

BVES Comments Regarding Initial Proposals for 2022 and 2023 Executive Compensation Guidelines Docket No. 2022-EC

In a Notice of Staff Workshop, the Office of Energy Infrastructure Safety (“Energy Safety”) indicated that it intends to update 2022 and 2023 executive compensation guidelines through a public process. The noticed workshop, held on September 29, 2021, is the start of that public process. These comments are submitted in accordance with the Notice, which stated that written feedback regarding the workshop would be accepted through October 15, 2021.

The Presentation Agenda indicated that Energy Safety intended to address the issue of the definition of the term “contract” as used in Public Utilities Code §8389(e)(6)(A), as well as the following potential changes to the guidelines:

- Who is included in the executive compensation structure?
- What qualifies as a “primary portion” and pay for performance?
- Increasing long-term compensation transparency.
- How much indirect and ancillary compensation occurs?

The following Bear Valley Electric Service, Inc.’s (“BVES” or “Bear Valley”) comments, which are preliminary, will focus primarily upon the issues of the definition of the term “contract” and what qualifies as a primary portion of pay related to performance. BVES reserves the right to expand, modify or amend its comments if or when Energy Safety formally issues proposed revisions to the 2022 or 2023 executive compensation guidelines.

Energy Safety’s Position That All Employees Have a Contract with Their Employer Is Contrary to California Law.

Slide #5 of material used by Energy Safety at the September 20 Workshop regarding the definition of “contract” in Section 8389(e)(6)(A)¹ includes several footnotes. In footnote #2, Energy Safety claims: “All employees have a contract with their employer.” In footnote #4 of that slide, Energy Safety asserts:

As noted, every employee has a contract with their employer, so every new employee represents a new contract. If you change the terms and conditions of employment for any employee you have amended a contract.

¹ All statutory references are to the California Public Utilities Code, except as otherwise provided.

And finally, in footnote #5, Energy Safety concludes:

Bottom line: Section 8389(e)(6) applies to every new or amended contract for any executive officer. Section 8389(e)(6)(A) is not limited to contracts with certain termination, compensation, or other employment conditions.

At its core, it appears that Energy Safety is taking the legal position that all employees have a contract with their employer in order to effectuate and impose the requirements of Section 8389(e)(6)(A) on all utilities. Although Energy Safety cites several statutes, it is unclear how those statutes support its position that all employees have a contract with their employer. Indeed, Energy Safety's position is contrary to well-established California labor law.

Under California Labor Code Section 2922, all employment in the state is presumed to be "at will" unless the parties agree otherwise or an exception to at-will employment applies. It states, in relevant part: "An employment, having no specified term, may be terminated at the will of either party on notice to the other." Claiming that all employees have a contract with their employer is contrary to the provisions of Labor Code Section 2922 and the antithesis of "at will" employment.

BVES President Has No Employment Contract and Is an "At Will" Employee.

The President of BVES is currently the only position covered by Bear Valley's executive compensation plan. In a written offer outlining the terms and conditions of employment for the current President of BVES, the offering document provides:

No employment contract is created or implied. Employees of the Company are employed on an "at will" basis, and the relationship may be terminated by either the Company or you at any time with or without notice and with or without cause.

The offering document clearly states there is no employment contract, express or implied, with regard to the position of President, and that the President is an "at will" employee. Even if Energy Safety's position was that California law creates a *presumption* that all employees have an employment contract with their employer (which is not the law, nor the apparent position of Energy Safety), the existence of a signed document between Bear Valley and its President stating there is no employment contract, express or implied, and he is an "at will" employee would overcome any such presumption.

The facts clearly establish that BVES has no executive employment contracts. Therefore, the requirements of Section 8389(e)(6)(A) are not applicable to Bear Valley's executive compensation plan.

Energy Safety’s Interpretation of Section 8389(e)(6)(A) Regarding Contracts Is Contrary to the Rules of Statutory Interpretation.

One of the rules of statutory interpretation is that significance should be attributed to every word and phrase of a statute, and a construction making some words surplusage should be avoided.² A corollary to that rule is that, generally, if the Legislature chose to include language, it must be given some meaning. Laws should be interpreted to avoid rendering some words surplusage, null or absurd.³

In addition, words in a statute should be given their plain and common sense meaning.⁴ In the context of executive compensation, use of the term “contract” would logically mean an *employment* contract. To interpret it to mean some other type of contract would be contrary to a common sense meaning when used in the context of a statute dealing with executive compensation.

