



OFFICE OF ENERGY INFRASTRUCTURE SAFETY

715 P Street, 20th Floor | Sacramento, CA 95814
916.902.6000 | www.energysafety.ca.gov

Caroline Thomas Jacobs, Director

December 9, 2021

Paul Marconi
Bear Valley Electric Service, Inc.
630 E Foothill Blvd
San Dimas, CA 91773

Mr. Marconi,

On June 29, 2020, the California Public Utilities Commission's (CPUC) Wildfire Safety Division (WSD) engaged Crowe LLP (Crowe) to conduct an independent audit of wildfire mitigation expenditures by the six investor-owned utilities (IOUs), who submitted 2019 and 2020 Wildfire Mitigation Plans (WMPs). WSD, along with all its functions, transitioned to the Office of Energy Infrastructure Safety (Energy Safety), a new department under the California Natural Resources Agency on July 1, 2021. Crowe recently completed its audit and Energy Safety is publicly releasing Crowe's final audit reports.

The purpose of Crowe's audit was to examine IOUs' spending in the execution of its WMP programs and initiatives relative to its prior General Rate Cases (GRCs). Crowe assessed the relationship between expenses and/or investments identified in the 2019 and 2020 WMPs and operating and capital expenditures approved in previous GRCs.

Enclosed is Crowe's Performance Audit of Bear Valley Electric Service, Inc. Wildfire Mitigation Plan Expenditures Final Report. The report identifies four findings and offers Crowe's recommendations regarding wildfire mitigation costs which may not be appropriate for cost recovery in future CPUC proceedings. Energy Safety may consider the final audit report in completing its annual report on compliance for the 2020 WMP. Energy Safety also provides this report to the CPUC for their review and consideration as the CPUC deems appropriate.

Sincerely,

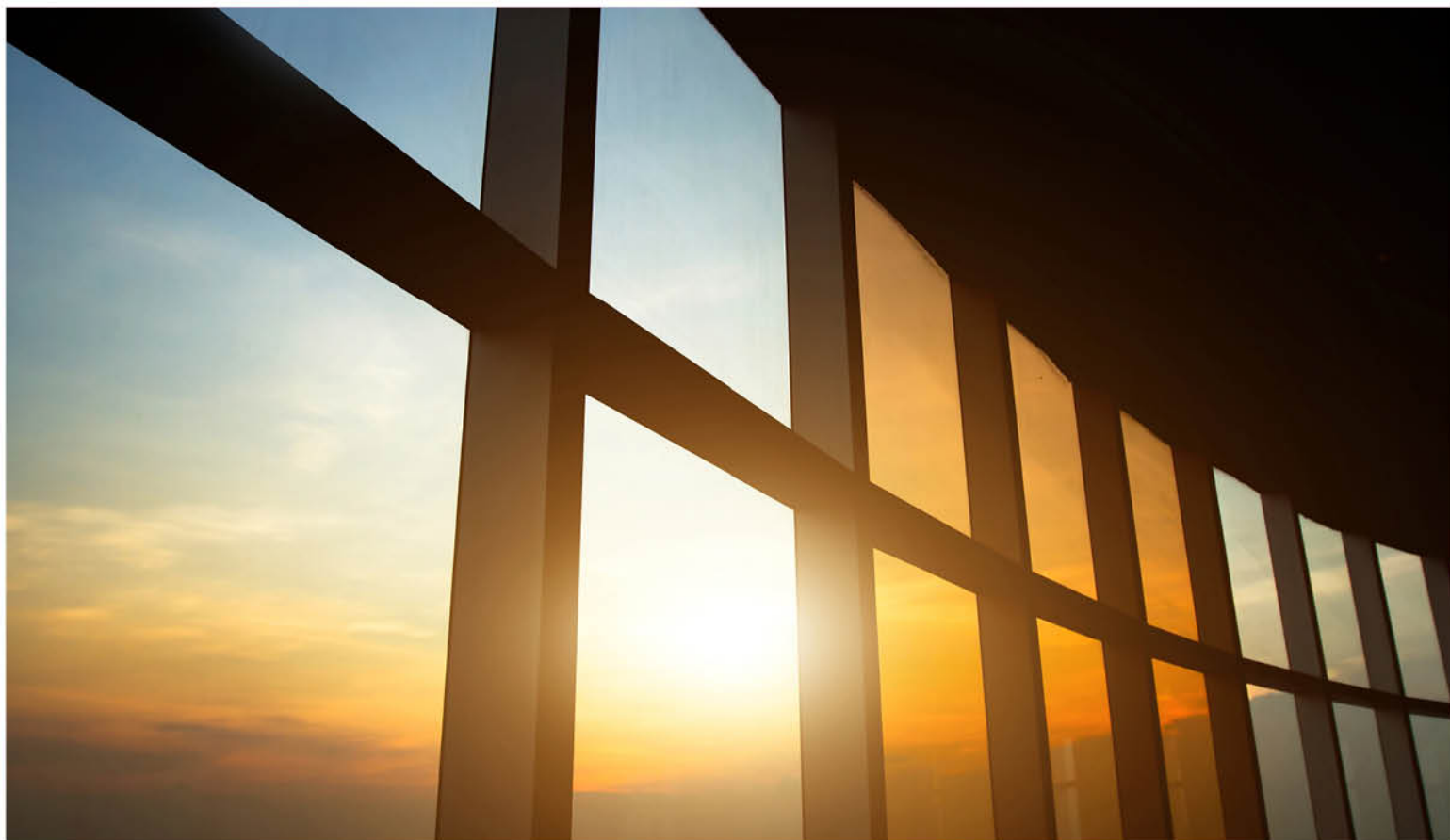
Caroline Thomas Jacobs
Director
Office of Energy Infrastructure Safety

Performance Audit of Bear Valley Electric Service

Wildfire Mitigation Plan Expenditures

Final Report

December 8, 2021



| | |
|--|-----------|
| Independent Auditor’s Report | 3 |
| Executive Summary | 4 |
| Introduction | 6 |
| Performance Audit Approach | 13 |
| Performance Audit Results | 15 |
| Appendix A – Procedures Performed | 26 |
| Appendix B – List of Records Examined..... | 29 |
| Appendix C – Comparison of 2020 GRC Authorized Costs to Actual Costs (2018 to 2020) | 30 |
| Appendix D – Management Response | 33 |

Independent Auditor's Report

Crowe has conducted a performance audit of Bear Valley Electric Service (BVES) for the period from January 1, 2017 through December 31, 2020 to determine whether BVES complied with General Rate Case (GRC) rules and regulations and to determine whether any expenses and/or investments identified in the 2019 and 2020 WMPs are duplicative of operating and capital expenditures approved in previous GRCs.

We have conducted our performance audit in accordance with *Government Auditing Standards* issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our conclusion based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for the findings and conclusions based on our audit objectives.

Our audit was limited to the following three objectives:

- Determine whether actual expenditures to date, and documented future planned expenditures, comply with approved General Rate Case (GRC) funding, related to wildfire mitigation activities, in accordance with GRC rules and regulations.
- Determine whether operating or capital expenditures identified in BVES's 2019 and 2020 Wildfire Mitigation Plans (WMPs) are duplicative of operating or capital expenditures approved in the 2018 GRC.
- Determine whether BVES's actual expenditures to date, and documented future planned expenditures, comply with the 2019 and 2020 WMPs for activities that BVES received approval and funding from GRCs or similar applications submitted to California Public Utilities Commission (CPUC) between 2017 and 2020.

Solely to assist us in planning and performing our performance audit, we obtained an understanding of the internal controls of BVES to determine the audit procedures that are appropriate for the purpose of providing a conclusion on BVES adherence to GRC rules and regulations and wildfire related accounting practices, as specified, but not for the purpose of expressing an opinion on the effectiveness of internal control. Accordingly, we do not express any assurance on the internal control.

The results of our tests indicated that, BVES met objectives 1 and 3 and did not meet objective 2 for the period of January 1, 2017 through December 31, 2020 in all significant respects. The cumulative effect of findings 1 through 4 result in questioned costs that exceeded the materiality threshold for the audit and our conclusion that BVES did not meet objective 2.

BVES's written responses included to the Findings and Recommendations Section of this report were not subjected to the performance auditing procedures, accordingly, we express no conclusion on them.

Crowe LLP
Crowe LLP

San Francisco, California

Executive Summary

Crowe LLP (Crowe) conducted a performance audit of Bear Valley Electric Company (BVES) in accordance with Generally Accepted Government Auditing Standards (GAGAS). In this section we provide background on the performance audit, an overview of the project background and scope, and a summary of Crowe's findings and recommendations related to this examination.

- A. *Project Background and Scope*
- B. *Crowe Findings and Recommendations*
- C. *Report Organization*

A. Project Background and Scope

The California Public Utilities Commission (CPUC) and its Wildfire Safety Division (WSD) (which is now the Office of Energy Infrastructure Safety (Energy Safety) with the California Natural Resources Agency¹) engaged Crowe to conduct an independent performance audit, in accordance with Generally Accepted Government Auditing Standards (GAGAS), of BVES, and submitted 2019 and 2020 Wildfire Mitigation Plans (WMPs). The CPUC and the WSD wanted to determine whether actual BVES expenditures to date, and documented future planned expenditures, comply with approved General Rate Case (GRC) funding, related to wildfire mitigation activities, in accordance with GRC rules and regulations. They were also interested to determine whether any expenses and/or investments identified in the 2019 and 2020 WMPs are duplicative of operating and capital expenditures approved in previous GRCs.

The audit period covers electric line of business expenditures from January 1, 2017 through December 31, 2020 and includes BVES's final and approved 2019 and 2020 WMPs and the most recent GRC application filed by BVES that is final and approved, any applications or advice letter requests that the IOU has filed with the CPUC as necessary to meet the scope of work.

| Wildfire Mitigation Plan | Cost Data Presented in WMP | | Applicable GRCs Used in Crowe Analysis |
|--------------------------|----------------------------|-----------|--|
| | 2019 | 2020 | |
| 2019 Plan | Actual | N/A | 2018 GRC |
| 2020 Plan | Actual | Projected | 2018 GRC |

B. Crowe Findings and Recommendations

This performance audit resulted in four (4) findings, totaling questioned costs of \$803,210, which we summarize in **Exhibit ES-1**. We also provide recommendations to address these findings.

¹ During the course of this engagement, the CPUC's Wildfire Safety Division transitioned into the Office of Energy Infrastructure Safety, a new department under the California Natural Resources Agency.

Exhibit ES-1**Performance Audit Findings and Recommendations Summary**

| Description of Finding | Questioned Costs | Recommendation(s) |
|--|------------------|---|
| 1. BVES Identified Total Actual Capital and Operating Costs (Inclusive of Incremental Vegetation Management Costs), Fell \$1.28M Below GRC Authorized Amounts for 2018 through 2020, and the CPUC Should Assess Whether 2018 through 2020 Incremental Vegetation Management Costs of \$2.51M Should be Recoverable in a Future Application | N/A | <ul style="list-style-type: none"> During the next rate cycle, or at a time if/when BVES seeks recovery of incremental vegetation management costs, the CPUC should evaluate whether the 2018 to 2020 incremental vegetation management costs are allowable for rate recovery given that BVES underspent relative to GRC funding for 2018 through 2020 inclusive of these incremental vegetation management costs. The CPUC should consider whether BVES ultimately completed (perhaps at a later date) the GRC O&M and capital projects/activities which were planned/approved and not completed during this time period. |
| 2. BVES Incurred Wildfire Mitigation Plan (WMP) Preparation Costs Required to Rework and Resubmit the WMP Following the CPUC's Rejection of the Original 2020 WMP | N/A | <ul style="list-style-type: none"> Evaluate whether the \$86,392.23 credit for WMP preparation costs was sufficient to compensate ratepayers and the CPUC for the problems associated with the WMP filing. |
| 3. BVES Incurred Unsubstantiated Legal Expenses in Incremental Wildfire Mitigation Accounts for Wildfire Mitigation Plan (WMP) Preparation/Review Costs | \$803,210 | <ul style="list-style-type: none"> The CPUC should request adequate justification for the \$803,209.82 in legal costs associated with the WMP in order to determine whether these costs should be treated as incremental for future funding in a subsequent proceeding. |
| 4. Wildfire Mitigation Cost Categories Provided in WMPs Do Not Align with How Wildfire Mitigation Costs are Categorized and Adopted as Part of GRCs, Making it Difficult to Monitor Incremental Wildfire Mitigation Costs | N/A | <ul style="list-style-type: none"> As part of the WMP process, BVES should provide wildfire mitigation costs separately for capital and for operating expenditures at a program level that is equivalent to, or can be easily reconciled to, the program level it uses for cost presentation in its GRC and RSARs. |
| Total | \$803,210 | |

C. Report Organization

The main body of this report includes the following components.

