Pacific Gas and Electric Company®

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April 24, 2023

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

Re: Pacific Gas and Electric Company's Response to Public Advocates Office's Comments on 2023 Executive Compensation Structure Submissions (2023 Executive Compensation Docket, #2023-EC Docket)

Dear Director Thomas Jacobs:

Pacific Gas and Electric Company ("PG&E") respectfully submits the following reply to the comments of the Public Advocates Office ("CalAdvocates") on the investor-owned utilities' 2023 executive compensation structure submissions.

CalAdvocates does not and cannot dispute that PG&E's executive compensation program is "structured to promote safety as a priority and to ensure public safety and utility financial stability," and that it otherwise meets the requirements of Assembly Bill ("AB") 1054.[1] CalAdvocates nevertheless asks the Office of Energy Infrastructure Safety ("Energy Safety") to require PG&E to make purported "improvements" to two of 17 performance metrics in PG&E's Short-Term Incentive Plan ("STIP") and Long-Term Incentive Plan ("LTIP") program designs. CalAdvocates' request is inappropriate: If an executive compensation structure, overall, meets the requirements of AB 1054—which is the case here—there is no statutory basis for a "line item veto" of particular performance metrics. CalAdvocates thus is asking Energy Safety to exceed its jurisdiction, and this invitation should be declined. Moreover, as explained below, one of CalAdvocates' suggested revisions to the metrics would contravene a 2020 decision of the California Public Utilities Commission ("CPUC") and would undercut the shared goal of wildfire safety.

CalAdvocates also asks Energy Safety to define the term "executive officers" as used in AB 1054, and to establish rules for redaction of employees' financial information in executive compensation submissions. These are rulemaking proposals that are procedurally inappropriate here; such proposals are better made in connection with an Energy Safety workshop or in comments on Energy Safety's annual publication of executive compensation structure submission guidance, not in comments on the utilities' particular executive compensation programs. In any event, CalAdvocates' request to define "executive officers" should be rejected

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[1] Pub. Util. Code § 8389(e)(4); *see also id.* § 8389(e)(6).

because it ignores authority from the CPUC and the courts making clear that "executive officers" already has a settled and clear definition, such that it is not open to reinterpretation.

<u>PG&E's STIP and LTIP Metrics</u>

CalAdvocates offers suggestions for "improving" two of PG&E's metrics, but in doing so, appears to misconstrue the issue Energy Safety is statutorily charged with deciding. AB 1054 does not burden Energy Safety with superintending a utility's executive compensation program as a general matter or with micro-finessing a utility's performance metrics. That would be an unrealistic regulatory task, particularly given that, even in executive compensation circles, "there is little consensus on the specific principles that should guide EC decisions."[2] Rather, AB 1054 leaves the responsibility for designing an appropriate program where the law has always placed it—with the board of directors and its independent compensation committee,[3] subject to retrospective advisory input from shareholders[4] and, in PG&E's case, "[a]nnual review of awards by an independent consultant."[5] The statute charges Energy Safety with the more limited role of verifying that a utility's "compensation *structure* . . . meets the principles set forth in [Public Utilities Code § 8389(e)(4) and (e)(6)(A)],"[6] including that the program be "*structured* to promote safety as a priority and to ensure public safety and utility financial stability."[7] There can be no serious question that PG&E's structure—which is overwhelmingly weighted to safety and financial stability—satisfies the statute irrespective of the validity or invalidity of CalAdvocates' suggestions for improvement.

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[2] Willis Towers Watson, *Principles and Elements of Effective Executive Compensation Design*, at 2 (April 2017) (noting the lack of consensus after interviewing "hundreds of board members across various organizations and industries," and taking into account views expressed during "a series of in-depth workshops to distill the insights and experience of more than 100 . . . senior EC consultants").

[3] *See* New York Stock Exchange Listed Company Manual § 303A.05 ("The compensation committee must . . . have direct responsibility to: (A) review and approve corporate goals and objectives relevant to CEO compensation, evaluate the CEO's performance in light of those goals and objectives, and, either as a committee or together with the other independent directors (as directed by the board), determine and approve the CEO's compensation level based on this evaluation; [and] (B) make recommendations to the board with respect to non-CEO executive officer compensation, and incentive compensation and equity based plans that are subject to board approval . . . .").

