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Subject: Office of Energy Infrastructure Safety Approval of Pacific Gas and Electric Company's 2021 Executive Compensation Structure Pursuant to Public Utilities Code Sections 8389(e)(4) and (e)(6)

Ms. Laanisto:

This letter approves Pacific Gas and Electric Company's (PG&E) 2021 executive compensation structure. The Office of Energy Infrastructure Safety (Energy Safety) finds that PG&E's executive compensation structure minimally satisfies the requirements of Public Utilities Code sections 8389(e)(4) and (e)(6).

Background

Public Utilities Code section 8389(e)(4) requires an electrical corporation's executive compensation structure be approved by the California Public Utilities Commission's (CPUC) Wildfire Safety Division (WSD)[1] and "structured to promote safety as a priority and to ensure public safety and utility financial stability with performance metrics, including incentive compensation based on meeting performance metrics that are measurable and enforceable, for all executive officers, as defined in [Public Utilities Code] Section 451.5."

Public Utilities Code section 8389(e)(6)(A) further requires:

> The electrical corporation has established a compensation structure for any new or amended contracts for executive officers, as defined in [Public Utilities Code] Section 451.5, that is based on the following principles:
> (i) (I) Strict limits on guaranteed cash compensation, with the primary portion of the executive officers' compensation based on achievement of objective

[1] On July 1, 2021, the WSD transitioned to the Office of Energy Infrastructure Safety (Energy Safety), a new department under the California Natural Resources Agency. In accordance with Public Utilities Code section 326, all functions of the WSD are transferred to Energy Safety.

performance metrics.

(II) No guaranteed monetary incentives in the compensation structure.

(ii) It satisfies the principles identified in [Public Utilities Code section 8389(e)(4)].

(iii) A long-term structure that provides a significant portion of compensation, which may take the form of grants of the electrical corporation's stock, based on the electrical corporation's long-term performance and value. This compensation shall be held or deferred for a period of at least three years.

(iv) Minimization or elimination of indirect or ancillary compensation that is not aligned with shareholder and taxpayer interest in the electrical corporation.

In addition to the requirements set forth in Public Utilities Code sections 8389(e)(4) and (e)(6), the December 22, 2020 guidance letter issued by the WSD required an electrical corporation seeking approval of its 2021 executive compensation structure to submit the following information:[2]

- An explanation of executive compensation components, including base pay, annual bonus/incentive information, and long-term incentive pay, including percentages of overall compensation for each component.
- A description of all metrics, including safety metrics, used to calculate incentive compensation, including an explanation of whether safety metrics are outcome or input based (e.g., number of ignitions versus number of miles of distribution lines inspected).
- A breakdown of the percentage of executive compensation based on safety metrics versus other metrics (e.g., financial performance).
- A description of how safety performance is calculated for incentive compensation.
- Examples of incentive compensation reduced or withheld in the last five years as a result of failure to meet safety metrics.

Related to the above requirements, CPUC Decision 20-05-053 required Pacific Gas and Electric Company (PG&E) to comply with the requirements of Assigned Commissioner Ruling (ACR) Executive Compensation Proposal 9.[3]

The December 22, 2020 WSD guidance letter directed electrical corporations seeking a Safety Certification for 2021 to submit a formal request for approval of its executive

[2] WSD Executive Compensation Submission Guidance Letter, page 2. https://energysafety.ca.gov/wp-content/uploads/docs/misc/wsd/wsd-executive-compensation-guidance-20201222.pdf.

[3] Investigation 19-09-016, Assigned Commissioner Ruling and Proposals, February 18, 2020: https://docs.cpuc.ca.gov/PublishedDocs/Efile/G000/M327/K303/327303409.PDF.

compensation structure by January 15, 2021. PG&E submitted a request for approval of its 2021 executive compensation structure on January 15, 2021.[4]

On January 29, 2021, the Public Advocates Office at the California Public Utilities Commission (Cal Advocates) and The Utility Reform Network (TURN) submitted comments on PG&E's and other electrical corporations' 2021 executive compensation structures.[5] On February 5, 2021, PG&E submitted a reply comment.

On March 2, 2021 PG&E submitted a supplement to its January 29th submission.[6] PG&E outlined some structural changes in its executive compensation program and provided milestones for all except two performance metrics.

On April 30, 2021 Cal Advocates submitted updated comments on PG&E's and other electrical corporations' 2021 executive compensation structures.[7]

On June 4, 2021 PG&E submitted a second supplement to its January 29th submission.[8] This update replaced the "Reportable Fire Ignitions" metric with a "Wildfire Risk Reduction" metric.