- Section 1**

In this section, immediately following the Executive Summary, we provide general information on the scope and objectives of this performance audit and contextual information about Bear Valley Electric Service.

- Section 2**

In this section, we outline our approach, including procedures and sampling methods applied.

- Section 3**

In this section, we provide our performance audit results, including our findings and recommendations.

Introduction

In this introduction section, we provide background on the performance audit of Bear Valley Electric Service (BVES), a division of Golden State Water Company (GSWC). We describe the BVES wildfire mitigation program, recently applicable general rate case proceedings, and memorandum accounts. This introductory section also provides the scope of the audit and sampling methodology employed. The remainder of this section is organized as follows:

- A. *Project Background*
- B. *Bear Valley Electric Service Wildfire Mitigation Program Profile*
- C. *Bear Valley Electric Service General Rate Cases*
- D. *Bear Valley Electric Service Memorandum Accounts*
- E. *Performance Audit Scope.*

A. Project Background

The CPUC and its WSD (now Energy Safety) engaged Crowe to conduct an independent performance audit, in accordance with Generally Accepted Government Auditing Standards (GAGAS), of BVES, who is regulated by the CPUC and submitted 2019 and 2020 Wildfire Mitigation Plans (WMPs). The CPUC and WSD wanted to determine whether actual BVES expenditures to date, and documented future planned expenditures, comply with approved General Rate Case (GRC) funding, related to wildfire mitigation activities, in accordance with GRC rules and regulations. They also were interested to determine whether any expenses and/or investments identified in the 2019 and 2020 WMPs are duplicative of operating and capital expenditures approved in previous GRCs.

The audit period covers electric line of business expenditures from January 1, 2017 through December 31, 2020 and includes BVES's final and approved 2019 and 2020 WMPs and the most recent GRC application filed by BVES that is final and approved, any applications or advice letter requests that the IOU has filed with the CPUC as necessary to meet the scope of work.

B. Bear Valley Electric Service Wildfire Program Profile

Senate Bill (SB) 901 required all California electric utilities to prepare plans on constructing, maintaining, and operating their electrical lines and equipment to minimize the risk of catastrophic wildfire. In its *Order Instituting Rulemaking to Implement Electric Utility Wildfire Mitigation Plans Pursuant to Senate Bill 901 (2018)*, Rulemaking (R.) 18-10-007 (Wildfire OIR), the CPUC outlined wildfire mitigation plan requirements.

1. 2019 BVES Wildfire Mitigation Plan

On February 9, 2019, BVES submitted its 2019 Wildfire Mitigation Plan (referred to as the 2019 WMP). The 2019 WMP provides details on BVES's strategies and programs to prevent wildfires. Programs included in BVES's 2019 WMP included:

- *Design & construction*, including system, equipment and structure design and technical upgrades intended to improve system hardening and prevent contact between infrastructure and fuel sources (e.g., vegetation)
- *Inspection & maintenance*, including assessment and diagnostic activities to ensure infrastructure in working condition and vegetation adheres to minimum distance specifications
- *Operational practices*, including proactive day to day actions taken to mitigate wildfire risk (e.g., prepare for de-energization)
- *Situational & conditional awareness*, including methods to improve system visualization and awareness of environmental conditions (e.g., camera installations)

- **Response & recovery**, including procedures to react to de-energization, wildfire or related emergency conditions.

Section 7.1, including Table 7-1 of the 2019 WMP included BVES's mitigation measures and cost recovery methods. **Exhibit 1** provides BVES's 2019 WMP mitigation measures identified in the 2019 WMP which BVES identified as are either GRC funded or memorandum account funded. For memorandum account funded measures, the cost is also captured.

Exhibit 1
Bear Valley Electric Service
Estimated Total Costs
Required to Support Wildfire Mitigation Programs
(Source: 2019 Wildfire Mitigation Plans)

| Program, Mitigation Measure, Measure Number | Operating Expense (E) or Capital Cost (C) | Funding Source | |
|--|---|----------------|--|
| | | GRC Funded | 2019 WMP Memorandum Account, Estimated Costs (\$ Millions) |
| Design & Construction | | | |
| 1 Pineknot Substation Upgrades, 4 Tree Attachment Removal Project, 5 Pole Loading Assessment & Remediation | C&E | x | |
| 2 Ute Undergrounding | C | | \$3.2 |
| 3 Fuse Upgrades | C | | \$5.2 (\$2.6/yr) |
| 6 Covered Conductor Replacement Pilot Program | C | | \$0.458 |
| 7 Covered Conductor Wrap Pilot Program | C | | \$0.292 |
| 8 Radford Line Covered Conductor Replacement Project | C | | \$2.5 |
| Inspection & Maintenance | | | |
| 9 First Annual On-Ground Inspection, 11 Predictive-Based Maintenance, 12 Electrical Preventative Maintenance Program, 14 GIS Data Collection & Sharing | E | x | |
| 10 Second Annual On-Ground Inspection | E | | \$0.090 |
| 13 LIDAR Inspection | E | | \$0.220 |
| 15 Vegetation Management | | x | FHPMA |
| Operational Practices | | | |
| 16 Operational Considerations/Special Work Procedures, 17 Automatic Recloser Upgrades, 18 Emergency Reporting, 19 Wildfire Infrastructure Protection Teams | | x | |
| Situational & Conditional Awareness | | | |
| 20 SCADA Installations, 21 GIS-Based Applications, 22 Web-Based Weather Resources, 26 Grid Automation | C&E | x | |
| 23 BVES-Owned Weather Stations | C | x | \$0.122 |
| 24 Weather Forecasting | E | | \$0.046 |
| 25 Remote Monitoring (Cameras) | N/A | N/A | N/A (not in plan period) |
| Response & Recovery | | | |
| 27 PSPS Protocols | E | x | \$0.042 |
| 28 Post Incident Recovery, Restoration & Remediation | C&E | x | CEMA |

2. 2020 Wildfire Mitigation Plan

On February 7, 2020, BVES submitted its 2020 WMP. The 2020 WMP incorporated lessons learned from the 2019 wildfire season and outlined the additional programs planned from 2020 to 2022 to prevent catastrophic wildfires.

Section 4.4, including Table 4-2 of the 2020 WMP included BVES's mitigation measures and cost recovery methods. **Exhibit 2** provides BVES's 2020 WMP mitigation measures identified in the 2020 WMP which BVES identified as are either GRC funded or memorandum account funded. For memorandum account funded measures, the cost is also captured.

Exhibit 2
Bear Valley Electric Service
Estimated Total Costs
Required to Support Wildfire Mitigation Programs
(Source: 2020 Wildfire Mitigation Plans)

| Program, Mitigation Measure, Measure Number | Operating Expense (E) or Capital Cost (C) | Funding Source | |
|---|---|----------------|--|
| | | GRC Funded | 2020 WMP Memorandum Account, Estimated Costs (\$ Millions) |
| Design & Construction | | | |
| 1 Pineknot Substation Upgrades, 2 Palomino Substation Safety and Technical Upgrades, 7 Tree Attachment Removal Project, 9 Pole Loading Assessment & Remediation | C&E | x | |
| 3 Ute Undergrounding | C | | \$3.5 (separate application) |
| 4 Construct an Energy Storage Facility within BVES' Service Territory | | | Separate application |
| 5 Critical Infrastructure PSPS Renewable Avoidance Package | | | TBD |
| 6 Fuse Upgrades | C | | \$5.2 (\$2.6/yr) |
| 8 Evacuation Route Hardening | | | \$0.200 |
| 10 Radford Line Covered Conductor Replacement Project | C | | \$5.6 |
| 11 Covered Wire Installation Program (35.5 kV System) | C | | \$10.9 (\$1.8/yr.) |
| 12 Covered Wire Installation Program (4 kV System) | C | | \$35.1 (\$3.5/yr.) |
| 13 Alternative Technologies, Install On-line | C | | TBD |
| Inspection & Maintenance | | | |
| 14 First Annual On-Ground Inspection, 16 Electrical Preventative Maintenance Program, 18 GIS Data Collection & Sharing | E | x | |
| 15 Second Annual On-Ground Inspection | E | | \$0.090 |
| 17 LIDAR Inspection | E | | \$0.240 |
| 19 Vegetation Management | | x | FHPMA |
| 20 Forester Consulting Services (Preventative Maintenance Checks) | E | | \$0.145 |
| Operational Practices | | | |
| 16 Operational Considerations/Special Work Procedures, 17 Automatic Recloser Upgrades, 18 Emergency Reporting, 19 Wildfire Infrastructure Protection Teams | | x | |

| | | | |
|---|-----|---|-------------------------|
| Situational & Conditional Awareness | | | |
| 20 SCADA Installations, 21 GIS-Based Applications, 22 Web-Based Weather Resources, 26 Grid Automation | C&E | x | |
| 23 BVES-Owned Weather Stations | C | x | \$0.027 |
| 24 Weather Forecasting | E | | \$0.045 |
| 25 Remote Monitoring (Cameras) | C | | \$0.500 (\$0.250/yr) |
| 26 Grid Automation | | x | |
| Response & Recovery | | | |
| 27 PSPS Protocols | E | x | \$0.042 |
| 28 Post Incident Recovery, Restoration & Remediation | C&E | x | CEMA |

C. Bear Valley Electric Service General Rate Cases

Our scope of work required that we review whether BVES expenditures to date, and documented future planned expenditures, comply with approved General Rate Case (GRC) funding, related to wildfire mitigation activities, in accordance with GRC rules and regulations. Below we provide an overview of CPUC GRC rules and regulations and background of the 2018 GRC.

1. General Rate Case Rules and Regulations

As specified on the CPUC website:

General rate cases (GRCs) are proceedings used to address the costs of operating and maintaining the utility system and the allocation of those costs among customer classes. For California's three large investor-owned utilities (IOUs), the GRCs are parsed into two phases. Phase I of a GRC determines the total amount the utility is authorized to collect, while Phase II determines the share of the cost each customer class is responsible and the rate schedules for each class. Each large electric utility files a GRC application every three years. For smaller utilities, authorized costs and allocation of costs are done in just one phase.

The CPUC reviews detailed cost data for various areas of utility operations and approves a budget for the first year – called a test year – of the GRC cycle. For years 2 and 3 – called post-test years – the GRC decision prescribes how to adjust the test year budget for inflation and other factors that may affect costs, such as additional capital projects between test years. The Commission has put in place regulatory mechanisms to adjust the costs approved in GRCs for unforeseen circumstances. For example, the Catastrophic Event Memorandum Account allows utilities to record costs for state emergencies declared by the governor.

Primary rules related to the GRC related to BVES rates/spending associated with the GRC are summarized in the GRC "Utility General Rate Case – A Manual for Regulatory Analysts," (Rate Manual) developed by the CPUC's Policy & Planning Division on November 13, 2017:

- GRCs establish revenue from customers to provide safe and reliable service at just and reasonable rates (costs).
- PUC Codes 454 and 728 hold the Commission responsible for ensuring that rates are just and reasonable.
- Major investor-owned utilities operating in California are required to file a GRC application with the Commission every 36 months (3 years).

- IOUs are required to submit a Risk Spending Accountability Report, in which the utility compares its GRC projected spending for approved risk mitigation projects with the actual spending on those projects, and explains any discrepancies.
- Cost of service regulation sometimes is referred to as rate of return regulation because in cost of service ratemaking utilities have an opportunity to earn authorized rate of return on prudently incurred capital investments. However, utilities are not guaranteed to earn their authorized return. Rates are set prospectively and an element of the authorized revenues is planned to repay investors for the use of their money. However, if the utility fails to manage its business efficiently and overspends, then it will likely fail to earn its authorized rate of return. This uncertainty is symmetrical, and if the utility spends less than authorized revenues it will earn greater than its authorized return.

Other notable aspects of the GRC process are identified below:

- The year in which the rate is set is referred to the “test year”
- The years between test years are referred to as “attrition years.”
- Budgets within the GRC generally are based on a unit cost multiplied by a number of units.
- Budgets in the GRC are not reconciled later with actual results.
- At the time the GRC is approved, the unit costs in the GRC are not tied out to BVES's costs of doing business (e.g., labor or overheads) as there are other sources of funding which BVES uses to cover its full revenue requirements
- Where unit costs evolve over time for a specific cost area, these unit costs are then adjusted through the ongoing GRC process during each test year.

