August 2, 2018

Honorable Bill Dodd, Co-Chair, Wildfire Preparedness and Response Legislative Conference Committee
Honorable Chris Holden, Co-Chair, Wildfire Preparedness and Response Legislative Conference Committee
Honorable Anthony Cannella, Member, Wildfire Preparedness and Response Legislative Conference Committee
Honorable Ben Hueso, Member, Wildfire Preparedness and Response Legislative Conference Committee
Honorable Hannah-Beth Jackson, Member, Wildfire Preparedness and Response Legislative Conference Committee
Honorable Jeff Stone, Member, Wildfire Preparedness and Response Legislative Conference Committee
Honorable Brian Dahle, Member, Wildfire Preparedness and Response Legislative Conference Committee
Honorable Chad Mayes, Member, Wildfire Preparedness and Response Legislative Conference Committee
Honorable Eloise Gomez Reyes, Member, Wildfire Preparedness and Response Legislative Conference Committee
Honorable Jim Wood, Member, Wildfire Preparedness and Response Legislative Conference Committee

Dear Conference Committee Members:

Collectively we represent residential and commercial property insurers serving over 95% of the market share in California. Insurers have spent the last nine months helping fire victims secure immediate relief following the fires and assisting victims in preparing for their futures. In contrast, the investor owned utilities (IOUs), which have received a preferred tax status, the power of eminent domain, and monopolistic marketing advantages, have responded in this period of crisis and recovery by advocating not for fire victims, but for the financial gain of their investors by attempting to convince the Legislature to strip constitutional rights from damaged property owners after failing to convince California courts to do so for over twenty years. Instead of focusing on their own financial gain, IOUs should focus on producing viable ideas for preventing and mitigating wildfire exposure and funding the costs of helping citizens harmed by the fires they ignite. This is particularly applicable to PG&E, who has already been found by CAL FIRE to have caused 16 of the North Bay fires, with the cause of the deadly Tubbs Fire still to be released.

We urge the conferees to consider the following:

- The Legislature cannot by statute legally grant PG&E the liability bailout it is seeking;
- Even if the Legislature could grant the relief, it would be unwise to do so from a legal and public policy standpoint;
- Contradicting the courts on inverse cannot be reconciled with the insurance regulatory environment and removes incentives for IOUs to implement critical safety procedures; and,
- The focus on “inverse condemnation” is a distraction from the real, pressing issues, which include a real meaningful reduction in wildfire risk and ensuring there is an effective and sound utility regulatory regime.

The Legislature cannot by statute legally grant PG&E the bailout it is seeking

PG&E, as well as other utilities, want financial relief for their investors at the expense of others by shifting their liability elsewhere. To accomplish this, they are asking the Legislature for financial relief from "inverse condemnation" liability even though the Legislature cannot constitutionally grant their request. A property owner may file an "inverse condemnation" lawsuit because of rights guaranteed under the California Constitution's "Takings Clause[1]." Under this clause, the government has the power to take private property (and pay "just compensation") using the power of eminent domain. An inverse condemnation action is simply the reverse: focusing on the property owner's rights, a property owner can claim that government has implicitly "taken" (or condemned) their property and file an "inverse condemnation" action to recover "just compensation."

The Legislature cannot by statute change the California Constitution[2]. Similarly, the Legislature cannot modify constitutional rights announced in cases by the California judiciary. In a July 5, 2018 letter to Senator Jerry Hill, Legislative Counsel Diane Boyer-Vine states: "Although the Legislature is free to overturn the courts' *statutory* interpretations when dissatisfied with them, the courts 'are the final arbiters of the meaning of the California Constitution.[3]' The Legislative Counsel concludes that "the Legislature may not statutorily interpret the California Constitution in a manner that conflicts with a judicial interpretation."