On June 25, 2021 Cal Advocates and TURN submitted comments on PG&E's second supplement to its January 29th submission. On July 2, 2021 PG&E submitted a reply comment.

Discussion

PG&E's executive compensation structure has three components: 1) base pay plus benefits, 2) Short Term Incentive Pay (STIP), and 3) Long Term Incentive Pay (LTIP). These components provide an average of 41.6% of total compensation at the target level for base pay, 18.2% for STIP and 40.2% for LTIP. These compensation components vary depending on the executive position.

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[4] PG&E January 15, 2021 letter:
https://energysafety.ca.gov/wp-content/uploads/docs/misc/wsd/pge-executive-compensation-2021.pdf.

[5] Cal Advocates January 29, 2021 letter:
https://energysafety.ca.gov/wp-content/uploads/docs/misc/wsd/public-advocates-office-comments-on-2021-executive-compensation-plans.pdf;
and TURN January 29, 2021 letter:
https://energysafety.ca.gov/wp-content/uploads/docs/misc/wsd/turn-comments-on-executive-compensation-20210129.pdf.

[6] PG&E March 2, 2021 letter:
https://energysafety.ca.gov/wp-content/uploads/docs/misc/wsd/pge-supplemental-executive-compensation-submission-to-wsd.pdf

[7] Cal Advocates April 30, 2021 letter:
https://energysafety.ca.gov/wp-content/uploads/docs/misc/wsd/comments-of-the-public-advocates-office-on-supplemental-submissions.pdf

[8] PG&E June 4, 2021 letter:
https://energysafety.ca.gov/wp-content/uploads/docs/misc/wsd/pge-second-supp.-exec.-comp.-submission-to-wsd.pdf

An average of 58.4% of executive pay is based on the achievement of performance metrics (STIP and LTIP) for all executive positions. Therefore, PG&E's executive compensation structure meets the requirements of Public Utilities Code section 8389(e)(6)(A)(i)(I), with the primary portion of the executive officers' compensation based on achievement of objective performance metrics.

PG&E's executive structure meets Public Utilities Code section 8389(e)(6)(A)(i)(II) since there is no guaranteed monetary compensation in the performance portion of the executive compensation package. PG&E's performance metrics are structured with a "threshold," "target" and "maximum" scaled compensation; with commensurate 50%, 100% and 200% adjustments to the rewards. Failing to achieve the threshold for a STIP or LTIP metric results in no payout for that metric.

The proposed executive compensation structure appears to satisfy the principles outlined in Public Utilities Code section 8389(e)(4) and the requirements outlined in Public Utilities Code section 8389(e)(6)(A)(iii) and (iv). The metrics used in the STIP and LTIP performance compensation portions of PG&E's executive compensation plan are relevant to PG&E's top risks as identified by the Enterprise and Operational Risk Management program. The STIP is awarded on a yearly basis and includes ten metrics that are safety-related and constitute 60% of the potential reward; another 15% of the reward is based on four customer service and reliability performance metrics with the final 25% based on a single financial metric. Many of the STIP metrics are similar, if not identical, to executive compensation metrics approved by the CPUC in Decision 20-05-053.[9] The LTIP compensation is awarded annually but not granted for at least three years after being awarded. It is important to note that unlike all other 2021 executive compensation plans submitted to Energy Safety, PG&E's longer-term compensation is not based entirely on a financial metric(s). Two equally weighted input-based public safety metrics constitute 35% of LTIP compensation; two equally weighted customer-service related metrics comprise another 35%, and the final 30% is awarded based on two equally weighted financial metrics. Additionally, PG&E stated in their January 15, 2021 submission that executives receive "de minimis" perquisites, such as parking and health club memberships, that are included to improve recruiting and retention and are therefore aligned with shareholder and stakeholder interests.[10]

Finally, CPUC Decision 20-05-053 required PG&E to comply with the requirements of Assigned Commissioner Ruling Executive Compensation Proposal 9. The January 15, 2021 executive compensation structure submitted by PG&E included an item-by-item

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[9] Investigation 19-09-016: Order Instituting Investigation on the Commission's Own Motion to Consider the Ratemaking and Other Implications of a Proposed Plan for Resolution of Voluntary Case filed by Pacific Gas and Electric Company, pursuant to Chapter 11 of the Bankruptcy Code, in the United States Bankruptcy Court, Northern District of California, San Francisco Division, In re Pacific Gas and Electric Corporation and Pacific Gas and Electric Company, Case No. 19-30088.