2. 2018 BVES General Rate Case

On May 1, 2017, BVES filed its 2018 test year GRC for rates to become effective January 1, 2018 (A.17-05-004, 2018 GRC). In the 2018 GRC, BVES requested a decrease of 4.4 percent over 2017 revenues. BVES also requested adjustments for the 2018 through 2021 attrition years. In Decision 19-08-27 (August 22, 2019), the CPUC adopted lower attrition year amounts than requested. The CPUC also added an additional 2022 attrition year to extend the capital funding rate cycle and to complete some of the programs that the CPUC believed BVES could not complete in a four-year cycle. The 2018 GRC had the following proposed and adopted total revenue requirement for 2018 to 2022:

| Description | 2018 Revenue Requirement (\$1,000) | 2019 Revenue Requirement (\$1,000) | 2020 Revenue Requirement (\$1,000) | 2021 Revenue Requirement (\$1,000) | 2022 Revenue Requirement (\$1,000) |
|--|------------------------------------|------------------------------------|------------------------------------|------------------------------------|------------------------------------|
| Proposed (in Application) ² | \$37.2 (4.4% decrease) | \$39.0 (4.6% increase) | \$41.3 (6.0% increase) | \$43.6 (5.5% increase) | |
| Proposed (in Application), Net of Supply Cost Revenues and PPPC Revenues | \$24.8 | \$26.3 | \$28.1 | \$29.9 | |
| CPUC Adopted Net of Supply Cost Revenues and PPPC Revenues ³ | \$22.5 | \$23.7 | \$24.9 | \$26.0 | \$27.0 |

² Source: page 1 of the Application.

³ Source: D.19-09-002, Appendix A, pages 7, 9. The Commission was informed of an error in Appendix A of D.19-08-027. The text of the Settlement Agreement was inadvertently omitted from Appendix A. Appendix A of D.19-08-027 only included the motion to amend the original Settlement Agreement. Therefore, on September 6, 2019 the Commission issued D.19-09-002, attaching the complete Settlement Agreement, and correcting its inadvertent omission.

This 2018 GRC process was completed a year prior to the requirement for a WMP, which began in 2019.

D. Bear Valley Electric Service Memorandum Accounts

Utilities in California recover a large portion of their revenue requirement through balancing and memorandum accounts.⁴ The Rate Manual indicates:

A balancing account is an account established to record certain authorized amounts for recovery through rates and to ensure that the revenue collected matches the authorized amounts. Balancing accounts usually accrue interest – to be additionally returned to ratepayers if the utility is over-collected, or to recover additional revenue if the utility is under-collected.

Memorandum accounts are similar to balancing accounts except that they do not usually establish an authorized revenue requirement and are subject to further scrutiny by the CPUC. Upon Commission review expenses accrued in Memorandum accounts may or may not be recoverable through rates.

Below are specific characteristics of a memorandum account:

- Requires approval from CPUC
- Approval is through an advice letter (AL)
- Captures costs with specific program needs (often unforeseen) and that are in excess of costs included in rates set through the GRC process
- Costs accounted for separately from GRC costs
- Typically, memorandum account costs incurred are subsequently “trued up” or recovered in the next GRC.

BVES memorandum accounts applicable for this audit are shown in **Exhibit 3**.

Incrementality

- The basic idea of incrementality is that in order to recover any costs recorded in a memorandum account, those costs must be incremental, and not recovered in another way, such as in a GRC. For example, if BVES had forecast certain wildfire-related costs in a GRC, resulting in those costs being included in rates, they would not be incremental, and BVES could not record those same costs in a memorandum account and subsequently seek rate recovery. Incremental costs are costs that were not forecasted in the GRCs.
- Commission ratemaking is done on a prospective basis. The Commission's practice is not to authorize increased utility rates to account for *previously* incurred expenses, unless, before the utility incurs those expenses, the Commission has authorized the utility to book those expenses into a memorandum account or balancing account for possible future recovery in rates.

Exhibit 3 **Bear Valley Electric Service** **Memorandum Accounts**

⁴ Source: GRC Manual, page 7.

| BVES Memorandum Account | Abbrev. | Date Established | Type | Reference | Purpose |
|--|---------|------------------|---------|------------------------|--|
| Catastrophic Event Memorandum Account | CEMA | 1991 | Two-way | CPUC Resolution E-3238 | Establishes three categories of costs that are eligible for inclusion in the CEMA: (1) restoring utility services to customers; (2) repairing, replacing, or restoring damaged facilities; (3) complying with governmental agency orders in connection with events declared disasters by competent state or federal authorities. |
| Fire Hazard Prevention Memorandum Account | FHPMA | 9/10/2010 | Two-way | AL-244-E | Record costs related to the implementation of fire hazard prevention measures as adopted in D.09-08-029. |
| Fire Risk Mitigation Memorandum Account | FRMMA | 3/12/2019 | Two-way | AL 352-E | Record incremental costs of fire risk mitigation work that are not otherwise recovered in the adopted revenue requirement; track costs before WMP finalized; remain open to track wildfire mitigation costs not included in an approved WMP. |
| Wildfire Mitigation Plan Implementation Memorandum Account | WMPIMA | 6/6/2019 | Two-way | AL 364-E | The purpose of the WMPIMA is to track the implementation costs incurred for the Commission-approved fire risk mitigation plan that are not otherwise in BVES's revenue requirement. These costs shall include, but are not limited to, expenses and capital expenditures for increased inspections and patrols; system hardening and infrastructure modernizing, such as fuse upgrades, replacement of line with covered conductors; expanded monitoring automation and system protection such as Supervisory and Data Acquisition (SCADA); improved situational awareness and wildfire detection such as installation of weather stations; enhanced capacity to respond to events and incidents, including animal incidents; and vegetation management activities |

E. Bear Valley Electric Service Accounting

BVES uses JD Edwards (JDE) as its accounting system. JDE is an enterprise resource platform that houses numerous applications including but not limited to: general ledger, payroll, vendor setup, inventory, and capital assets. BVES account coding is profiled in **Exhibit 4** below:

Exhibit 4
Bear Valley Electric Service
Primary Account Code Descriptions

| Account Code | Description |
|----------------|--|
| Business unit | Type of business expense incurred, including for example Executive, Accounting, or Operations. |
| Object account | A field tracking whether the expense is an operating or capital expense. Operating expenses are code as 6000 to 7999 while capital costs are coded as the 1200 series. |
| Subsidiary | Details the type of expense, including for example, wildfire mitigation, vegetation management, or tree trimming. |

Additionally, BVES uses PowerPlan as its asset management system which tracks expenses for a specific project. PowerPlan houses capital asset detail and job costing information; and acts as a project management and capital asset management application. PowerPlan has limited integration with JDE; therefore Accounting & Finance reconciles capital assets in PowerPlan to the JDE general ledger and capital assets modules on a monthly basis.

F. Other Reports and Applications

In conducting our performance audit procedures, we relied on additional BVES reports and applications which are described below.

1. Risk Spending Accountability Reports

BVES is required to submit Risk Spending Accountability Reports (RSAR) on a quarterly basis. BVES submits RSARs in order to comply with the Phase Two Decision Adopting Risk Spending Accountability Report Requirements and Safety Performance Metrics for Investor-Owned Utilities and Adopting a Safety Model Approach for Small and Multi-Jurisdictional Utilities (Decision (D.) 19-04-020). RSARs provide a comparison of budgeted to actual spending. BVES includes explanations for budget to actual cost variances when they exceed a certain threshold.⁵ Specific RSARs and related documents we used for this project included:

- Advice Letter 371-E, RSAR, submitted October 14, 2019, covering actual costs as of 10/10/19
- CPUC response to AL 371-E, noting certain deficiencies with the RSAR
- Advice Letter 388-E, RSAR, submitted May 14, 2020, covering actual costs as of 10/10/19 and correcting deficiencies identified by the CPUC
- CPUC response to AL 388-E, accepting the RSAR.

Performance Audit Approach

The CPUC and its WSD (now Energy Safety) engaged Crowe to conduct this independent Performance Audit, in accordance with the Generally Accepted Government Auditing Standards (GAGAS). In accordance with GAGAS, Crowe followed 2018 Government Audit Standards (GAO-18-568G) which require us to establish an overall approach to apply in planning and performing this audit to obtain sufficient, appropriate evidence that provides a reasonable basis for findings and conclusions based on audit objectives.⁶

Crowe developed our audit plan and procedures to meet specific CPUC objectives identified in the Request for Proposal for this project. In developing this audit plan, among other factors, we primarily

⁵ The threshold variance for expenses is at least \$10 million, or a percentage variance of at least 20 percent subject to a minimum variance of \$5 million; for capital the threshold variance is at least \$20 million, or a percentage variance of at least 20 percent subject to a minimum variance of \$10 million; for units the threshold variance is at least 20 percent.

⁶ Section 8.01 of GAO-18-568G.

considered the following:

- Understanding the CPUC GRC process and wildfire mitigation program, including other existing forms of BVES oversight (e.g., GRC review processes)
- Addressing audit objectives specified by the CPUC
- Reducing audit risk to acceptable levels
- Designing a methodology to obtain sufficient audit evidence to provide a reasonable basis for findings and conclusions
- Developing suitable criteria to use to evaluate performance as it related to audit objectives
- Determining the significance or relative importance of the matter
- Communicating results to those in charge with governance or management.

A. Performance Audit Procedures Applied

Our performance audit objectives and procedures are detailed in **Appendix A**. Crowe also reviewed the documents identified in **Appendix B**. The CPUC had three (3) objectives for this performance audit:

1. Determine whether actual expenditures to date, and documented future planned expenditures, comply with approved General Rate Case (GRC) funding, related to wildfire mitigation activities, in accordance with GRC rules and regulations.
2. Determine whether operating or capital expenditures identified in BVES's 2019 and 2020 Wildfire Mitigation Plans (WMPs) are duplicative of operating or capital expenditures approved in the 2017 GRC.
3. Determine whether BVES's actual expenditures to date, and documented future planned expenditures, comply with the 2019 and 2020 WMPs for activities that BVES received approval and funding from GRCs or similar applications submitted to the CPUC between 2017 and 2020.

We submitted several data requests to the company which were progressively more focused throughout the engagement as we obtained more detailed data and information on the company's wildfire mitigation accounting practices. We interviewed management to understand BVES accounting systems and use of supporting information systems. We conducted an internal controls assessment, in particular to obtain an understanding of BVES internal controls as it related to differentiating GRC-funded expenses from memorandum account funded expenses.⁷ Finally, we also developed workpapers to document results of the performance audit.

As a basis for conducting our procedures, for the population we obtained and relied upon a database of capital and operating expenditures for 2018 through 2020. To test the veracity of BVES's cost database, we reconciled the cost data in this database to cost data used by BVES in several published documents in the record, including the GRC applications, WMPs, and RSARs.

Below, we identify several scope limitations related to this performance audit:

1. Our scope of work did not serve to validate the process and outcomes associated with the CPUC's GRC proceedings. Our scope was targeted to determining how BVES spent funds approved in GRC's which provided funding for WMP programs.
2. BVES presents costs in its GRC organized into generation, and electric and gas distribution lines of business (LOB). Our scope is targeted to the electric distribution LOB.
3. The timeframe for our audit spanned actual BVES wildfire expenditures incurred between January 1,

⁷ Where internal control is a process effected by an entity's oversight body, management, and other personnel that provides reasonable assurance that the objectives of an entity will be achieved (GAO-18-568, Fieldwork Standards for Performance Audits, Section 8.38c, page 164).

2017 to December 31, 2020.⁸

4. The audit did not cover BVES's 2021 Wildfire Mitigation Plan which was published on March 5, 2021. Wildfire mitigation plan requirements and priorities have evolved significantly over the 2019 to 2021 planning period with guidance from Energy Safety, actual program results, and lessons learned.

B. Sampling Methodology

We developed our sampling methodology for the examination using guidance from the American Institute of Certified Public Accountants (AICPA). Specifically, we relied on Chapter 11 (Audit Sampling) of the AICPA's Government Auditing Standards and Single Audits – Audit Guide (hereafter referred to as the AICPA Audit Guide).

The AICPA Audit Guide's minimum sample level threshold for obtaining a high level of assurance for a higher risk of material non-compliance was 60 sampling units. We stratified the population into the expense and capital populations.

After obtaining a database of BVES cost data, Crowe selected 76 total transactions (reflecting a combination of random and judgmental sampling) including 49 sampled from incremental wildfire subledgers and 27 from GRC funded accounts.