[4] *See* 15 U.S.C. § 78n-1(a)(1), (c) ("Not less frequently than once every 3 years, a proxy or consent or authorization for an annual or other meeting of the shareholders for which the proxy solicitation rules of the [Securities and Exchange] Commission require compensation disclosure shall include a separate resolution subject to shareholder vote to approve the compensation of executives [paid for the prior year, as disclosed in the proxy statement]. . . . [Such] shareholder vote . . . shall not be binding on the issuer or the board of directors of an issuer, and may not be construed . . . as overruling a decision by such issuer or board of directors.").

[5] Decision Approving Reorganization Plan of PG&E and PG&E Corporation, D.20-05-053, at 88 (June 1, 2020).

[6] Pub. Util. Code § 8389(e)(6)(B).

[7] *Id.* § 8389(e)(4).

CalAdvocates does not dispute the point. It does not contend that PG&E's overall executive compensation structure fails to comply with the statute, nor does CalAdvocates contend that adopting its suggestions is necessary for PG&E's program to pass muster. Accordingly, CalAdvocates' proposal to require PG&E to modify two of its metrics has no statutory basis, and, if adopted, would exceed Energy Safety's jurisdiction.[8] The proposals should be rejected for that reason alone.

In any event, CalAdvocates' critiques of the metrics are meritless:

Wildfire Risk Reduction Metric: The Wildfire Risk Reduction metric, weighted 15% in the STIP, promotes reduction of the most serious wildfires. It measures the number of ignitions in PG&E's High Fire Threat Districts ("HFTDs") and High Fire Risk Areas ("HFRAs") that are reportable to the CPUC per D.14-02-015 and that result in a fire that burns more than 5000 acres, damages or destroys more than 500 structures, or causes a third-party fatality. The Wildfire Risk Reduction metric operates in tandem with a separate metric called Reportable Fire Ignitions in HFTDs, which measures the count of *all* reportable ignitions. Both of those metrics work alongside PG&E's robust, multi-year programs for reducing wildfire risk, such as its system hardening initiative—which is itself the subject of a separate performance metric in the LTIP called System Hardening Effectiveness

CalAdvocates does not criticize the Wildfire Risk Reduction metric as such, nor does it dispute that this metric, like the executive compensation program as a whole, promotes public safety. Rather, CalAdvocates merely suggests that the metric might promote safety even *more* effectively if, instead of using a performance range, the metric score becomes zero if there is just one qualifying wildfire while PG&E's system hardening and other wildfire risk mitigation initiatives remain ongoing.

CalAdvocates' proposal is misguided and would undercut the shared goal of wildfire safety. For one thing, CalAdvocates neglects to mention that the metric score *is* automatically reduced to zero in the event of a qualifying fire that results in a fatality, because PG&E regards such an outcome as categorically unacceptable.[9] For another, CalAdvocates overlooks that the circumstances and community impacts of different fires can be very different, such that it could be potentially unfair to withhold all compensation on this metric in the event of a single qualifying fire. For example, a fire that does not result in a fatality, and does not burn a single structure, but burns more than 5000 unpopulated acres because firefighting authorities determined that it was best to let it burn itself out, presents a very different scenario. Zeroing out the metric in the case of just one such fire is potentially problematic from the standpoint of recruiting and retention. As PG&E previously explained:

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[8] *See* Gov't Code § 15475.5(c) (providing for judicial vacatur of a decision if Energy Safety "proceeded without, or in excess of its jurisdiction" or "failed to proceed in a manner required by law").

[9] *See* PG&E's 2023 Executive Compensation Structure Submission at 8.

> If incentive compensation or a material portion thereof is perceived as subject to withholding in unpredictable ways, then an executive will likely substantially discount it when assessing the value of an overall compensation package—which could hurt a utility's ability to recruit and retain the talent required to meet its mission of providing safe, reliable, affordable and clean energy to its customers. This observation stems from an executive compensation concept called "line of sight," which stresses the importance of an executive being able to see a clear link between the executive's efforts on the job and the achievement of incentive compensation performance metrics, and a clear link between achievement of performance metrics and payment of incentive compensation. If "line of sight" is unclear or subject to breakage in ways that are perceived as outside the executive's control, then incentive compensation loses its incentive effect and can lose its value as a recruitment/retention tool, and thereby fail to promote the activities it is meant to promote.[10]

Here, there are myriads of factors affecting wildfire ignition risk, and wildfire scope and scale, that are outside the control of PG&E and its executive officers (*e.g.*, climate, fuel and other environmental conditions, and wind strength and direction, and decisions by firefighting authorities, to name a few). Those factors already make it challenging to design an efficacious metric that promotes reducing the most severe wildfires. Zeroing out the metric if there is just one qualifying fire that does not involve a fatality could compound the problem because just one such fire driven by factors outside the executive officers' control would result in no pay on the metric. That could be unpredictable and potentially unfair, thereby hurting PG&E's ability to recruit and retain the executive officers who are necessary to lead the company in its efforts to continually improve public safety.

