UCAN DATA REQUEST
UCAN-SDG&E-DR-2
SDG&E 2019 GRC – A.17-10-007
SDG&E RESPONSE
DATE RECEIVED: MARCH 5, 2018
DATE RESPONDED: MARCH 21, 2018

1. What is the current limit of the Wildfire Damage Reinsurance program?

SDG&E Response 1:

The information necessary to answer this question is confidential. Upon receipt of a signed non-disclosure certificate, SDG&E will provide this information. The non-disclosure certificate was sent to UCAN on January 12, 2018 and again on March 19, 2018.

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2. In the estimation of SDG&E and its brokers, does that limit represent the total market capacity presently available?
   a. If not, what is your best estimate of the total market capacity presently available?

SDG&E Response 2:

a. It is difficult to reasonably estimate the amount of general excess/wildfire liability capacity currently available in the market, or know if the limits of our current policies will even be available for our 2018 policies, which are due to be renewed by June 26, 2018. At this point, we have just started our renewal discussions/negotiations with over 50 retail and reinsurance insurers. In general, our preliminary feedback to date with insurers is that they are re-evaluating their CA liability exposures and are considering several options, which include exiting California completely, reducing the amount of capacity offered and/or increasing their premiums. Insurers are re-evaluating their positions due to the October and December 2017 CA wildfires, in which the losses are currently estimated to be approximately $12 billion, as reported by the CA department of insurance as of January 31, 2018.[1]

[1] https://www.insurance.ca.gov/0400-news/0100-press-releases/2018/release013-18.cfm

3. SDG&E acknowledged that if another wildfire event were to occur before the effective date of the 2019 GRC, the forecasts provided by the Company's broker in March, 2017 could be "understated". Given the catastrophic wildfires that occurred in both Northern and Southern California in the Fall of 2017, it seems improbable that any credence can be given those projections.
    a. Please provide a narrative explaining what, if any, impact the Fall, 2017 California wildfires have had upon the structure and cost of the Wildfire Damage Reinsurance program up to the present date.
    b. Specifically, has SDG&E experienced the loss of any insurance capacity to date or been informed that any participating insurers are withdrawing from the program?
    c. Secondly, have any insurers re-priced their participation in the program or announced their intention to do so? If so, please provide details of the current and/or anticipated changes that have or are expected to occur.

    Section 4 on Page NKC-16 Liability Insurance Premium Balancing Accounts (LIPBA) makes reference to the challenges created by the California legal environment and inverse condemnation in controlling insurance costs. Additionally, it makes reference to SDG&E's 2010 Z Factor application and Account 925 in the FERC Uniform System of Accounts. Presumably, these references are in support of the need for a Premium Balancing Account but no further detail is provided.

    Reference is again made on Page NKC-17 to a "new two-way balancing account for liability insurance premiums" and refers to the direct testimonies of Norma Jasso and Rae Marie Yu.
    d. Please provide the details of this proposed account. What confidence, if any, should be placed in the Wildfire liability forecasts shown on Page NKC-17 in light of the proposed balancing account?

SDG&E Response 3:

SDG&E objects to the form of the question, which is argumentative. Notwithstanding this objection, SDG&E responds as follows.

a. As explained in response to Question 2 above, we won't know with certainty what our 2018 liability premiums will be until our June 26, 2018 renewal, but given current CA statewide insurance loss estimates for the October and December 2017 wildfires approaching approximately $12 billion, we expect that our insurance premiums will increase, if insurance is even available.

b. See the responses to Questions 2 and 3.a above.

SDG&E Response 3 (continued):

c. See the responses to Question 2 and 3.a above.

d. The Liability Insurance Balancing Account ("LIPBA") is proposed as a two-way interest-bearing balancing account to record the difference between the liability insurance premiums authorized in this 2019 Test Year GRC and actual liability insurance expenses. Any forecasted amounts authorized above SDG&E's actual expenses will be returned to ratepayers with interest. Likewise, should SDG&E pay more for insurance than what is authorized, that money will be collected from ratepayers through the regular balancing account true-up process.