Crowe requested invoices, timesheets, business cases and other relevant documentation to test whether expenditures were allowable wildfire related costs. The selection represented \$1.07M in operating and maintenance activities and \$1M in capital costs, over the 2019 to 2020 period for purposes of conducting detailed testing to determine whether:

- Costs were supported by appropriate documentation, such as approved purchase orders, receiving reports, vendor invoices, canceled checks, timesheets, overhead tables and records, and correctly charged to account, amount, and period.
- Transactions were for an allowable activity under BVES's wildfire mitigation plan and memorandum account.
- Services were provided in the location or event identified by BVES.
- Transactions were consistent with policies and procedures (internal procedures, contract agreement, etc.)

Performance Audit Results

Our performance audit resulted in four (4) findings as presented in the remainder of this section. We have identified observations of controls and processes related to BVES wildfire mitigation related expenditures. Each finding includes a recommendation to correct the issue, and is organized into the following six (6) components:

- *Condition* – includes the error observed based on facts revealed from the examination.
- *Criteria* – the basis for our evaluation; in this case a specific policy, procedure, or leading practice.
- *Cause* – the underlying reason for why the non-compliance or error occurred.
- *Effect* – the impact on the organization and/or the ratepayer from the error.
- *Recommendation* – a suggested action to correct the deficiency; or what can be done to address both the cause and condition.
- *Management Response* – an opportunity for the company to provide its response to the finding and/or recommendation.

Findings and recommendations from this performance audit are provided beginning on the next page. In **Exhibit 7** below we summarize each of the four (4) findings and related questioned costs.

⁸ While our scope spanned this 2017 to 2020 audit period, BVES had a small amount of actual wildfire expenditures in 2018 with most actual wildfire expenditures incurred in 2019 and 2020.

Our consideration of internal control was for the limited purpose of designing procedures that were appropriate in the circumstances for the purpose of making a conclusion as to whether BVES met the performance audit objectives but not for the purpose of expressing an opinion on the effectiveness of BVES's internal control. Accordingly, we do not express an opinion on the effectiveness of BVES's internal control. Our consideration of internal control was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies and therefore material weaknesses or significant deficiencies may exist that were not identified. However, as discussed below, we identified two (2) deficiencies in internal control that we consider to be significant deficiencies.

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct misstatements in a timely manner. A material weakness in internal control is a deficiency, or combination of deficiencies, in internal control, such that there is a reasonable possibility that misstatements will not be prevented or detected and corrected in a timely manner. We did not identify any material weaknesses.

A significant deficiency in internal control is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance. We consider the deficiencies in BVES's internal controls identified in findings 2 and 3 to be significant deficiencies.

Exhibit 7
Summary of Findings and Questioned Costs

| Description of Finding | Questioned Costs | Failure to Meet Which of the 3 Audit Objectives |
|--|------------------|---|
| 1. BVES Identified Total Actual Capital and Operating Costs (Inclusive of Incremental Vegetation Management Costs), Fell \$1.28M Below GRC Authorized Amounts for 2018 through 2020, and the CPUC Should Assess Whether 2018 through 2020 Incremental Vegetation Management Costs of \$2.51M Should be Recoverable in a Future Application | N/A | 2 |
| 2. BVES Incurred Wildfire Mitigation Plan (WMP) Preparation Costs Required to Rework and Resubmit the WMP Following the CPUC's Rejection of the Original 2020 WMP | N/A | 2 |
| 3. BVES Incurred Unsubstantiated Legal Expenses in Incremental Wildfire Mitigation Accounts for Wildfire Mitigation Plan (WMP) Preparation/Review Costs | \$803,210 | 2 |
| 4. Wildfire Mitigation Cost Categories Provided in WMPs Do Not Align with How Wildfire Mitigation Costs are Categorized and Adopted as Part of GRCs, Making it Difficult to Monitor Incremental Wildfire Mitigation Costs | N/A | 2, 3 ⁹ |
| Total | \$803,210 | |

⁹ This finding was not considered significant to objective 3.

Finding 1 - BVES Identified Total Actual Capital and Operating Costs (Inclusive of Incremental Vegetation Management Costs), Fell \$1.28M Below GRC Authorized Amounts for 2018 through 2020, and the CPUC Should Assess Whether 2018 through 2020 Incremental Vegetation Management Costs of \$2.51M Should be Recoverable in a Future Application

Deficiency

Condition:

As shown in the line #1 of the table below, in the 2018 GRC the CPUC authorized operating and maintenance (O&M) costs of \$10.6M for the 2018 to 2020 period. In the supporting database provided by BVES to Crowe, BVES coded a total of \$10.8M of O&M costs for the 2019 to 2020 period as GRC-funded, \$0.175M above the 2018 GRC authorized amounts. These actual 2018 through 2020 O&M costs included incremental vegetation management costs recorded in wildfire memorandum accounts. **Exhibit C-2 in Appendix C** provides details of this excess spending by program area.

In the 2018 GRC, as shown in line #2 of the table below, the CPUC authorized capital costs of \$18.2M for the 2018 to 2020 period. In the supporting database provided by BVES to Crowe, BVES coded a total of \$16.8M of capital costs for the 2019 to 2020 period as GRC-funded, or \$1.45M below the 2018 GRC authorized amounts. **Exhibit C-2 in Appendix C** provides details of this under-spend by program area.

Taken together, BVES underspent its total operating and maintenance, and capital cost budget by \$1.28M from 2018 to 2020 (see line #3 of the table). This is inclusive of all vegetation management costs incurred during this time which exceeded GRC-adopted amounts by \$2.514M and totaled \$3.53M as shown in the line #5 of the table below.

Based on this underspend of \$1.28M relative to GRC-adopted amounts between 2018 and 2020, and because this underspend fully included the entire overspend of \$2.51M in vegetation management costs, the CPUC should evaluate whether BVES can later recover incremental vegetation management costs of \$2.51M as during this time BVES did not complete certain GRC approved activities/projects and thus had sufficient GRC funds to cover these incremental vegetation management costs.¹⁰

| Description | Total GRC Adopted Costs | Total Actual Costs | Difference |
|---|-------------------------|--------------------|--------------------|
| 1. 2018 through 2020 Operating and Maintenance Costs | \$10,610,170 | \$10,785,264 | \$175,094 |
| 2. 2018 through 2020 Capital Costs | 18,241,126 | 16,788,136 | (1,452,990) |
| 3. Total 2018 through 2020 Combined Operating and Maintenance and Capital Costs | \$28,851,296 | \$27,573,400 | \$(1,277,896) |
| Breakout of 2018 to 2020 Operating and Maintenance Costs | | | |
| 4. 2018 through 2020 Vegetation Management Costs (Includes Incremental Amounts Coded to Wildfire Memo Accounts) | \$1,016,379 | \$3,530,527 | \$2,514,148 |
| 5. 2018 through 2020 All Other Operating Costs | 9,593,791 | 7,254,737 | (2,339,054) |
| 6. 2018 through 2020 Operating Costs (ties to #1. Above) | \$10,610,170 | \$10,785,264 | \$175,094 |

¹⁰ The incremental amount of vegetation management costs exceeded the annual amount of vegetation management costs in rates of \$338,793.

Criteria:

The purpose of the Wildfire Mitigation Plan Memorandum Account (WMPMA) is to record, pursuant to Senate Bill (SB) 901 (Public Utilities Code Section 8386.4 (a)) and the Wildfire Mitigation Plan (also known as the Wildfire Safety Plan) approved by the Commission, incremental costs incurred to implement an approved wildfire mitigation plan that are not otherwise recovered in BVES's adopted revenue requirements. Such costs may include expense and capital expenditures for activities including but not limited to: operational practices, inspection programs, system hardening, enhanced vegetation management, enhanced situational awareness, public safety power shutoffs, and alternative technologies. Costs recorded to the WMPMA will not include costs approved for recovery in BVES General Rate Cases (GRCs) or recovered through BVES's Catastrophic Event Memorandum Account (CEMA), Fire Hazard Prevention Memorandum Account (FHPMA), Fire Risk Mitigation Memorandum Account (FRMMA), or other cost recovery mechanisms.

Cause:

Offsetting the increase in incremental vegetation management spending, BVES underspent in a number of capital and operating cost areas as identified below:

Operating & Maintenance (O&M) Costs

- 2019 Pole Loading Assessment and Remediation Program – underspent by \$186,743
- 2019 Power Generation Maintenance (FERC 546-555) – underspent by \$705,524
- 2019 Transmission System Maintenance (FERC 562-573) – underspent by \$191,716
- 2019 Distribution System Maintenance (FERC 580-598) – underspent by \$147,202
- 2020 Power Generation Maintenance (FERC 546-555) – underspent by \$930,066
- 2020 Transmission System Maintenance (FERC 562-573) – underspent by \$102,376

Capital Costs

- 2019 GO 174 Substation Safety and Reliability Compliance Projects – underspent by \$134,728
- 2019 BVPP – Install Engine System Monitor – underspent by \$915,961
- 2020 Safety and Upgrades of Palomino Station – underspent by \$882,061
- 2020 Replacement of Fawnskin Conductors – underspent by \$182,890

Effect:

BVES may recover incremental wildfire mitigation costs in a subsequent proceeding even though BVES underspent GRC adopted amounts, for approved projects/activities, enough to offset these additional incremental vegetation management costs for the 2018 through 2020 period.

Recommendation:

During the next rate cycle, or at a time if/when BVES seeks recovery of incremental vegetation management costs, the CPUC should evaluate whether the 2018 and 2020 incremental vegetation management costs are allowable for rate recovery given that BVES underspent relative to GRC funding for 2018 through 2020 inclusive of these incremental vegetation management costs. The CPUC should consider whether BVES ultimately completed (perhaps at a later date) the GRC O&M and capital projects which were planned/approved and not completed during this time period.

Management Response:

BVES believes Finding 1 is fundamentally flawed. BVES objects to Finding 1 defining “incremental costs” by aggregating *overall* O&M costs plus *overall* capital costs adopted in Bear Valley’s most recent GRC *over a three-year period* and comparing that amount to *actual overall O&M costs plus overall capital costs incurred over that three-year period*. This definition of “incremental costs” is inconsistent with the CPUC’s definition as confirmed in Commission decisions of “incremental costs” which compares the amount of a *specific category* of costs in a *single year’s* rates to the actual amount of costs incurred for that *specific category* of costs for that *single year*. BVES also claims that the Auditor failed to include in Finding 1 the critical fact that in Bear Valley’s most recent GRC the CPUC approved a settlement that contained \$338,793 in annual rates specifically for vegetation management costs. BVES claims that had the Auditor applied the CPUC definition of “incremental costs” it would have concluded that any actual vegetation costs that exceed \$338,793 in any of the calendar years of 2018, 2019 or 2020 are incremental, subject

to confirmation in a future CPUC proceeding to recover such costs. BVES claims that Finding 1, along with its Recommendation that BVES should not include the 2019 and 2020 incremental vegetation management costs for future CPUC rate recovery, should be withdrawn or rescinded.

Crowe Response:

BVES's primary concerns related to Finding #1 are that Crowe used an incorrect definition of incremental costs for purposes of cost recovery, did not disclose the amount of vegetation management costs in the base rates, and recommended preempting BVES from submitting vegetation management costs in a future proceeding.

Regarding the use of an incorrect incrementality definition, Crowe never suggested that the vegetation management costs in question were not incremental to the vegetation management costs of \$338,793 approved in the base rates. Nor did we intend to indicate that the company could not submit a request for such incremental funding.

The intent of this finding is to identify to the CPUC that certain GRC projects/activities were not completed during the 2018 to 2020 period and simultaneously BVES incurred substantial incremental vegetation management costs which are currently tracked in a memorandum account. Absent BVES completing the GRC approved 2018 to 2020 activities and projects, or there being a true up of the costs of these 2018 to 2020 activities and projects in later rate cycles, BVES could have shifted GRC approved funding to immediately cover the incremental vegetation management costs and then also recover these costs in a future cost recovery proceeding.

Crowe notes that this finding is an outcome of differences in the timing of the GRC ratemaking process and Wildfire Mitigation Plan (WMP) implementation. GRC approval cycles did not align with the requirements for additional work outlined in the WMPs. We acknowledge that during this transitional period between GRC cycles, there arose the need to fund certain WMP activities that were critical or emergency in nature to defend against wildfires and adhere to WMP requirements and that these new incremental WMP costs be recorded in memorandum accounts. However, we continue to recommend that in cases where GRC funds that were previously approved for certain projects/activities and time periods were instead used to fund incremental new wildfire related projects/activities, the CPUC should carefully consider whether to provide future rate recovery of these same incremental new wildfire-related costs in a subsequent proceeding. In evaluating the potential impacts of this finding, the CPUC should consider whether GRC capital projects which were planned/approved and not completed during the time period of the audit were ultimately completed at a later date without additional rate funding. The CPUC should also consider to what extent underspent GRC O&M funding, which may have been diverted to fund WMP activities, is ultimately "trued up" prospectively in a subsequent GRC cycle.