Section 8389(e)(6) provides, in relevant part,

[Energy Safety] shall issue a safety certification to an electrical corporation if the electrical corporation provides documentation . . . [that] the electrical corporation has established a compensation structure **for any new or amended contracts** for executive officers, as defined in Section 451.5, that is based upon the following principles: . . . (bolded added)

Energy Safety’s claim that all employees have contracts with their employers would, in effect, render the “for any new or amended contracts” language in Section 8389(e)(6)(A) null and surplusage. Such a result is contrary to rules of statutory interpretation. The bolded language is *limiting* language to the applicability of Section 8389(e)(6)(A). An interpretation effectively eliminating such language broadens the applicability of that statute well beyond that which was intended by the Legislature.

As statutory construction rules require, the phrase “for any new or amended contracts” must be given some meaning. It cannot simply be ignored. If properly read, it *limits* the requirement of a particular compensation structure to only those circumstances where executive officers have new or amended employment contracts with the electrical corporation. Energy Safety’s unsupported claim that *all* employees (which would include executive officers as defined in Section 451.5) have an employment contract with their employers (electrical

² *People v. Woodhead*, 43 Cal.3d 1002, 1010; *Moyer v. Workmen’s Comp. Appeals Bd.*, 10 Cal.3d 222, 230.

³ *Ingredient Communications Council, Inc. v. Lungren*, 2 Cal App.4th 1480, 1492.

⁴ *Mercer v. Dept. of Motor Vehicles*, 53 Cal. 3d 753, 763.

corporations) would render the limiting language meaningless and surplusage, which is contrary to the rules of statutory construction.

If the Legislature had intended to require electrical corporations to establish a compensation structure that applied to *all* executive officers, it would not have added the modifying and limiting language “for any new or amended contract” in front of the phrase “for executive officers, as defined in Section 451.5.” It would simply have not included such language at all. But it did include such modifying and limiting language, and it is improper statutory construction to simply read out the phrase “for any new or amended contract” as if it does not exist.

In summary, Energy Safety is without authority, and would be in violation of the law, to attempt to require BVES to comply with Section 8389(e)(6)(A). The Legislature expressly limited the law’s application to only those circumstances where an employment contract exists between the electrical corporation and its Section 451.5 executive officers. No such employment contract exists with Bear Valley’s President. Therefore, Section 8389(e)(6)(A) is not applicable to BVES.

Notwithstanding that the provisions of Section 8389(e)(6)(A) are not applicable to BVES, BVES voluntarily commits that its future executive compensation plans will continue to comply with Section 8389(e)(6)(A) requirements in a manner generally consistent with the 2021 plan approved by Energy Safety.

Bear Valley Is Fundamentally Different Than the Large California Utilities

Bear Valley appreciates Energy Safety’s efforts to standardize the requirements of executive compensation plans. Similar utilities should be treated similarly. However, where utilities are materially different, rigid interpretations and unyielding allegiance to uniformity can lead to counterproductive results.

BVES is materially different than the three large investor-owned electric utilities in California. It currently has only 45 employees and approximately 24,500 customers, with annual revenues of approximately \$40 Million. In comparison, Southern California Edison Company has approximately 12,700 employees, with over 5 million customers and annual revenues of approximately \$13.5 Billion. Relatively speaking, BVES has approximately 0.4% of Edison’s workforce, approximately 0.5% of its customer base and approximately 0.3% of its annual revenues. The comparison of annual revenues is important because annual revenues of a

corporation play a key role in identifying peer group companies in studies comparing top executives' total compensation. As can be seen by these numbers, Bear Valley's financial picture is starkly different than Southern California Edison's, as well as the other two large electric utilities whose annual revenues are also in the multi-billion dollar range.

BVES is the only small electric IOU in the state to apply for a Safety Certificate under the provisions of Section 8389. Accordingly, BVES is the only small electric utility in the state that must seek approval of Energy Safety for Bear Valley's executive compensation plan under the provisions of Section 8389.

The provision in Section 8389(e)(6)(A)(i)(I) requiring the primary portion of executive total compensation to be based upon achieving objective performance metrics is extremely difficult for a very small utility to comply with and still attract and retain competent executives that are incentivized to provide safe, reliable and cost-effective service to its customers. BVES and its customers must be allowed to have an executive compensation package that is structured and sized competitively with similarly-sized corporations. BVES should not be required to needlessly pay its executives more than the market requires when there are interpretations of statutory provisions which would avoid such an indefensible result.

In the workshop presentations, there were no corporations the size of BVES that were included in the so-called peer group used for comparisons. BVES is very concerned that its fundamentally different circumstances, when compared with the three large California investor-owned electric utilities, are simply being ignored. These very substantial differences must not be swept under the rug. They warrant recognition and reasonable accommodation to realize important Legislative objectives without harming the utility and its customers.