To PG&E's frustration, California courts have equated IOUs with traditional government agencies (such as a public utility) for purposes of constitutional analysis. In *Barham v. Southern California Edison*[4], California's 4th District Court of Appeal held that it was "not convinced that any significant differences exist regarding the operation of publicly versus privately owned electric utilities…" and found "no rational basis upon which to find such a distinction." The Court of Appeal rejected any differentiation "between damage resulting from the operation of a utility based solely upon whether the utility is operated by a governmental entity or by a privately owned public utility, thereby ensuring that Californians enjoy constitutional protection when any utility, whether owned by investors or taxpayers, causes damage when providing electrical service. In short, if IOUs are provided the same eminent domain power as government, and thus act as "government," the same rules should apply; injured parties should have protection under the Takings Clause so they can seek just compensation using an inverse condemnation action.

Still, long dissatisfied with the *Barham* decision, the IOUs unsuccessfully attempted to obtain a contrary court interpretation. In 2012, the 2nd District Court of Appeal came to the same conclusion in *Pacific Bell Telephone Company v. Southern California Edison*[5], a case in which Pacific Bell sued Edison in inverse condemnation when a surge in Edison's underground electrical lines caused Pacific Bell's telephone cables buried in the same trench to burn. In upholding *Barham*, the *Pacific Bell* court replied upon and adopted previous appellate court holdings and held:

> Of particular significance in this case is that "a public utility's monopolistic or quasi-monopolistic authority derives directly from its exclusive franchise provided by the state…" and that monopoly "is guaranteed and safeguarded by the state Public Utilities Commission, which

[1] California Constitution, Article 1, Section 19: "Private property may be taken or damaged for a public use and only when just compensation, ascertained by a jury unless waived, has first been paid to, or into court for, the owner…"
[2] Citing People v. Birks, 19 Cal.4th 108, 117 (1998).
[3] Citing People v. Birks, 19 Cal.4th 108, 117 (1998).
[4] 74 Cal.App.4th 744 (1999).
[5] 208 Cal.App.4th 1400 (2012).

> possesses the power to refuse to issue certificates of public convenience and necessity to permit potential competition to enter" the market.

The Court went on:

> We do not believe the happenstance of which type of utility operates in an area should foreclose a property owner's right to just compensation under inverse condemnation for the damage, interest and attorney fees and should limit the property owner to traditional tort remedies.

The IOUs are now asking the Legislature to overturn these appellate decisions, which protect property owners' constitutional rights. It cannot be ignored that the incredibly nuanced and sophisticated constitutional construct of inverse condemnation has been repeatedly interpreted by the California judiciary to be good and fair public policy.

The Legislature cannot constitutionally legislate away the Courts' interpretation of the Constitution. During last week's conference committee hearing, Michael Wara's reliance on *Methodist Hospital v. Saylor* case was misplaced. Unlike here, *Saylor* involved ambiguous constitutional provisions that the Court had not previously ruled upon, not constitutional provisions with decades of case law interpretation. Further, Legislative Counsel has concluded that the proposal originally circulated by the IOUs (which is similar to the Governor's proposal) is unconstitutional as it runs afoul with the Separation of Powers framework of the Constitution. Because courts have equated IOUs to public utilities, damaged property owners can commence inverse condemnation actions. If PG&E disagrees with these decisions, it must go to the judicial branch because, as the California Supreme Court has stated: "If we have construed [the Constitution] incorrectly, only we can remedy the mistake[6]."

In fact, the IOUs have three pending cases to challenge application of inverse condemnation. For the Butte Fire (2015), PG&E has a pending petition for review with the California Supreme Court requesting that the Court overturn adverse lower court rulings. For the North Bay Fires (2017), PG&E has filed an appeal with the First Appellate District Court of Appeal, after the trial court judge allowed an inverse condemnation action to proceed. For the Thomas and Rye Fires (2017), Edison has given notice of intent to challenge the inverse condemnation action in the Superior Court and its plans to appeal an adverse decision. The Superior Court hearing date is on Oct. 4, 2018[7].

The courts are the proper forum for considering whether IOUs should be treated as "government" for purposes of California's Constitution. The Legislature cannot alter previous court interpretations of property owners' rights under the Constitution. The relief PG&E is seeking must be obtained in the judicial branch – and there are three immediate opportunities for doing so.