Finding 2 - BVES Incurred Wildfire Mitigation Plan (WMP) Preparation Costs Required to Rework and Resubmit the WMP Following the CPUC's Rejection of the Original 2020 WMP*Significant Deficiency*Condition:

BVES utilized a third-party to complete its Wildfire Mitigation Plan (WMP). BVES submitted this 2020 WMP to the CPUC for approval on February 7, 2020 (as amended March 6, 2020 and May 22, 2020). On July 22, 2020, the CPUC issued its Draft Action Statement noting key substantive and substantial concerns with the WMP which included proposed undergrounding of all of its power lines resulting in costs three times higher than they should have been and significantly higher costs than BVES peers.¹¹ The WMP also was not prepared using the correct format. BVES subsequently acknowledged committing a fundamental error in proposing undergrounding in its original plan. BVES resubmitted its WMP on September 18, 2020 and received final approval of the plan on January 14, 2021.

BVES received a credit amount of \$86,392.23, about 14 percent of the total incurred WMP plan preparation costs between 5/1/2019 and 1/21/2021 of \$628,574.30.

Criteria:

The purpose of the Wildfire Mitigation Plan Memorandum Account (WMPMA) is to record, pursuant to Senate Bill (SB) 901 (Public Utilities Code Section 8386.4 (a)) and the Wildfire Mitigation Plan (also known as the Wildfire Safety Plan) approved by the Commission, incremental costs incurred to implement an approved wildfire mitigation plan that are not otherwise recovered in BVES's adopted revenue requirements. Such costs may include expense and capital expenditures for activities including but not limited to: operational practices, inspection programs, system hardening, enhanced vegetation management, enhanced situational awareness, public safety power shutoffs, and alternative technologies. Costs recorded to the WMPMA will not include costs approved for recovery in BVES General Rate Cases (GRCs) or recovered through BVES's Catastrophic Event Memorandum Account (CEMA), Fire Hazard Prevention Memorandum Account (FHPMA), Fire Risk Mitigation Memorandum Account (FRMMA), or other cost recovery mechanisms.

Cause:

All BVES WMP preparation costs, including preparation costs and rework costs, are currently recorded in the BVES subledger #68552. Credit amounts are not easily identified within the ledger.

Effect:

There is the potential for WMP costs, which were caused by the failure of the consultant and company to catch significant errors, to later be claimed as incremental in a subsequent proceeding.

Recommendation:

Evaluate whether the \$86,392.23 credit for WMP preparation costs was sufficient to compensate ratepayers and the CPUC for the problems associated with the WMP filing.

Management Response:

BVES believes that Finding 2 in the Draft Report was based on a misunderstanding regarding the facts surrounding the costs for the preparation of the 2020 WMP. BVES ultimately did not compensate any vendor for work on the Rejected 2020 WMP. It only compensated vendors for work on the Refiled 2020 WMP, which was approved. In the exit interview with BVES, the Auditors concurred with Bear Valley's approach to only pay vendors for work on the Refiled 2020 WMP. BVES requests that the Auditors withdraw or rescind Finding 2 in its entirety.

¹¹ The CPUC indicated that use of a consultant to prepare documents does not relieve a regulated entity of the obligation to submit accurate information to the consultant, check the consultant's work, verify it is accurate, and submit material to the Commission and the WSD that meets statutory and regulatory requirements. Had the WSD not found the errors in BVES' WMP, it is not clear BVES would have ever discovered or corrected them on its own.

Crowe Response:

Crowe disagrees that this finding should be removed based on a misunderstanding of the facts. In performing our procedures nothing initially came to our attention to clearly identify that a credit amount was paid to BVES for the flawed initial work and that BVES only paid the vendor for the rework. Crowe subsequently requested additional information regarding this finding and BVES provided support for the amount of initial WMP preparation costs that ratepayers were reimbursed for. BVES furnished additional documentation that identified that BVES received a credit amount of \$86,392.23, or about 14 percent of the total WMP plan preparation costs of \$628,574.30 that it incurred between 5/1/2019 and 1/21/2021. We recommend that the CPUC assess whether the \$86,392.23 amount represents a sufficient credit to cover the problems associated with BVES's initial WMP.

Finding 3 - BVES Incurred Unsubstantiated Legal Expenses in Incremental Wildfire Mitigation Accounts for Wildfire Mitigation Plan (WMP) Preparation/Review Costs*Significant Deficiency*Condition:

Between 2018 and 2020, BVES incurred \$803,209.82 in legal expenses within its wildfire mitigation memorandum accounts which BVES indicated was for WMP activities. In our sample of transactional testing, we requested detailed support for 11 legal service invoices representing of \$226,786 of legal expenses. BVES provided us with completely redacted versions of these sampled invoices rendering it impossible for us to determine whether these expenses were legitimately associated with WMP activities. As a result, Crowe could not perform procedures to conclude that these were legitimate incremental wildfire-related expenses.

Criteria:

The purpose of the Wildfire Mitigation Plan Memorandum Account (WMPMA) is to record, pursuant to Senate Bill (SB) 901 (Public Utilities Code Section 8386.4 (a)) and the Wildfire Mitigation Plan (also known as the Wildfire Safety Plan) approved by the Commission, incremental costs incurred to implement an approved wildfire mitigation plan that are not otherwise recovered in BVES's adopted revenue requirements. Such costs may include expense and capital expenditures for activities including but not limited to: operational practices, inspection programs, system hardening, enhanced vegetation management, enhanced situational awareness, public safety power shutoffs, and alternative technologies. Costs recorded to the WMPMA will not include costs approved for recovery in BVES General Rate Cases (GRCs) or recovered through BVES's Catastrophic Event Memorandum Account (CEMA), Fire Hazard Prevention Memorandum Account (FHPMA), Fire Risk Mitigation Memorandum Account (FRMMA), or other cost recovery mechanisms.

Cause:

All BVES WMP legal costs are currently recorded in the BVES subledger #688552 which is an account BVES uses to capture incremental costs dedicated to wildfire mitigation. BVES indicated in its response that it could not provide unredacted versions of these legal invoices which would allow us to assess the validity of these transactions. BVES cited that these invoices are covered under Attorney-Client-Privilege and that the CPUC has accepted redacted legal invoices in the past.

Effect:

There is the potential that these legal costs are not legitimate wildfire related expenses and that BVES can later claim them as incremental in a subsequent proceeding.

Recommendation:

The CPUC should request adequate justification for the \$803,209.82 in legal costs associated with the WMP in order to determine whether they should be treated as incremental for future funding in a subsequent proceeding.

Management Response:

BVES objects to the request for unredacted legal invoices. BVES states that California law has long recognized the preeminence of protecting attorney-client privileged communications, and that those protections apply to CPUC proceedings, as well as to invoices for legal services. BVES claims that the CPUC has previously approved of legal costs without violating the protections of attorney-client privileged communications. BVES requests that Finding 3 either be rescinded in its entirety or substantially revised to recognize the sanctity of attorney-client privileged communications which includes legal invoices. BVES does not object to the Auditors noting that without unredacted copies of legal invoices the Auditors 11 are unable to satisfy their auditing requirements to confirm the validity of Bear Valley's WMP legal costs. In any event, BVES requests that the recommendation that the CPUC should not include any of Bear Valley's WMP legal costs in any subsequent CPUC proceeding be withdrawn or rescinded, as recommendations regarding CPUC ratemaking matters is beyond the scope of the audit.

Crowe Response:

Crowe maintains our position on this finding and that it is well within the scope of the audit to evaluate WMP-related costs. These WMP-related legal expenses are currently tracked in a wildfire memorandum account and BVES may submit them for cost recovery in the future. If these costs are submitted for reimbursement, without adequate documentation and justification, the CPUC will ultimately be challenged to determine to what extent these WMP-related legal expenses are allowable for cost recovery.

Finding 4 - Wildfire Mitigation Cost Categories Provided in WMPs Do Not Align with How Wildfire Mitigation Costs are Categorized and Adopted as Part of GRCs, Making it Difficult to Monitor Incremental Wildfire Mitigation Costs*Deficiency*Condition:

In the past, BVES Wildfire Mitigation Plans (WMPs) have included cost information at the following levels:

2019 Plan

- By program strategy, including operational practices, plans for inspection, vegetation management, system hardening, and situational awareness (as estimated annual costs). These costs were presented separately for capital and operating expenditures.

2020 Plan

- Wildlife mitigation activity (2019 planned, 2019 actual spend, 2020 spend target), organized into situational awareness and forecasting, grid design and system hardening, asset management and inspections, and vegetation management and inspection. These costs were presented as separately for capital and operating expenditures.

We find that approved BVES WMP capital and operating costs provided at these levels alone are inadequate for purposes of reconciling these costs to those adopted as part of the GRC process. During the course of the GRC process, and in its RSARs, BVES provides costs at a program level separately for capital and operating expenditures. However, while the 2019 and 2020 WMPs costs are also provided at a general program area level, these program categories are different from those used in the GRC. This creates challenges for reconciling GRC funded costs to WMP authorized costs.

Criteria:

WMP requirements are delineated in the following documents:

- 2019 WMP – D1905036 Guidance Decision on 2019 Wildfire Mitigation Plans
- 2020 WMP – RES WSD-002 Final Guidance Resolution, and Guidance Appendices
- 2021 WMP – 2021 WMP Guidelines Template.

Cause:

The CPUC has not required capital and operating expenditures delineated to a level that aligns with GRC cost categories as part of WMP content requirements. Additionally, WMP content requirements are evolving as Energy Safety gains more experience and knowledge of program needs.

Effect:

Energy Safety will have difficulty reconciling future BVES wildfire mitigation related capital and operating expenditures approved as part of the WMPs to those funded through the GRC process.

Recommendation

As part of the WMP process, BVES should provide wildfire mitigation costs separately for capital and for operating expenditures at a program level that is equivalent to, or can be easily reconciled to, the program level it uses for cost presentation in its GRC and RSARs.

Management Response:

BVES recognizes that it is challenging to reconcile costs in its GRC as compared to costs in its WMPs. The cost categories and other supporting data for Bear Valley's 2018 GRC were prepared years in advance of preparation of its 2019 WMP. BVES intends to better align cost categories in its upcoming GRC application to facilitate comparison with costs in its WMPs.

Crowe Response:

None.

Appendix A – Procedures Performed

The CPUC specified three (3) objectives for this performance audit of BVES. In **Exhibit A-1**, we list these three (3) objectives. **Exhibit A-2** provides a list of nineteen (19) tests we performed to meet the three (3) objectives.