The CPUC implicitly has recognized the problems with proposals like the one CalAdvocates makes, because the CPUC affirmatively declined to adopt such a regime. In the CPUC's June 1, 2020 Decision Approving Plan of Reorganization of PG&E and PG&E Corporation, D.20-05-053, the CPUC provided merely that there shall be "[a] *presumption* that a material portion of executive incentive compensation shall be withheld if . . . PG&E is the ignition source of a catastrophic wildfire," and that this presumption can be overcome if withholding would be "inappropriate based on the conduct of the utility."[11] Yet under CalAdvocates' proposal, there would not be a presumption, but, instead, an *automatic* withholding of a material portion of executive officer incentive compensation (15% of STIP payments at target) in the event of a fire meeting the criteria specified in the metric. CalAdvocates' proposal thus not only is imprudent, but also improperly contravenes the CPUC's decision.

Simply put, the Wildfire Risk Reduction metric, like PG&E's executive compensation program as a whole, indisputably promotes safety. CalAdvocates' suggestion for

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[10] Declaration of John Lowe, attached as Appendix D to PG&E's Post-Hearing Brief and Comments on Assigned Commissioner's Proposals in I.19-09-16, at ¶ 7.

[11] D.20-05-053 at 88 (emphasis added).

"improvement" would exceed Energy Safety's jurisdiction, would contravene the CPUC's prior decision, and would undercut the shared goal of wildfire safety. The proposal should be rejected.

Electric Corrective Maintenance in HFRAs: This metric promotes reducing the backlog of outstanding tags in PG&E's HFTDs and HFRAs that present potential wildfire risk. CalAdvocates does not dispute that this metric, too, promotes wildfire safety. CalAdvocates merely argues that it might promote safety *even more* if it extended beyond the backlog of tags existing as of year-end 2022, and included tags newly created in 2023. CalAdvocates does not and cannot contend, however, that that is necessary to render PG&E's executive compensation structure compliant with AB 1054, and, accordingly, CalAdvocates cannot credibly contend that Energy Safety has authority to require such a change. Stated differently, whether a different or revised metric might be beneficial, or even better than the existing one, is not the question here.

Moreover, there is no requirement in AB 1054, or in executive compensation best practices, that incentive compensation cover the waterfront of every priority. Incentive compensation is just one of many tools for promoting achievement of a utility's objectives, and PG&E already has processes in place for risk-prioritizing and addressing new tags as they are created. That the metric does not extend to newly created tags does not make the metric, much less PG&E's entire executive compensation structure, deficient.

Additionally, it is a hallmark of effective incentive compensation design that performance milestones be clearly defined, measurable, and enforceable—a principle enshrined in AB 1054 itself.[12] Here, that means taking a defined population of tags as of the date immediately before the start of the performance period, and setting milestones based on resolving particular percentages of them (in this case, 40% for the minimum milestone, 48% for target, and 56% for the maximum milestone).[13] It would not be feasible to set milestones based on an ever-shifting population that include tags added during the performance period itself. A performance metric that constantly moves the goalposts is not a meaningful or effective metric.

Furthermore, CalAdvocates is incorrect in asserting that while the "metric incentivizes clearing the backlog, it but [sic] could also incentivize the prioritization of less critical backlog tags over newly generated tags with a higher safety priority."[14] PG&E's work in reducing its tag backlog is based on risk reduction and does not ignore newly generated tags. Indeed, as of January 1, 2023, PG&E has committed to being in a "steady state" such that all new ignition risk tags in HFRAs/HFTDs will be completed in compliance with GO timelines.[15] Thus, there is no risk of PG&E prioritizing less critical backlog tags over newly generated tags with a higher safety priority.

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[12] *See* Pub. Util. Code § 8389(e)(4) (requiring "performance metrics that are measurable and enforceable, for all executive officers").

[13] *See* PG&E's 2023 Executive Compensation Structure Submission at 54.

[14] CalAdvocates Comments at 7.

[15] *See* PG&E Revised 2022 Wildfire Mitigation Plan at 684; PG&E 2023 Wildfire Mitigation Plan at 448, 451.

Simply put, CalAdvocates' critique of this metric is both legally and factually meritless, and evinces little regard for principles of effective incentive compensation design.