Even if the Legislature could grant the relief, it would be unwise

Solving one "problem" by creating others is a mistake. When the Legislature previously attempted a "quick fix" related to utilities, the utility deregulation led to a disaster of unintended and unforeseen consequences. Relieving IOUs of equipment-caused wildfire liabilities will simply impose problems onto others with little understanding of the future unintended and unforeseen consequences. Shifting financial responsibility from IOUs to homeowners, who are less financially prepared for such a burden, is not an appropriate or effective

[6] People v. Birks, 19 Cal.4th 108, 117 (1998).

[7] Edison just settled its liabilities in a fourth case, for the Round Fire (2015), without appealing the Superior Court's adverse ruling on inverse condemnation.

response to the current situation. Moreover, a legislative bailout of an IOU, who failed to engage in necessary wildfire prevention activities, would send the wrong public policy message to all organizations and private industries in the state that the Legislature will excuse the legal liability and societal responsibility of politically powerful business entities. This approach will hinder the state in crafting a proactive approach to address ongoing wildfire risk exposure.

The financial costs of such a bailout would be borne by three groups: 1) governments, 2) property owners/renters/businesses with insurance, and 3) property owners/renters/businesses without insurance.

Governments

Federal, state and local governments expend hundreds of millions of dollars in short-term suppression and relief costs, as well as costs related to destruction of government infrastructure. Local governments experience significant long-term costs related to landscape rehabilitation, lost business and tax revenues, degraded ecosystem services, depreciated property values, and impacts to tourism and recreation[8].

Insured Property Owners, Renters, and Businesses

Insurance provides significant immediate relief to property owners and renters. Property insurance typically pays for relocation expenses[9] (emergency shelter, clothing and food), transportation and storage costs, furniture rental for temporary residence, lost personal belongings, debris removal, home rebuilding and vehicle replacement. In the 2017 Northern California fires, commercial insurance will pay for damage to a variety of businesses, including ranches and vineyards, for losses such as damaged property and business interruption. Californians have filed 45,000 insurance claims related to the 2017 fires totaling $12 billion and covering damage to or destruction of 32,000 homes, 4,300 businesses, and more than 8,200 vehicles, watercraft, farm vehicles, and other equipment[10]. California depends on the availability of insurance.

Once an insurer pays a property owner or renter's insurance claim, it is permitted to seek reimbursement from the party that caused the damages. This process, called "subrogation," is common and used by many businesses and governments. A common example is California's Medi-Cal system which pays medical costs for indigent patients and then seeks recovery from any third party that caused the injuries. When insurers use subrogation, they 1) use the recoveries to repay their customers' deductibles and then 2) the California Department of Insurance ensures that insurance rate levels are lowered accordingly. Insurance subrogation is an important and necessary insurance rate cost containment practice that benefits insurance consumers and helps to hold liable parties accountable.

Uninsured Property Owners and Renters

There are often many individuals and businesses who have no insurance, or limited insurance, for their fire losses. In 2017, there were over 300 uninsured home losses. Federal and state relief will not be sufficient to make them whole.

Transferring utility liability onto these governments, businesses and individuals would trigger a cascade of negative impacts.

[8] https://headwaterseconomics.org/wildfire/homes-risk/full-community-costs-of-wildfire/
[9] http://www.insurance.ca.gov/01-consumers/105-type/95-guides/03-res/res-prop-claim.cfm#whatmaybe
[10] http://www.insurance.ca.gov/0400-news/0100-press-releases/2018/release013-18.cfm

Contradicting the courts on inverse cannot be reconciled with the insurance regulatory environment and removes incentives for IOUs to implement critical safety procedures

Insurance issues, alone, are incredibly complicated. Unlike any other jurisdiction in the world, California imposes profound control and cost containment over insurer operations – which will increase considerably once the additional restrictions from the 2018 legislation are enacted[11]. Even though the IOUs argue that climate change is making wildfire risks unmanageable, property insurance remains available in all communities in California. While insurance customers in high fire risk areas may experience more difficulty (even including a non-renewal), replacement insurance is available. And, in the rare event it is not obtainable in the regular market, every homeowner in California has a right to obtain fire insurance through the California FAIR Plan, which California law requires each insurer to join and fund with private funds (no State funds at all).

Despite the continuing commitment of property insurers to all California communities, many express frustrations when the risk of wildfire makes it harder or more expensive to obtain. Insurers ask the Legislature to consider this contradiction: insurers are told to serve every community but then are not only criticized when they signal the significant risks within certain communities, but they are also not permitted to set the actual prices that would adequately reflect the risk.