Exhibit A-1 Performance Audit Objectives

| Number | Objective |
|--------|--|
| 1 | Determine whether actual expenditures to date, and documented future planned expenditures, comply with approved General Rate Case (GRC) funding, related to wildfire mitigation activities, in accordance with GRC rules and regulations. |
| 2 | Determine whether operating or capital expenditures identified in BVES's 2019 and 2020 Wildfire Mitigation Plans (WMPs) are duplicative of operating or capital expenditures approved in the 2017 GRC. |
| 3 | Determine whether BVES's actual expenditures to date, and documented future planned expenditures, comply with the 2019 and 2020 WMPs for activities that BVES received approval and funding from GRCs or similar applications submitted to the CPUC between 2017 and 2020. |

Exhibit A-2 Performance Audit Procedures

| Objective | Procedures |
|---|---|
| 1 - Determine whether actual expenditures to date, and documented future planned expenditures, comply with approved General Rate Case (GRC) funding, related to wildfire mitigation activities, in accordance with GRC rules and regulations. | <ol style="list-style-type: none"> 1. Obtain and review GRC guidelines available in resolutions, decisions, and GRC proceedings (for the 2019 and 2020 rate cases) applicable to spending GRC funds for wildfire mitigation. 2. Interview BVES regulatory and finance management to assess how the IOU is complying with applicable GRC resolutions, decisions, and proceedings related to wildfire mitigation spending. 3. Compare actual BVES wildfire mitigation activity spending practices with GRC rules and regulations and assess compliance. 4. Document non-compliance with GRC rules and regulations related to wildfire mitigation activity spending. |
| 2 - Determine whether operating or capital expenditures identified in BVES's 2019 and 2020 Wildfire Mitigation Plans (WMPs) are duplicative of operating or capital expenditures approved in the 2017 | <ol style="list-style-type: none"> 1. Request and obtain a database of actual BVES capital and operating expenditures covering the period from January 1, 2017 through the present, including expenses for electric operations (transmission and distribution). 2. Reconcile expenditure amounts included in the database with amounts reported in BVES's audited financial statements. 3. Reconcile GRC-funded expenditure amounts included in the database to amounts approved by the CPUC in the GRCs. To perform this test, obtain and review workpapers and exhibits associated with GRC rate case proceedings. |

| Objective | Procedures |
|--|---|
| GRC. | 4. Reconcile capital and operating expenditure amounts included in the database to amounts approved in the 2019 and 2020 WMPs. |
| | 5. Perform analytical procedures to determine whether expenditures reported as GRC funded in the database are also captured as incremental in a memorandum account. |
| | 6. Perform risk assessment of transaction types to inform risk-based sample selection in cost categories with potential duplication between GRC and memorandum accounts. Develop a sample of transactions to test to determine that wildfire mitigation activity expenditures are recorded properly as either GRC funded or incremental in a memorandum account or similar account. |
| | 7. Interview BVES and document procedures used by BVES to establish approved GRC expenditures by cost category and to track actual expenditures up to approved amounts. This includes potential imputing of approved GRC costs into subordinate cost categories. |
| 3 - Determine whether BVES's actual expenditures to date, and documented future planned expenditures, comply with the 2019 and 2020 WMPs for activities that BVES received approval and funding from GRCs or similar applications submitted to the CPUC between 2017 and 2020. | 8. Document and quantify instances of duplication between GRC-funded expenditures and incremental (memorandum account) expenditures. |
| | 1. Using prior GRCs or similar applications, and supporting workpapers and exhibits, create a data set of approved wildfire mitigation related expenditures by cost category. |
| | 2. Using data provided in approved 2019 and 2020 WMPs, create a data set of actual and planned capital and operating wildfire mitigation expenditures by planned funding source. |
| | 3. Link the data sets in item 7a and 7b above to identify funding for 2019 and 2020 WMP activities where BVES has received approval for in prior GRCs or similar applications. |
| | 4. Link the database in Item 6a to compare approved WMP capital and operating expenditures with actual WMP capital and operating expenditures. |
| | 5. Assess whether BVES is spending or plans to spend funds approved for in past GRCs or similar applications. |
| | 6. Perform risk assessment of transaction types to inform risk-based sample selection in cost categories with ambiguity between approved amounts and actual spend amounts. Develop a sample of transactions to test to assess whether actual recorded wildfire mitigation activity expenditures are aligned with approved expenditures. |
| | 7. Assess whether actual BVES wildfire mitigation spending is in accordance with the 2019 and 2020 WMPs and consistent with funding provided in past GRCs or similar applications. Document exceptions. |

Additionally, using the data obtained/developed in the above procedures, and interviews of BVES accounting and wildfire mitigation program management, we developed an expense tracking tool (in Microsoft Excel, provided under separate cover to the CPUC's WMD) that identifies and tracks the following data:

1. How current spending on WMP activities relate to current requests in GRCs for future spending and whether BVES is currently performing work and recording expenditures in a memorandum account in addition to requesting additional funds in a pending GRC for the same work currently being performed.
2. How GRC approved capital expenditures relate to wildfire activity spending in WMP memo accounts and other fire risk mitigation accounts, and if services and corresponding expenditures are additional activities beyond what was previously authorized. For approved capital expense projects, include start and end date.
3. How GRC approved operating expenditures relate to wildfire activity spending in WMP memo accounts and other fire risk mitigation accounts, and if services and corresponding expenditures are additional activities beyond what was previously authorized. For approved operating expense projects, include start and end date.
4. Proposed capital expenditures for wildfire mitigation. Identify capital projects that are: i) continuations of projects identified in the first GRC where the continuation is due to the initial approved amounts being spent as authorized and the need continues, ii) continuations of projects in the first GRC where the continuation is needed due to the project being unable to be carried out, iii) the same project identified in the first GRC (where no distinction is clear from the accounting records to prevent double recovery of funds for the same expenditures).
5. Proposed operating expenditures for wildfire mitigation. Identify operating expense projects that are: i) continuations of projects identified in the first GRC where the continuation is due to the initial approved amounts being spent as authorized and the need continues, ii) continuations of projects in the first GRC where the continuation is needed due to the project being unable to be carried out, iii) the same project identified in the first GRC (where no distinction is clear from the accounting records to prevent double recovery of funds for the same expenditures).
6. Any other capital or operating expenditure that could also be attributable to wildfire mitigation plan expenses.

Appendix B – List of Records Examined

1. 2019 Wildfire Mitigation Plan, dated February 6, 2019
2. 2020 Wildfire Mitigation Plan, dated February 7, 2020
3. 2020 Wildfire Mitigation Plan errata, dated May 20, 2020
4. 2020 Wildfire Mitigation Plan (refiled), dated September 18, 2020
5. Risk Spending Accountability Report (RSAR)
 - a. 2018 RSAR, submitted October 14, 2019 via Advice Letter U913 E (costs as of 10/10/19)
 - b. 2019 RSAR, submitted May 14, 2020
 - c. 2020 RSAR, submitted April 6, 2021
6. 2018 General Rate Case Application 17-05-004
7. 2018 General Rate Case Decision 19-08-027 and Appendix A, dated August 15, 2019
8. Audited Financial Statements for calendar years 2018 and 2019
9. Internal policies and procedures related to accounting
10. Capital and operating expenditures for calendar years 2019 and 2020
11. CPUC WSD Draft Action Statement on Bear Valley Electric Service Inc.'s 2020 Wildfire Mitigation Plan dated July 22, 2020

Appendix C – Comparison of 2020 GRC Authorized Costs to Actual Costs (2018 to 2020)

In this appendix we compare costs authorized as part of the 2018 General Rate Case for 2018, 2019 and 2020 with actual costs incurred by BVES. This appendix includes the following two (2) exhibits:

- Exhibit D-1 - Comparison of Authorized to Actual Expenses (2018 through 2020)
- Exhibit D-2 - Comparison of Authorized to Actual Capital Costs (2018 through 2020).

Exhibit C-1
Bear Valley Electric Service
2018 General Rate Case
Comparison of Authorized to Actual O&M Expenses
By Program
(Calendar Years 2018 through 2020)

| Year | Program | Authorized Budget (per RSAR) | Actual Costs | Difference |
|------|--|------------------------------|---------------------|--------------------|
| 2018 | Vegetation Management | \$338,793 | \$407,485 | \$68,692 |
| 2018 | Electrical Preventative Maintenance | 108,282 | - | (108,282) |
| 2018 | Predictive Based Maintenance of Overhead Lines | 98,544 | 83,000 | (15,544) |
| | 2018 O&M Expenses Subtotal | \$545,619 | \$490,485 | \$(55,134) |
| 2019 | Pole Loading Assessment and Remediation Program | \$287,010 | \$100,267 | \$(186,743) |
| 2019 | Vegetation Management | 338,793 | 902,447 | 563,654 |
| 2019 | Electrical Preventative Maintenance | 105,566 | 21,654 | (83,912) |
| 2019 | Predictive Based Maintenance of Overhead Lines | 96,073 | 60,104 | (35,969) |
| 2019 | Power Generation Maintenance (FERC 546-555) | 1,461,886 | 756,362 | (705,524) |
| 2019 | Transmission System Maintenance (FERC 562-573) | 294,316 | 102,600 | (191,716) |
| 2019 | Regional Market Equipment Maintenance (FERC 576) | 9,042 | 9,930 | 888 |
| 2019 | Distribution System Maintenance (FERC 580-598) | 2,566,902 | 2,419,700 | (147,202) |
| 2019 | General Plant Maintenance (FERC 935) | 58,602 | 49,102 | (9,500) |
| | 2019 O&M Expenses Subtotal | \$5,218,190 | \$4,422,166 | \$(796,024) |
| 2020 | Pole Loading Assessment and Remediation Program | \$459,216 | \$ - | \$(459,216) |
| 2020 | Vegetation Management | 338,793 | 2,220,596 | 1,881,803 |
| 2020 | Electrical Preventative Maintenance | 105,566 | 268,587 | 163,021 |
| 2020 | Predictive Based Maintenance of Overhead Lines | 96,073 | - | (96,073) |
| 2020 | Power Generation Maintenance (FERC 546-555) | 1,266,592 | 336,526 | (930,066) |
| 2020 | Transmission System Maintenance (FERC 562-573) | 179,476 | 77,100 | (102,376) |
| 2020 | Regional Market Equipment Maintenance (FERC 576) | 9,200 | 10,005 | 805 |
| 2020 | Distribution System Maintenance (FERC 580-598) | 2,332,367 | 2,802,600 | 470,233 |
| 2020 | General Plant Maintenance (FERC 935) | 59,078 | 157,200 | 98,122 |
| | 2020 O&M Expenses Subtotal | \$4,846,361 | \$5,872,614 | \$1,026,253 |
| | Total 2018 through 2020 O&M Expenses | \$10,610,170 | \$10,785,264 | \$175,094 |

Exhibit C-2
Bear Valley Electric Service
2018 General Rate Case
Comparison of Authorized to Actual Capital Expenses
By Program
(Calendar Years 2018 through 2020)

| Year | Program | Authorized Budget (per RSAR) | Actual Costs | Difference |
|------|---|------------------------------|---------------------|----------------------|
| 2018 | Pole Loading Assessment and Remediation Program | \$1,500,000 | \$1,471,019 | \$(28,981) |
| 2018 | Tree Attachment Removal | 500,000 | 567,340 | 67,340 |
| | 2018 Capital Expenses Subtotal | \$2,000,000 | \$2,038,359 | \$38,359 |
| 2019 | Pole Loading Assessment and Remediation Program | \$2,444,130 | \$5,096,681 | \$2,652,551 |
| 2019 | Tree Attachment Removal | 762,018 | 701,348 | (60,670) |
| 2019 | Replacement of Summit Conductors | 185,010 | 387,806 | 202,796 |
| 2019 | GO 174 Substation Safety and Reliability Compliance Projects | 410,000 | 275,272 | (134,728) |
| 2019 | Wire Upgrade and Relocation Project | 80,000 | 79,145 | (855) |
| 2019 | GO 95/165 Safety and Reliability Compliance Projects | 925,000 | 649,134 | (275,866) |
| 2019 | Shifting Tree Attachment to Poles/Underground Projects | 30,000 | - | (30,000) |
| 2019 | Public Works Project Support | 30,000 | 27,427 | (2,573) |
| 2019 | Office Furniture and Equipment Project | 25,000 | 23,755 | (1,245) |
| 2019 | BVPP Misc. Tools & Safety Equipment Project | 20,000 | 11,011 | (8,989) |
| 2019 | Field Operations Misc. Tools & Safety Equipment Project | 85,000 | 95,576 | 10,576 |
| 2019 | Minor Additions to General Structure Project | 45,000 | 40,307 | (4,693) |
| 2019 | Replacement of Baldwin Conductors | 184,674 | - | (184,674) |
| 2019 | BVPP – Install Engine System Monitor | 915,961 | - | (915,961) |
| 2019 | BVPP – Oil Filter Conversion and Cylinder Upgrades | 887,898 | - | (887,898) |
| 2019 | Safety and Technical Upgrades of Palomino Substation | 1,551,773 | - | (1,551,773) |
| 2019 | Replacement of Fawnskin Conductors | 182,890 | - | (182,890) |
| | 2019 Capital Expenses Subtotal | \$8,764,354 | \$7,387,462 | \$(1,376,892) |
| 2020 | Pole Loading Assessment and Remediation Program | \$2,444,130 | \$2,546,760 | \$102,630 |
| 2020 | Tree Attachment Removal | 732,018 | 1,453,218 | 721,200 |
| 2020 | BVPP – Install Engine System Monitor | 915,961 | 987,538 | 71,577 |
| 2020 | Safety and Technical Upgrades of Palomino Substation | 1,551,773 | 669,712 | (882,061) |
| 2020 | Replacement of Fawnskin Conductors | 182,890 | - | (182,890) |
| 2020 | GO 174 Substation Safety and Reliability Compliance Projects | 410,000 | 415,270 | 5,270 |
| 2020 | GO 95/165 Safety and Reliability Compliance Projects | 925,000 | 1,053,152 | 128,152 |
| 2020 | Office Furniture and Equipment Project | 25,000 | 33,929 | 8,929 |
| 2020 | Wire Upgrade and Relocation Project | 80,000 | - | (80,000) |
| 2020 | Field Operations Misc. Tools & Safety Equipment Project | 85,000 | 149,458 | 64,458 |
| 2020 | Minor Additions to General Structure Project | 45,000 | 53,279 | 8,279 |
| 2020 | Shifting Tree Attachment to Poles/Underground Projects | 30,000 | - | (30,000) |
| 2020 | Public Works Project Support | 30,000 | - | (30,000) |
| 2020 | BVPP Misc. Tools & Safety Equipment Project | 20,000 | - | (20,000) |
| | 2020 Capital Expenses Subtotal | \$7,476,772 | \$7,362,315 | \$(114,457) |
| | Total 2018 through 2020 Capital Expenses | \$18,241,126 | \$16,788,136 | \$(1,452,990) |
| | Total Combined O&M and Capital (2018 through 2020) | \$28,851,296 | \$27,573,400 | \$(1,277,896) |

Appendix D – Management Response



November 17, 2021

[REDACTED]
Crowe LLP
575 Market Street, Suite 3300
San Francisco, California 94105-5829

Re: Comments on Draft Performance Audit of Bear Valley Electric Service
Wildfire Mitigation Plan Expenditures

[REDACTED]
Under cover letter dated November 3, 2021, Mr. Koko Tomassian of the Office of Energy Infrastructure Safety ("Energy Safety") provided to Bear Valley Electric Service Inc. ("BVES" or "Bear Valley") a draft of the Performance Audit of Bear Valley Electric Service Wildfire Mitigation Plan Expenditures, dated October 8, 2021 ("Draft Report") by Crowe LLP ("Crowe" or "the Auditors"). Mr. Tomassian requested BVES to provide its written comments to Crowe on the Draft Report by November 17, 2021. BVES provides its comments below.