[10] Energy Safety addressed the topic of indirect and ancillary executive compensation at the September 29, 2021 Executive Compensation Workshop, and we are considering potential changes to the 2022 Executive Compensation Guidelines that will clarify the required reporting of indirect and ancillary compensation.

discussion of how PG&E's proposed executive compensation plan meets those requirements.[11]

Stakeholder comments

PG&E's January 15, 2021 executive compensation structure submission had no performance metric milestones. In its January 29, 2021 comments TURN expressed concern that PG&E's executive compensation plan had not "calibrated its metrics milestones to properly incentivize improved safety performance."[12] This is similar to a criticism levied by Cal Advocates in its April 30, 2021 comments after PG&E had updated its submission to include performance metric milestones.

Cal Advocates April 30, 2021 comments included two suggestions applicable to all utilities. First, Cal Advocates recommended WSD require the utilities provide historical data underlying their metrics and targets. Second, Cal Advocates recommended WSD require all utilities to provide an explanation of the derivation for each minimum, target, and maximum metric goals. Both recommendations are noteworthy, and Energy Safety will consider them further in the development of future guidelines.

In its April 30, 2021 comments Cal Advocates commented specifically on PG&E's March supplemental executive compensation plan. Cal Advocates recommended that WSD should require PG&E establish concrete milestones for all metrics prior to approving its executive compensation plan.

In its March 2021 supplement, PG&E provided "threshold," "target" and "maximum" performance milestones for all metrics except for Reportable Fire Ignitions and Non-Generally Accepted Accounting Principles (GAAP) Core Earnings Per Share. However, for the Non-GAAP Core Earnings Per Share STIP metric, PG&E did establish a range for the milestones, effectively providing the "threshold" and "maximum" performance levels. Energy Safety assesses this as sufficient to meet the requirement of a target metric.

In its April 30, 2021 comments Cal Advocates recommended that Energy Safety should require PG&E to 1) justify how maximum safety performance milestones represent significant improvements to public safety, and, 2) ensure that its performance metric milestones promote improvement and excellence. Both of these comments are noteworthy and Energy Safety will consider them further in the development of future guidelines.

The June 4, 2021 PG&E supplement replaced the Reportable Fire Ignitions (RFI) metric with a Wildfire Risk Reduction (WRR) metric that specified milestone targets. In its June

[11] PG&E January 15, 2021 letter pages 15-19: https://energysafety.ca.gov/wp-content/uploads/docs/misc/wsd/pge-executive-compensation-2021.pdf.

[12] The Utility Reform Network letter pages 5-6: https://energysafety.ca.gov/wp-content/uploads/docs/misc/wsd/turn-comments-on-executive-compensation-20210129.pdf.

25th comments Cal Advocates and TURN expressed conflicting views of the new WRR metric. Cal Advocates opposes the new metric and supports returning to the RFI metric while TURN is supportive of the new WRR metric, with the caveat of increasing the stringency of the metric's goals.

The RFI metric consists of all powerline-involved fire incidents in High Fire Threat Districts (HFTDs) annually reportable to the CPUC per Decision 14-02-015. The WRR metric consists of all powerline-involved ignitions that result in 100 acre or greater fires in HFTDs that are annually reportable to the CPUC per Decision 14-02-015. In essence the WRR metric is a subset of the RFI set of incidents, which in turn is a subset of all powerline-involved fire incidents. The WRR is clearly an important wildfire and public safety indicator. However, an RFI reportable fire that is not an WRR reportable fire also represents an important wildfire and public safety indicator. In essence RFI reportable fires are the necessary precursors to WRR reportable fires. It is recommended that PG&E considers using both metrics in future executive compensation structure submissions.

Conclusion

Energy Safety finds that PG&E has met the minimum requirements set forth in Public Utilities Code sections 8389(e)(4) and (e)(6), and the additional requirements set forth in the guidance letter.

The statutory requirements for the structure of an executive compensation program are detailed and complex, and PG&E must do more work to align executive compensation metrics to those used in the Wildfire Mitigation Plans and continue developing its executive compensation structure to reflect the spirit of Public Utilities Code section 8389 and promote safety as a priority. Energy Safety is initiating a process to develop the 2022 executive compensation guidelines and anticipates holding a public workshop related to that effort in the fall of 2021.

Sincerely,

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