotation marks, citations, and footnotes omitted).

[13] Pub. Util. Code § 8389(e)(4).

Submission of Historical Data: The Draft Guidelines would require utilities to populate charts (Tables 3f.1 and 4e.1) with several years of historical metric performance data. PG&E has concerns with this broad requirement because (among other reasons PG&E previously has expressed),[14] although PG&E strives to use the best data available for purposes of assessing metric performance, it can take time for the data to be audited. PG&E is concerned that including both audited and unaudited data could be confusing and otherwise problematic. PG&E therefore urges OEIS to include separate charts for audited and unaudited data (with no requirement to submit unaudited data where audited data is available).

Reporting of LTIP Information: PG&E finds several portions of the Draft Guidelines to be ambiguous when it comes to performance shares awarded under a Long-Term Incentive Plan ("LTIP"). PG&E generally distinguishes between *awards* or *grants* on the one hand, and *payouts* on the other hand. The Draft Guidelines, however, seem to conflate the two concepts, which may cause confusion.

PG&E conceives of awards or grants as awards in a particular calendar year at a target level, which may or may not be paid, or may be paid to a variable extent, depending on performance over a three-year period that spans the year of the grant plus the following two years. In other words, PG&E thinks of awards or grants of performance shares as an *opportunity* for the employee to receive the shares after the end of the performance period, depending on performance. PG&E conceives of payouts, by contrast, as the payment of performance shares after the three-year performance period is complete and metric performance results are certified—at which point the employee is able to monetize the award. To illustrate, PG&E made LTIP performance share awards at a target level in 2021 with a three-year performance period of 2021 through 2023. The PG&E Corporation People and Compensation Committee will certify the performance results in early 2024, and payouts of 2021 performance share awards will be made (as applicable) in 2024.

The Draft Guidelines seem to conflate grants with payouts in the following respects:

- Page 31 asks whether "the 2021 LTIP payouts [were] determined based on a performance range." In context, page 31 seems to be asking about LTIP awards made in 2021 (not LTIP awards made in 2018 and paid out in 2021), and if that is correct, then the question is unclear because there will be no "2021 LTIP payouts" at PG&E until 2024.

- Page 31, under the heading "2021 and 2022 LTIP Grants," asks about "Grant Value as a % of TIC" and "Earned Value as a % of TIC" for each of 2021 and 2022. Page 55 defines "Earned Value" as "[v]alue at the date of vesting." PG&E finds the question to be unclear because the "Earned Value" of 2021 and 2022

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[14] *See* October 15, 2021 Letter from PG&E to OEIS at 12-13 (commenting on OEIS's September 29, 2021 workshop, and explaining that submitting historical data would go beyond what AB 1054 contemplates, would be of limited usefulness, and would potentially result in erroneous conclusions).

performance share grants will not be determinable until such grants vest in 2024 and 2025, respectively.[15]

- Page 31 also uses the term "2021 Performance Year" and "2022 Performance Year." PG&E does not understand these terms in the context of LTIP performance share awards. As noted, PG&E's LTIP program design for performance shares uses a three-year performance period, not a one-year period.

- All of the foregoing issues also appear in Table 7a.1 on page 48.

PG&E respectfully requests that OEIS clarify the foregoing prior to issuing final guidance for 2022.

Reporting of "STIP Changes": Page 27 of the Draft Guidelines has a Section 3e, which is entitled "*Significant* STIP Changes" (emphasis added). The instructions on this page, by contrast, ask about "*any* changes between 2021 and 2022 in terms of STIP eligibility, structure, modifiers, metrics . . . , weightings, definitions, etc." (emphasis added). PG&E therefore is unsure whether the Draft Guidelines are asking utilities to identify only "significant" changes, or instead "any" changes. PG&E requests that OEIS clarify that only "significant" changes need be described, because describing "any" changes could be burdensome on utilities. It also could inundate OEIS with minutiae that OEIS would not find useful in fulfilling its statutory mandate to determine whether an overall executive compensation "structure meets the principles set forth in [AB 1054]."[16]

Definitions of "Incentive Compensation" and "Incentive-Based Compensation": Page 55 defines two very similar terms—"Incentive Compensation" and "Incentive-Based Compensation"—differently, which is inherently confusing. Moreover, although the definitions sound similar on their face, they could be quite different as applied. For example, RSUs that are awarded under an LTIP based on service would seem to qualify as "Incentive Compensation," because "Incentive Compensation" is defined to include all LTIP compensation. It is less clear whether RSUs awarded based on service would qualify as "Incentive-Based Compensation," which is defined to include only "[c]ompensation awarded based on meeting performance metrics that are measurable and enforceable."[17] PG&E recommends clarifying these definitions.

2021 vs. 2022 Data: Page 17 asks for certain 2021 data under the heading, "Use of a Performance Range – 2021." Page 18 asks for exactly the same 2021 data, but under the heading, "Use of a Performance Range – 2022." The second references to 2021 appear to be typographical errors that OEIS may wish to correct prior to finalization.

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[15] Other forms of long-term incentive compensation, such as restricted stock units ("RSUs") based on service, may vest incrementally over time. PG&E does not currently use RSUs as a form of long-term incentive compensation for executive officers.

[16] Pub. Util. Code § 8389(e)(6)(B).

[17] PG&E believes that RSUs would qualify as "Incentive-Based Compensation" because their value depends on the performance of the underlying stock, which is objective and measurable.

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PG&E's executive compensation structure is an important part of its commitment to safety, to its customers, and to having the best executive team possible to deliver for PG&E's stakeholders and the communities it serves. PG&E thanks OEIS for allowing PG&E an opportunity to comment on the Draft Guidelines prior to finalization. If PG&E can provide further information, please do not hesitate to contact me.

Sincerely,

/s/ Lisa Laanisto

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