Insurers continue to be deprived of pricing tools they employ in other states. If the costs of reinsurance for California wildfire risk goes up, California regulations (not required by Proposition 103) prohibit insurers from passing along the additional costs – leading to rate inadequacies in high risk areas and pressure to reduce exposure accordingly. Further, as talk of the "new normal" and climate change has dominated this debate, insurers are not permitted to include models of climate change risk in their rate filings. Now the Legislature is being asked to consider having insurers relieve utilities of climate-related risk, when insurers are not allowed to include climate-related risk in insurance rates.

If, as the IOUs assert, we are headed to apocalyptic levels of uncontrollable fires, then will insurers be permitted to manage their risk exposure appropriately or will they be asked to: 1) stay in every community regardless of risk concentration, 2) charge inadequate rates, and 3) ask fewer questions about claims and pay benefits for longer periods of time? That was the thrust of the 2018 legislation and there will undoubtedly be consequences from some of the changes that are signed into law. We respectfully urge the conference committee to consider the inherent contradiction between bailing out a publicly owned company whose own equipment has been identified as the cause of at least 16 of the 2017 fires and who has faced criminal sanctions related to past maintenance lapses while continuing to impose additional costs and operational constraints on insurers who continue to help Californians across the state rebuild their lives after a loss. Even now many insurers are on the ground throughout the state working with our customers affected by the latest fires.

We hope to emphasize to the conference committee just how complicated, and unwise, the proposed transfer of liability would be without first undertaking significant analysis to understand the societal trade-offs. This applies not only to insurance customers, but also to the local governments that would face pressure for tax increases and the uninsured victims who would have no place to go.

The focus on "inverse condemnation" is a distraction from the real, pressing issues

With the remaining time in the legislative session, there are important opportunities for needed reform instead of "inverse condemnation." These include, at the very least, the following issues: 1) effective vegetation

[11] AB 1772 (Aguiar-Curry/Wood), AB 1797 (Levine), AB 1800 (Levine), AB 1875 (Wood), AB 2229 (Wood), AB 2594 (Friedman), SB 824 (Lara), SB 894 (Dodd/McGuire), and SB 917 (Jackson).

management and fuel reduction, 2) utility system hardening, and 3) certainty for IOUs in how to allocate liabilities among ratepayers and shareholders, including partial apportionment in "prudent manager" proceedings.

Instead of using this moment to work through these issues, we unfortunately are embroiled in a clash about "inverse condemnation" that is stalling all other efforts. We are running out of time and the prospects for important reforms will dim as this stalemate continues. Transferring IOU fire liabilities to others will not only result in immediate litigation (adding another case to the pile), but would be done with an incredible lack of understanding about the complicated tradeoffs. And, an important safety incentive would evaporate. Meanwhile, important reforms will be imperiled.

We respectfully request that conferees quickly, loudly, and unequivocally pronounce that an inverse condemnation "reform" will not be part of any final conference committee report. This would allow all interested stakeholders an opportunity to focus upon meaningful proactive wildfire risk prevention and mitigation activities, as opposed to merely limiting the legislative discussion to that of bailing out IOUs for their failure to protect citizens of the state from wildfire exposure caused by their improper business activities. It is time for us all to work jointly on identifying a set of important proactive reforms before the end of session. Citizens of the state need this legislative leadership and deserve a thoughtful and constructive approach to the wildfire risk exposure prevention and mitigation problem, not a debate on how to shift IOUs financial responsibility.

Should you have any questions, please contact Kara Cross, Personal Insurance Federation of California (916-442-6646/kcross@pifc.org); Armand Feliciano, Property and Casualty Insurers Association of America (916-440-1117/armand.feliciano@pciaa.net); Katherine Pettibone, American Insurance Association (916-873-3677/kpettibone@aiadc.org); Shari McHugh, Pacific Association of Domestic Insurance Companies (916-930-1993/smchugh@mchughgr.com); or Christian Rataj, National Association of Mutual Insurance Companies (303-907-0587/crataj@namic.org)

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