Large Utility Executive Compensation Is, and Should Be, Materially Different Than BVES Executive Compensation

BVES recognizes that there is, and should be, a very substantial difference in total compensation paid to top executives of very large IOUs as compared to BVES executives. With compensation packages that have much higher total compensation, executives of the large IOUs may still receive a very substantial, and attractive, base salary while having a compensation package that still allocates the primary portion of total direct compensation to achieving objective performance metrics.

For example, a compensation package totaling in excess of \$2,000,000 of compensation could provide an executive with a very attractive base salary of up to \$1,000,000 and still be

compliant with Section 8389. In contrast, if Bear Valley's executive's overall annual compensation is less than \$400,000, then the requirements in Section 8389 would limit the base salary to under \$200,000. Bear Valley is very concerned that such a relatively modest base salary for the President would not allow BVES to retain and recruit highly-competent, motivated utility executives. BVES needs such executives to not only help to ensure that BVES is operated safely and efficiently, but also to lead its efforts to develop and implement complex programs to reduce wildfire risks for the benefit of the state, BVES and its customers.

Requiring Bear Valley's Executive Plan to Meet Section 8389(e)(6) Requirements Based Upon Threshold Pay Could Seriously Undermine Bear Valley's Ability to Retain and Recruit Highly Competent and Motivated Executives

Similar to other executive compensation plans, Bear Valley's plan has three levels of performance metrics and corresponding compensation – Threshold, Target and Maximum. Bear Valley's 2021 approved executive compensation plan is based upon using metrics and compensation at the Target level.

Based on comments at the September workshop, BVES understands that Energy Safety is considering a potential change in how it will determine compliance with the requirement of Section 8389(e)(6)(A)(i)(I). Energy Safety proposes that the primary portion of an executive officer's compensation be based upon achievement of objective performance metrics at the Threshold level, rather than the Target level. If this potential change is adopted and applied to BVES, it would likely require yet another reduction in the base pay for Bear Valley's President. The potential reduction in base pay could be as much as 50% given the current payout for performance metrics at Threshold level compared to Target level. It is not hyperbole to state that yet another reduction in the President's base pay will further undermine Bear Valley's ability to retain and recruit highly competent and motivated executives to the position of President. Energy Safety must avoid such a counterproductive result.

In Bear Valley's initial, January 15, 2021, filing of its 2021 Executive Compensation Plan, Bear Valley submitted a Plan that resulted in base pay being 66.7% of total compensation at Target performance level, with performance-based compensation comprising 33.3% of total compensation. After stating that it had no new or amended contract with its executive officers, Bear Valley noted that Section 8389(e)(6)(A) was not applicable to it. Nevertheless, Bear Valley's Plan voluntarily satisfied many of the principles set forth in that statute. In an April 14,

2021 Action Statement, Energy Safety denied Bear Valley's submission, concluding that the Plan did not meet the requirements of Section 8389(e)(6)(A)(1).

Bear Valley submitted a revised Plan dated May 24, 2021. In its revised Plan, Bear Valley again stated that because it has no new or amended contracts with its executive officers, it was not statutorily required to adopt the principles set forth in Section 8389(e)(6)(A). However, BVES stated it was revising its Plan in order to comply with Energy Safety's Action Statement.

To meet the requirements of Section 8389(e)(6)(A), it was necessary for BVES to significantly restructure its Plan, placing substantially more of the President's pay at risk. It ultimately was necessary for BVES to reduce its President's base pay. Those changes, and in particular the reduction in base pay, increased the risk of the loss of Bear Valley's current President. If that should happen, the revised Plan with reduced base pay would likely undermine Bear Valley's ability to replace him with an equally competent and motivated executive. Such a result would not be in the best interests of the state, BVES or its customers.

To Support Bear Valley's Ability to Retain and Recruit Highly Competent and Motivated Executives, Compensation Guidelines Must Recognize, and Accommodate, Bear Valley's Unique Circumstances

As indicated in Section 8389(e)(6), the executive incentive compensation structure is intended to promote safety as a priority and to ensure public safety. If Bear Valley's President is not highly competent and motivated, it undermines Bear Valley's ability to promote safety as a priority and to help ensure public safety by effectively, timely and efficiently implementing its wildfire mitigation plans and other crucial safety programs. Such a result would clearly be contrary to the Legislature's intent in crafting Section 8389.

It is not uncommon for the California Public Utilities Commission to effectively implement broad statutory requirements in a manner that recognizes and accommodates the material differences between large utilities and small utilities. Bear Valley urges Energy Safety to follow a similar course of action. The provisions of Section 8389 are sufficiently broad for Energy Safety to craft guidance for executive compensation plans that recognizes and accommodates Bear Valley's materially different circumstances while still achieving the Legislature's intent. Failing to do so poses real-world risks for Bear Valley's ability to retain and recruit highly competent and motivated executives. Such a result serves no one's best interests.