<u>Definition of "Executive Officers"</u>

When the Legislature used the term "executive officers" in AB 1054, it was not writing on a blank slate. Rather, the Legislature chose a term that has a settled meaning in the law, and that companies use and apply all the time. Because the term already has a clear definition, there is no room for CalAdvocates' proposed alternative definition, or for its proposal that Energy Safety "[]engage stakeholders" to come up with a "consensus definition."[16]

AB 1054's executive compensation structure requirements apply to "executive officers, as defined in [Public Utilities Code] Section 451.5."[17] Section 451.5(c) defines "executive officer" to mean "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." Section 451.5(c)'s definition closely tracks the definition of "executive officer" found in Securities and Exchange Commission Rule 3b-7, namely, a company's "president, any vice president of the [company] in charge of a principal business unit, division or function (such as sales, administration or finance), any other officer who performs a policy making function or any other person who performs similar policy making functions for the [company]."[18]

The CPUC's decisions make clear that § 451.5(c)'s definition of "executive officer" extends no further than Rule 3b-7 executive officers—a point CalAdvocates does not seem to dispute. In December 2018, the CPUC issued Resolution E-4963, which held that the term "officer" in a different section of the Public Utilities Code, § 706, "means those employees of the investor owned utilities in positions with titles of Vice President or above, *consistent with Rule 240.3b-7 of the Securities Exchange Act of 1934*."[19] And in its August 20, 2021 decision in Southern California Edison Company's General Rate Case, the CPUC, observing that § 451.5(c)'s definition of "executive officer" is "similar to the definition provided in Rule 3b-7," held that it is "reasonable to continue to apply the definition of 'officer' adopted in Resolution E-4963."[20] Accordingly, the CPUC held that the term "officer"—and by extension, "executive officer"—extends no further than Rule 3b-7 executive officers.

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[16] Public Advocate Office Comments on 2023 Executive Compensation ("CalAdvocates' Comments") at 1, 6 (submitted April 12, 2023).

[17] Pub. Util. Code § 8389(e)(4), (e)(6).

[18] 17 C.F.R. § 240.3b-7.

[19] Resolution E-4963 at 8, Finding 5 (CPUC Dec. 13, 2018) (emphasis added).

[20] Decision on Test Year 2021 General Rate Case for Southern California Edison Company, D.21-08-036, at 417 n.1353, 419 (CPUC Aug. 20, 2021).

The CPUC then explained that such officers are necessarily a small, high-level group, and that determining who is in that group requires a fact-intensive, officer-by-officer analysis:

> [O]nly VPs that are in charge of a "principal business unit, division or function" or who perform a policy making function are executive officers under Rule 3b-7. The adjective "principal" is a modifier of all of the nouns that follow in the list. By setting forth conditions under which a VP will be considered a Rule 3b-7 officer, it is clear that the Rule did not intend for all VPs to be considered Rule 3b-7 officers. . . . Rule 3b-7 officers are senior-level management, responsible for policy decisions of the company, and directly answerable to the [utility's] Board of Directors because their hiring and firing are determined by the Board.[21]

The CPUC's decision is in accord with judicial authority, which holds that "a court [must] reject reliance on an employee's title and instead . . . perform a fact-intensive analysis of the employee's duties and responsibilities."[22]

Moreover, the law is clear that "policy making" in this context requires "significant" policy making functions, not just any role in policy making.[23] Additionally, the courts have held that "policy making" requires the authority to implement—not merely to influence—such policy decisions. As one court put it: "To decide that [Rule 3b-7] reach[es] individuals involved in discussing company and strategy and policy, but who do not have authority to actually implement such policy, would expand the scope of [the rule] far beyond what any court to date has recognized as policy making authority."[24]

Against this legal backdrop, CalAdvocates' proposals must be rejected. First, CalAdvocates' proposed definition of "executive officers," namely, "all high-level executives, SVPs, and VPs whose roles have a direct nexus to electric safety and wildfire safety,"[25] is wholly untethered to the statutory definition and the case law construing it. Under CalAdvocates' proposed definition, an officer could qualify even if the officer does not engage in policy making in *any sense whatsoever*, as long as the officer's role has a "direct nexus" to safety (*e.g.*, an operational nexus). Certainly CalAdvocates' proposed definition would not require authority both to formulate and implement policy, which, as noted, the case law requires for "executive officer" status. Further, under CalAdvocates' proposed definition, an officer could qualify even if the officer's employment is not "subject to the approval of the board of directors"—an explicit requirement for "executive officer" status under § 451.5. Additionally, under CalAdvocates' definition, an officer could qualify even if the officer is not "in charge of a principal business unit, division, or function of the public utility"—which again is an explicit requirement under § 451.5. CalAdvocates' definition also makes no reference to the officer being "employed by the

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[21] *Id.* at 418-19.