The wildfire liability forecast included in our GRC testimony was based on the best available information at the time, which primarily consisted of insurance broker forecasts and expected market conditions at the time of our filing (our 2019 GRC was filed October 6th, 2017). The October and December CA wildfires started after our October 6, 2017 filing date. There was no reasonable way for us to anticipate the specific occurrence of the Fall 2017 wildfires, much less the resulting impacts to our insurance premiums. Given the current CA statewide insurance loss estimates of approximately $12 billion for the October and December 2017 wildfires, we anticipate that insurance premiums will increase, assuming insurance is even available. Our exposure to insurance market volatility is one of the reasons for our request for the LIPBA because insurance premiums can fluctuate based on factors that are outside of our control. For example, as explained in Exhibit SDG&E-27 (at p. NKC-14), our 2016 premiums were impacted as a result of the 2015 Butte wildfires in the Pacific Gas and Electric Company service territory.

4. SDG&E's Manager of Insurance & Risk Management commented in 2015 that Corporate Center continuously evaluates alternative risk transfer mechanisms and, among other approaches, has reviewed pooling wildfire liability with other investor –owned utilities. Additionally, it was mentioned that Corporate Center would be reviewing captive insurance options over the next year with the belief that "… a broader and more effective use of a captive insurance company can help drive more competition in the insurance markets, including the potential to reduce premiums on various programs as well as create mote capacity in the insurance marketplace." (See: *UCAN Data Request, UCAN –SDG&E-DR-03, SEU 2016 GRC-A.14-11-003/004, SEU Response, Date Received: April13,2015, Date Responded: May 4, 2015.*
   a. Please provide a narrative regarding the status of any subsequent consideration of the foregoing alternatives including the results of the review of captive insurance options.

SDG&E Response 4:

a. Corporate Center continuously evaluates alternative risk transfer (ART) mechanisms. As part of this process, we have engaged our insurance broker to help us evaluate insurance-linked securities (ILS) as a possible option to increase wildfire insurance capacity. ILS coverage triggers (i.e., parameter(s) that activate(s) indemnity payments) can be structured in various ways, such as indemnity or non-indemnity methods. In general, indemnity triggers are structured similar to insurance in that coverage is based on actual losses sustained by the insured. Non-indemnity options typically rely on a specific set of parameters (e.g., wind speed, acres burned, etc.) to trigger coverage. In theory, the insured could sustain a loss but receive no indemnity if the defined triggers were not met. Per Guy Carpenter,[2] historically, corporate users of ILS have typically focused the design of their protection on property damage and/or business interruption, and have utilized non-indemnity triggers due to single-site protection needs. ILS potentially could be available specifically for wildfire, but have not been done before and would require additional time and resources to explore.

   As part of the 2017 excess liability renewal process, we requested that our insurance broker provide updated ILS indemnity trigger pricing projections. An indemnity trigger was selected because non-indemnity triggers potentially could represent an unacceptable basis risk (a risk that we may not receive payment if coverage parameters are not met). The pricing forecast, at that time, showed limited potential pricing benefits when compared to the wildfire reinsurance pricing for a small portion of the program provided by a single insurance carrier. This insurance carrier also provides capacity on our general excess liability program, which potentially could be impaired by moving forward with an ILS substitute. For these reasons, we did not pursue the ILS option further at the time, but we intend to continue to evaluate ILS as part of our 2018 excess liability renewal process. ILS may have the potential to be a new

[2] Sempra's reinsurance broker.

SDG&E Response 4 (continued):

source of wildfire liability capacity in these changing market conditions. While never been done before with wildfire liability, it would function as a form of insurance.

Additionally, since 2012 we have included collateralized reinsurance as part of our wildfire reinsurance program. Collateralized reinsurance is essentially a non-traditional insurance method that allows ILS funds, hedge funds, pension funds, or other third-party capital providers to participate in reinsurance programs.

In 2016, our insurance group also evaluated the use of a captive to possibly provide coverage for general excess and wildfire liability coverage. We found that the premiums that would have to be paid into the captive would exceed the premiums (at that time) we would pay for acquiring our existing insurance, so we decided not to pursue this as an option. However, we may re-evaluate the use of a captive if insurance premiums increase significantly in the future.