Background

The Draft Report states that the Auditors have conducted a performance audit of BVES for the period from January 1, 2017 through December 31, 2020. As stated in the Draft Report, the purpose of the audit is to

[D]etermine whether BVES complied with General Rate Case (GRC) rules and regulations and to determine whether any expenses and/or investments identified in the 2019 and 2020 WMPs are duplicative of operating and capital expenditures approved in previous GRCs.¹

The Draft Report further states that the audit was limited to the following three objectives:

- Determine whether actual expenditures to date, and documented future planned expenditures, comply with approved General Rate Case (GRC) funding, related to wildfire mitigation activities, in accordance with GRC rules and regulations.

¹ Draft Report at p. 3.

- Determine whether operating or capital expenditures identified in BVES's 2019 and 2020 Wildfire Mitigation Plans (WMPs) are duplicative of operating or capital expenditures approved in the 2018 GRC.
- Determine whether BVES's actual expenditures to date, and documented future planned expenditures, comply with the 2019 and 2020 WMPs for activities that BVES received approval and funding from GRCs or similar applications submitted to California Public Utilities Commission (CPUC) between 2017 and 2020.²

The Auditors concluded that BVES met objectives 1 and 3, but did not meet objective 2 in all significant respects.³ The Draft Report identifies Findings of certain deficiencies in four areas, and proposes Recommendations associated with each Finding.

In these comments, BVES will respond to each of the four Findings from the Draft Report. In addition, BVES will describe its overarching concern that certain of the Auditors' Recommendations are inappropriate as they propose rate-recovery recommendations regarding BVES costs. These Recommendations are not only beyond the scope of this audit, but they also conflict with prior Commission decisions and practices.

BVES' Overarching Concern: The Audit Recommendations Regarding Cost Recovery Treatment in Future CPUC Ratemaking Proceedings Exceed the Audit Scope

As set forth above, the Draft Report described the objectives and the limitations of its audit.⁴ In the section entitled "Project Background and Scope," the Draft Report further describes the audit scope as determining whether actual BVES expenditures relating to wildfire mitigation activities comply with GRC funding and whether any expenditures and/or investments identified in Bear Valley's 2019 and 2020 WMPs are duplicative of operating and capital expenditures approved in previous GRCs.⁵ Nowhere in the stated scope or objectives of the audit is there any indication of a request or directive for the auditors to make recommendations as to BVES's permission or authority to seek cost recovery of the audited costs. Certain Recommendations in the Draft Report ventured into the area of CPUC ratemaking and cost recovery, which clearly exceeds the stated objectives and limitations of the audit. Specifically:

² Draft Report at p. 3.

³ *Id.*

⁴ *Id.*

⁵ *Id.* at p. 4.

- In Finding 1, the Draft Report concludes that BVES “should not be allowed to later claim incremental vegetation management costs of \$2.51M . . .”⁶; and recommends that BVES “should not include the 2019 and 2020 incremental vegetation management costs for future rate recovery . . .”⁷
- In Finding 2, the Draft Report recommends that BVES “should not include a total of \$159,757.78 in WMP rework costs as incremental for future funding in a subsequent proceeding.”⁸
- In Finding 3, the Draft Report recommends that “the CPUC should not include a total of \$803,209.82 in legal costs associated with the WMP as incremental for future funding in a subsequent proceeding.”⁹

BVES understands and supports the need for auditing WMP-related costs that BVES may seek to recover in a future CPUC proceeding. However, it expects such audits to be focused upon whether or not the WMP-related costs are valid and not duplicative of GRC costs. Making Recommendations regarding what BVES may request in future CPUC rate-making proceedings is not within the scope of the audit or the expertise of an Auditor. Utility ratemaking and cost recovery remains exclusively within the CPUC’s purview.

To be clear, there is no Finding in the Draft Report that costs identified in the 2019 and 2020 WMP and tracked in the audited memorandum accounts are duplicative of costs approved in Bear Valley’s GRC. Rather, the Draft Report Recommendations identified above are proposed based on extraneous circumstances cited by the Auditor. Opinions of this nature have no place in this audit.

Finding 1 BVES Identified Total Actual Capital and Operating Costs (Inclusive of Incremental Vegetation Management Costs), Fell \$1.28M Below GRC Authorized Amounts for 2018 through 2020, and BVES Should Not Later Claim 2018 through 2020 Incremental Vegetation Management Costs of \$2.51M for Recovery in a Future Application.

Finding 1 of the Draft Report states that from 2018 to 2020, BVES spent \$1.28M less in total operating and maintenance (“O&M”) and capital costs than what was authorized in Bear

⁶ Draft Report at p. 17.

⁷ *Id.* at p. 18.

⁸ *Id.* at p. 19.

⁹ *Id.* at p. 20.

Valley's most recent GRC. According to the Auditors, since BVES spent \$1.28M less over that three-year period (which included the "overspend" of \$2.51M in vegetation management costs) than was authorized in rates, BVES should not be allowed to later claim incremental vegetation management costs of \$2.51M because it had "sufficient GRC funds to cover these incremental vegetation management costs."¹⁰

Response to Finding 1 The Draft Report Recommendation Fails to Include a Crucial Fact, Fails to Calculate Incremental Costs on an Annual Basis, and Utilizes a Definition of Incremental Costs that Has Been Rejected by the CPUC.

Finding 1 is fundamentally flawed in several respects. The Auditors failed to correctly apply the CPUC's definition of "incremental costs," and failed to disclose and apply a crucial fact in determining "incremental costs" of Bear Valley's vegetation management costs. These failures render invalid the Auditors' conclusions and Recommendations in Finding 1.

Wrong Definition of Incremental Costs Is Used. The Draft Report fails to properly cite, and then apply, the CPUC's criteria of what constitutes "incremental costs" for purposes of cost recovery. The Draft Report uses as its base amount in rates a combination of *overall* O&M costs plus *overall* capital costs adopted in Bear Valley's most recent GRC *over a three-year period*. This approach to determining "incremental costs" is fundamentally flawed in two respects.

First, the Draft Report fails to follow proper CPUC criteria of determining incrementality of costs in rates -- which is on a single-calendar-year basis, not multiple years. And second, the Draft Report fails to follow proper CPUC criteria to determine incremental vegetation management costs, which requires a comparison of (i) the amount of vegetation management costs in rates for a given year to (ii) actual vegetation management costs incurred for that given year (*i.e.*, to compare *specific category* of costs in rates vs. *specific category* of costs actually incurred). Whether one or both of these failures are considered, the results are the same -- the Draft Report Finding 1 and the corresponding Recommendations 1 are invalid.

CPUC Has Rejected Use of Overall O&M Costs To Determine Incremental Costs of a Specific Category of Costs. Using the approach of comparing *overall* O&M spending to *overall* O&M costs in rates to determine incremental costs has been specifically rejected by the CPUC.

¹⁰ Draft Report at p. 17.

In a recent CPUC case, a utility sought recovery of certain vegetation management costs despite having spent less in total O&M expenses than total O&M costs in base rates. The CPUC was urged to deny the request for recovery of vegetation management costs as incremental due to overall “unspent” O&M funds. The CPUC rejected that approach to determining incremental costs, concluding that a *specific* category of costs (*e.g.*, vegetation management costs) in rates must be compared to the actual costs incurred for that *specific* category of costs (*i.e.*, actual vegetation management costs). Thus, the Draft Report has failed to use proper CPUC criteria for determining whether BVES incremental vegetation management costs are subject to cost recovery in a future CPUC proceeding.

Failure to Disclose and Apply CPUC-Approved Costs for Vegetation Management Lead to Different Conclusion. Another critical, and inexplicable, deficiency in Finding 1 is the Auditor’s failure to utilize, *or even disclose*, a key fact in its Draft Report. In Bear Valley’s most recent GRC, the CPUC approved a settlement agreement that included an annual amount in base rates of \$338,793 specifically for vegetation management costs. This base rate amount was established as the basis to calculate Bear Valley’s incremental vegetation management costs. Applying the correct CPUC definition for incremental costs and the \$338,793 as the proper amount of vegetation management costs in base rates, it is abundantly clear that any actual vegetation costs that exceed \$338,793 in any of the calendar years 2018, 2019 or 2020 are incremental and eligible for cost recovery, subject to confirmation in a future CPUC cost-recovery proceeding.

Finding 1 and the Associated Recommendation Should be Removed Entirely from the Draft Report. Given the fundamental deficiencies set forth above, Finding 1 should be deleted from the Final Audit Report as it is clearly wrong on the facts and the law. Furthermore, the Auditors did not take exception with the appropriateness or validity of the vegetation management costs incurred by Bear Valley – only how to characterize it in the context of “incremental costs.” Alternatively, if the Auditors should decide to substantially revise its Finding 1 to address its fundamental deficiencies, all language declaring that Bear Valley’s vegetation costs are not incremental should be deleted as that issue is for the Commission to decide in a future cost-recovery proceeding. Attempting to preempt Bear Valley from seeking to have the CPUC determine whether its vegetation costs are incremental with this Audit is misguided and contrary to CPUC practice. Final determination of incrementality of costs for cost recovery is reserved

exclusively to the CPUC in a CPUC-administered cost-recovery proceeding, not an audit conducted by a third-party contractor.

Recommended Summary of BVES Comments. Below is a summary of Bear Valley's concerns regarding Finding 1. BVES recommends and authorizes the summary to be copied verbatim and inserted into the final Audit Report:

BVES believes Finding 1 is fundamentally flawed. BVES objects to Finding 1 defining "incremental costs" by aggregating *overall* O&M costs plus *overall* capital costs adopted in Bear Valley's most recent GRC *over a three-year period* and comparing that amount to *actual overall O&M costs plus overall capital costs incurred over that three-year period*. This definition of "incremental costs" is inconsistent with the CPUC's definition as confirmed in Commission decisions of "incremental costs" which compares the amount of a *specific category* of costs in a *single year's* rates to the actual amount of costs incurred for that *specific category* of costs for that *single year*. BVES also claims that the Auditor failed to include in Finding 1 the critical fact that in Bear Valley's most recent GRC the CPUC approved a settlement that contained \$338,793 in annual rates specifically for vegetation management costs. BVES claims that had the Auditor applied the CPUC definition of "incremental costs" it would have concluded that any actual vegetation costs that exceed \$338,793 in any of the calendar years of 2018, 2019 or 2020 are incremental, subject to confirmation in a future CPUC proceeding to recover such costs. BVES claims that Finding 1, along with its Recommendation that BVES should not include the 2019 and 2020 incremental vegetation management costs for future CPUC rate recovery, should be withdrawn or rescinded.

Finding 2 BVES Incurred Wildfire Mitigation Plan (WMP) Preparation Costs Required to Rework and Resubmit the WMP Following the CPUC's Rejection of the Original WMP.