[22] *SEC v. Prince*, 942 F. Supp. 2d 108, 133 (D.D.C. 2013) (collecting cases).

[23] 17 C.F.R. § 240.16a-1(f) (note) (providing with respect to a very similar definition of "officer" that "[p]olicy-making function is not intended to include policy-making functions that are not significant").

[24] *Prince*, 942 F. Supp. 2d at 136.

[25] CalAdvocates' Comments at 6.

public utility"—which also is a requirement under § 451.5.[26] In short, CalAdvocates' preferred definition contravenes the *actual* definition, and should be rejected.

Second, there is no valid basis for CalAdvocates' request that Energy Safety "[]engage stakeholders" in an attempt to develop some new "consensus definition."[27] There already *is* a broadly recognized definition. A statute and regulation spell out the definition, the courts have interpreted it, and corporations nationwide apply it every day for purposes of compliance with the federal securities laws. It would be nothing but confusing, contradictory, and disruptive if Energy Safety were to develop a definition that differs from the existing definition.

Third, CalAdvocates' stated basis for the supposed need for a new definition—that the utilities' submissions differ as to how they interpret "policy making"—is incorrect. The utilities' submissions may use different words, but they all describe the same concept that is embodied in § 451.5, Rule 3b-7, and applicable case law: high-level authority to formulate and implement significant policy decisions.[28] And to the extent CalAdvocates asserts that the utilities' submissions are inconsistent because some classify certain officer positions as "executive" whereas others do not,[29] that is no inconsistency: As noted, the CPUC and the courts have made clear that determining whether someone is an "executive officer" requires examining the individual's role within a particular company, not just looking at titles.

In short, the definition of "executive officers" in AB 1054 is already clear. Energy Safety should apply the settled definition, and should decline CalAdvocates' invitation to come up with a new one.

<u>Redaction Issues</u>

CalAdvocates complains that the utilities did not all take the same approach to redacting (from the publicly filed versions of their submissions) specific compensation information for identified, named individuals. Though PG&E does not object to an effort at standardization, PG&E urges Energy Safety to bear in mind that "Californians enjoy a right to privacy in their private financial affairs."[30] Although this privacy interest can be lessened when an individual takes a job with compensation that is already subject to mandatory public disclosure, not all individuals who might qualify as "executive officers" under Public Utilities Code §§ 451.5 and 8389(e) necessarily fit into that category; for some, the securities laws may not require such disclosures in annual proxy statements. Such employees necessarily accept their positions

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[26] Executive compensation at PG&E's holding company parent, PG&E Corporation, also is structured to promote safety and utility financial stability, and generally tracks the structure for PG&E's own executive officers. Compensation information for PG&E Corporation's executive officers can be found in PG&E's and PG&E Corporation's joint proxy statements, which are available at https://investor.pgecorp.com/financials/annual-reports-and-proxy-statements/default.aspx.

[27] CalAdvocates' Comments at 1, 6.

[28] *See id.* at 4-5 (quoting the utilities' submissions).

[29] *See id.* at 1-3.

[30] *Sacramento Cty. Employees' Ret. Sys. v. Superior Ct.*, 195 Cal. App. 4th 440, 468 (2011).

without any pre-existing requirement that the dollar amounts of their individual salaries, or the values of their incentive compensation, be publicized. Accordingly, such executive officers have a protectable privacy interest in their financial information, and it would be inappropriate to require its public disclosure.[31]

For these reasons, PG&E urges Energy Safety to continue to permit redaction for executive officers whose compensation information is not subject to pre-existing public disclosure requirements.

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If PG&E can provide further information that would be helpful to Energy Safety as it considers PG&E's request for approval of its 2023 executive compensation structure, please do not hesitate to contact me.

Sincerely,

/s/

Lisa Laanisto
Director, Compensation
Pacific Gas and Electric Company

cc: safetypolicy@energysafety.ca.gov

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[31] *See, e.g.*, *International Fed'n of Pro. & Tech. Engineers, Loc. 21, AFL-CIO v. Superior Ct.*, 42 Cal. 4th 319, 331 (2007) (holding that government employees did not have a reasonable expectation of privacy in their salary information because the law long had provided that "the name of every public officer and employee, as well as the amount of his salary, is a matter of public record"—while observing that "the privacy expectation regarding income earned in the *private* sector" is "significantly" greater) (emphasis added).