BVES utilized a third-party vendor to assist in preparing its WMP filed on February 7, 2020. This WMP was ultimately rejected ("Rejected 2020 WMP"). Bear Valley also utilized a third-party vendor to assist in preparing a revised WMP, which was submitted on September 18, 2020 and ultimately approved ("Refiled 2020 WMP"). The Auditors identified costs paid to a third-party vendor to assist in the preparation of the Refiled 2020 WMP, and recommended BVES should not include such costs as incremental for future funding in a subsequent CPUC proceeding.¹¹

¹¹ Draft Report at p. 19.

Response to Finding 2 BVES Did Not Pay Vendor for Work on the Rejected 2020 WMP; BVES Only Paid Vendor for Work on the Refiled 2020 WMP That Was Ultimately Approved.

Based on discussion between BVES and the Auditors at the exit interview for this Audit, it appears that the Auditors mistakenly believed that BVES paid a third-party vendor for preparation of *both* the Rejected 2020 WMP as well as the Refiled 2020 WMP, and that those amounts were recorded in the audited memorandum account. As explained at the exit interview, that is not true.

BVES Only Paid for Work on the Refiled 2020 WMP. In the exit interview with the Auditors, BVES explained that it ultimately did not compensate the vendor for work on the Rejected 2020 WMP. It only compensated the vendor for work on the Refiled 2020 WMP, which was approved.

In the exit interview, the Auditors concurred with Bear Valley's approach to only pay the third-party vendor for preparation of the Refiled 2020 WMP. Given the fact that BVES ultimately did not compensate the vendor for work on the Rejected 2020 WMP, Bear Valley requests that the auditor withdraw or rescind Finding 2 in its entirety.

Recommended Summary of BVES Comments. Below is a summary of Bear Valley's concerns regarding Finding 2. BVES recommends and authorizes the summary to be copied verbatim and inserted into the final Audit Report:

BVES believes that Finding 2 in the Draft Report was based on a misunderstanding regarding the facts surrounding the costs for the preparation of the 2020 WMP. BVES ultimately did not compensate any vendor for work on the Rejected 2020 WMP. It only compensated vendors for work on the Refiled 2020 WMP, which was approved. In the exit interview with BVES, the Auditors concurred with Bear Valley's approach to only pay vendors for work on the Refiled 2020 WMP. BVES requests that the Auditors withdraw or rescind Finding 2 in its entirety.

Finding 3 BVES Incurred Unsubstantiated Legal Expenses in Incremental Wildfire Mitigation Expenses for Wildfire Mitigation Plan (WMP) Preparation/Review Costs.

The Auditors attempted to audit legal costs booked into Bear Valley's Wildfire Mitigation Memorandum Account over the period of 2018 through 2020. As part of the audit, the Auditors requested detailed support for 11 legal services invoices. Consistent with practices

utilized in prior CPUC proceedings, BVES provided redacted copies of the requested 11 legal invoices. The redacted invoices provided the name of the law firm, the date of the invoice, and the total amount of the invoice. Each invoice had a notation that the redacted material was privileged under California Evidence Code Section 954. The Draft Report concluded the information provided by BVES was insufficient to justify the legal expenses incurred by BVES and recorded in the memorandum account.¹²

Response to Finding 3 Auditors' Demand for Copies of BVES Legal Invoices Is Contrary to California Law; Auditors Improperly Recommend CPUC Rejection of WMP Legal Costs.

The redacted invoices provided to the Auditors included the name of the law firm, the date of the invoice, and the total amount of the invoice. The Auditors confirmed that BVES had indicated that those legal expenses were for WMP activities. BVES advised the Auditors that legal invoices are protected by the attorney-client privilege, and redacted legal invoices have been accepted in previous CPUC proceedings. Consistent with prior CPUC practice, BVES believes that, taken together, this information provides sufficient basis for the CPUC to conclude that the legal costs incurred by BVES were reasonable.

In the exit interview, after explaining its position, BVES asked what additional information would satisfy the needs of the Auditors with regard to these invoices. Based on that conversation, it is Bear Valley's understanding that, in essence, the Auditors indicated that unredacted copies of the requested legal invoices would be necessary to meet its auditing requirements, and that anything less than that was insufficient. Based on that understanding, BVES declined to provide the requested legal invoices.

Protection of California Attorney-Client Privilege Is Paramount. The attorney-client privilege protecting a client's communication with its attorneys has been a well-established part of American jurisprudence for over 400 years. The California attorney-client privilege, codified in California Evidence Code Section 954, prohibits a client from being ordered to disclose attorney-client privileged communication. The California Supreme Court has declared invoices for legal work are communications protected by the attorney-client privilege.

¹² Draft Report at p. 20.

In addition, the California Supreme Court has also concluded that a communication that is protected by the attorney-client privilege is not subject to breach through the extraordinary power of an “in camera” review. An auditor retained by a public agency, regardless of any claims of confidentiality or auditing standards by the auditor, has no legal authority to demand disclosure of attorney-client privileged communications.

Providing Legal Invoices to the Auditors Would Result in Waiver of Privilege. In the event BVES were to comply with the Auditors’ demand, it would likely be deemed a waiver of Bear Valley’s privilege, thereby making the invoices vulnerable to further discovery. To be clear, BVES has not waived its attorney-client privilege with respect to its legal invoices beyond the redacted forms provided for this audit.

Despite CPUC Statutory Authority To Compel Discovery, It Has No Authority to Require Disclosure of Attorney-Client Privileged Communications. It is beyond dispute that the attorney-client privilege applies to California agencies, including the CPUC. Even in light of the broad statutory power of the CPUC to compel discovery, the California Supreme Court has declared that such power must be tempered by the attorney-client privilege, concluding specifically that the CPUC’s powers are subject to the attorney-client privilege. The California Supreme Court recognized that application of the privilege will occasionally shield relevant information, which may very well create obstacles for agencies in carrying out their duties. The Court concluded, however, that both the Legislature and the courts of California have determined that such obstacles are outweighed by the importance of preserving the confidential communications that arise as a result of an attorney-client relationship.

To overcome any claims for protection under the attorney-client privilege, the CPUC has urged the California Supreme Court to consider the importance of the CPUC’s efforts to assure that a utility’s expenses are reasonable. Although the California Supreme Court acknowledged that important effort, it nevertheless concluded that such efforts may not come at the unnecessary expense of the protection of attorney-client communications. The Court observed that if it were to accede to the CPUC’s request to have the right to demand privileged information whenever an application to recover costs involved a legal issue, it would drastically impinge on a utility’s ability to obtain legal advice.

According to the California Supreme Court, a client would be much less likely to divulge all pertinent information to its attorneys if it knew that the CPUC would have access to attorney-client communications. Ultimately, the Court concluded that requiring a utility to waive its rights to attorney-client privileged communications would make it very difficult for the utility and its attorneys to openly discuss matters which might eventually lead to litigation. In rejecting the CPUC's position, the Court noted that in a complicated society that is governed by complex and detailed laws, expert legal advice is crucial. The California Supreme Court upheld the utility's attorney-client privilege and vacated the CPUC's order requiring the utility to either produce the confidential information or withdraw its application.

Auditor Should Expressly Recognize Legal Invoices Are Protected by Attorney-Client Privilege. Finding 3 of the Draft Report should be revised in the Final Report to expressly recognize that Bear Valley's legal invoices are protected by California's attorney-client privilege. BVES would not object if the auditor added a statement that, in accordance with its auditing standards, it was unable to sufficiently satisfy itself that the legal expenses reflected by the legal invoices were for WMP-related matters.

In any event, the Auditors should withdraw or rescind their Recommendation that the CPUC should not include any of Bear Valley's WMP legal expenses as incremental for future funding in a subsequent CPUC proceedings, as such a rate-making recommendation to the CPUC is beyond the scope of the audit and the Auditors' expertise. The final decision of what costs, if any, are incremental and subject to recovery is exclusively a CPUC decision made in a CPUC cost-recovery proceeding.

Recommended Summary of BVES Comments. A summary of Bear Valley's concerns regarding Finding 3 is set forth below. BVES recommends and authorizes the summary to be copied verbatim and inserted into the final Audit Report:

BVES objects to the request for unredacted legal invoices. BVES states that California law has long recognized the preeminence of protecting attorney-client privileged communications, and that those protections apply to CPUC proceedings, as well as to invoices for legal services. BVES claims that the CPUC has previously approved of legal costs without violating the protections of attorney-client privileged communications. BVES requests that Finding 3 either be rescinded in its entirety or substantially revised to recognize the sanctity of attorney-client privileged communications which includes legal invoices. BVES does not object to the Auditors noting that without unredacted copies of legal invoices the Auditors

are unable to satisfy their auditing requirements to confirm the validity of Bear Valley's WMP legal costs. In any event, BVES requests that the recommendation that the CPUC should not include any of Bear Valley's WMP legal costs in any subsequent CPUC proceeding be withdrawn or rescinded, as recommendations regarding CPUC ratemaking matters is beyond the scope of the audit.

Finding 4 Wildfire Mitigation Cost Categories Provided in WMPs Do Not Align with How Wildfire Costs are Categorized and Adopted as part of GRCs, Making it Difficult to Monitor Incremental Wildfire Mitigation Costs.

The Draft Report observes that there is insufficient alignment between categories of costs in Bear Valley's WMP as compared to cost categories in Bear Valley's GRC. The Draft Report recommends that as part of the WMP process BVES should provide WMP costs separately for capital and operating expenditures at a program level that are equivalent to, or can be easily reconciled to, the program level Bear Valley uses in its GRC and RSARs.¹³

Response to Finding 4 Insufficient Alignment of WMP Costs and GRC Costs Are Due to Timing Issues; BVES Intends to Better Align Costs in Its Upcoming GRC Application.

BVES recognizes that it is challenging to reconcile costs in its GRC with costs in its WMPs. The cost categories and other supporting data for Bear Valley's 2018 GRC (which was filed in early 2017) were prepared years in advance of preparation of its 2019 WMP. BVES contends that this Finding is primarily attributable to timing considerations.

Consistent with the observations in the Draft Report, BVES intends to better align cost categories in its upcoming GRC application to facilitate comparison with costs in its WMPs.

Recommended Summary of BVES Comments. A summary of Bear Valley's response to Finding 4 is set forth below. BVES recommends and authorizes the summary to be copied verbatim and inserted into the final Audit Report:

BVES recognizes that it is challenging to reconcile costs in its GRC as compared to costs in its WMPs. The cost categories and other supporting data for Bear Valley's 2018 GRC were prepared years in advance of preparation of its 2019 WMP. BVES intends to better align cost categories in its upcoming GRC application to facilitate comparison with costs in its WMPs.

¹³ Draft Report at p. 21.

Delete All References to PG&E in Draft Report

There are number of instances where “PG&E” is referred to in the Draft Report. It is unclear to BVES how anything relating to PG&E is relevant in a BVES audit. BVES urges that the Final Report either explain why PG&E is relevant to the audit of BVES or delete all references to “PG&E” in the audit Final Report.

Conclusion

Bear Valley appreciates the opportunity to provide comments on the Draft Report, and hopes that the Auditors will make substantive changes in the Final Report that reflect our well-founded concerns.

BVES objects to any recommendation in the Draft Report regarding CPUC ratemaking. Those issues are beyond the scope of the audit and the Auditors’ expertise. Finding 1 is fundamentally flawed in a number of respects. There are clearly incremental vegetation management costs consistent with the CPUC’s definition of “incremental costs.” Finding 1 should be withdrawn or rescinded entirely. Finding 2 is predicated upon a misunderstanding of the facts. Once clarified during the exit interview, the Auditors concurred with Bear Valley’s approach to only pay the vendor that assisted with the Refiled 2020 WMP. Therefore, Finding 2 should be withdrawn or rescinded entirely. Finding 3 ignores California law and CPUC practice regarding invoices for legal costs. Finding 3 should be substantially revised to recognize the sanctity of attorney-client privileged communications. BVES would not object if the auditor noted that without unredacted copies of the legal invoices that the auditor is unable to satisfy its auditing requirements to confirm the validity of Bear Valley’s WMP legal costs.

Sincerely,

Paul Marconi,
President BVES, Inc.

Digitally signed by Paul
Marconi, President BVES, Inc.
Date: 2021.11.17 15:13:19
+08'00'

Paul Marconi
BVES President, Secretary and Treasurer

Cc: Koko Tomassian, Energy Safety
Caroline Thomas Jacobs, Energy Safety
Edward Chavez, Energy Safety