Decision 12-12-034 December 20, 2012

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

Application of Southern California Edison Company (U338E) for Authority to Establish Its Authorized Cost of Capital for Utility Operations for 2013 and to Reset the Annual Cost of Capital Adjustment Mechanism.	Application 12-04-015 (Filed April 20, 2012)
And Related Matters.	Application 12-04-016 Application 12-04-017 Application 12-04-018

Angelica M. Morales, Attorney at Law, for Southern California Edison Company, applicant.
Laura M. Earl, Attorney at Law, for San Diego Gas & Electric Company, applicant.
Kim F. Hassan, Attorney at Law, for Southern California Gas Company, applicant.
Peter Van Mieghem, Attorney at Law, for Pacific Gas and Electric Company, applicant.
Marcel Hawiger, Attorney at Law, for The Utility Reform Network, interested party.
John Cummins, Attorney at Law, for Federal Executive Agencies;
Evelyn Kahl, Alcantar & Kahl, Attorney at Law, for Energy Producers and Users Coalition, interest party.
L. Jan Reid, for self, interested party.
Norman A. Pedersen, Attorney at Law, Hanna and Morton, LLP, for Southern California Generation Coalition, interested party.
Jonathan Bromson, Attorney at Law, for the Division of Ratepayer Advocates.

DECISION ON TEST YEAR 2013 COST OF CAPITAL FOR THE MAJOR ENERGY UTILITIES

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DECISION ON TEST YEAR 2013 COST OF CAPITAL FOR THE MAJOR ENERGY UTILITIES

1. Summary

This decision establishes the 2013 ratemaking return on common equity (ROE) and return on rate base (ROR) for Southern California Edison Company (SCE), San Diego Gas & Electric Company (SDG&E), Southern California Gas Company (SoCalGas) and Pacific Gas and Electric Company (PG&E). The test year 2013 authorized ROE, ROR and resulting revenue requirement reduction is as follows.

UTILITY	Return on Common Equity	Return on Rate Base	Reduction in Revenue Requirement
SCE[1]	10.45%	7.90%	$217 Million
SDG&E[2]	10.30%	7.79%	$ 34 Million
SoCalGas[3]	10.10%	8.02%	$ 22 Million
PG&E[4]	10.40%	8.06%	$237 Million

This reduction in revenue requirement is estimated to reduce the utility's average residential customer's monthly bill as follows.

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[1] Late-filed Hearing Exhibit 150 shows that a 10 basis point change (a one basis point change equals 0.01%) in SCE's authorized ROE equates to a $16.8 million revenue requirement change and a $0.20 change in an average residential customer monthly bill using 600 kilowatt-hours of electricity. The overall revenue requirement reduction is revised upward and average residential bill change downward to $0.16 per 10 basis point change pursuant to its opening comments on the proposed decision.

[2] Late-filed Hearing Exhibit 151 shows that a 10 basis point change in SDG&E's authorized ROE equates to a $3.4 million ($2.8 million electric and $.6 million gas) revenue requirement change and, a $0.04 change in an average residential customer monthly bill using 500 kilowatt-hours of non-core inland electricity and $0.02 change in an average residential customer monthly bill using 33 therms of gas. The overall revenue requirement reduction is revised upward pursuant to its opening comments on the proposed decision.

[3] Late-filed Hearing Exhibit 152 shows that a 10 basis point change in SoCalGas' authorized ROE equates to a $2.6 million revenue requirement change and a $0.03 change in an average residential customer monthly bill using 38 therms of gas. The overall revenue requirement reduction is revised upward pursuant to its opening comments on the proposed decision.

[4] Late-filed Exhibit 153 shows that a 10 basis point change in PG&E's authorized ROE equates to a $17 million ($13 million electric and $4 million gas) revenue requirement change and, a $0.08 change in an average electric residential customer monthly bill using 550 kilowatt-hours of electricity and $0.04 change in an average gas residential customer monthly bill using 37 therms of gas. The overall revenue requirement reduction is revised upward pursuant to its opening comments on the proposed decision.

UTILITY/SERVICE	AVERAGE MONTHLY USAGE	AVERAGE MONTHLY SAVINGS
SCE/Electric[5]	600 kilowatt-hours	$1.52
SDG&E/Electric	500 kilowatt-hours/noncore	$ .32
SDG&E/Gas	33 therms	$ .16
SoCalGas/Gas	38 therms	$ .22
PG&E/Electric	550 kilowatt-hours	$ .76
PG&E/Gas	37 therms	$ .38

This proceeding remains open to address modifications to the multi-year cost of capital mechanism adopted by Decision 08-05-035 for use in the two years between the energy utilities' triennial cost of capital applications.

2. Jurisdiction and Background

Applicants are public utilities subject to the jurisdiction of this Commission as defined in Section 218 of the Public Utilities Code.[6] Southern California Edison (SCE), a California corporation and wholly owned subsidiary of Edison International, provides electric service principally in southern California. San Diego Gas &Electric (SDG&E), a California corporation wholly owned by Sempra Energy, provides electric service in a portion of Orange County and electric and gas services in San Diego County. Southern California Gas Company (SoCalGas), a California corporation wholly owned by Sempra Energy, provides gas services throughout Central and Southern California from

[5] The differences between SCE's monthly bill change and those of the other utilities result from differences in rate base per customer served and the percentage of the total revenue requirement that is allocated to residential customers.

[6] All statutory references are to the Public Utilities Code unless otherwise stated.

Visalia to the Mexican border. Pacific Gas and Electric Company (PG&E), a California corporation, provides electric and gas services in northern and central California.

Three of the four utilities filed applications on April 20, 2012 for authority to reduce their Returns on Equity (ROEs). SCE seeks to reduce its ROE to 11.10% from 11.50%, SDG&E to 11.00% from 11.10% and PG&E to 11.00% from 11.35%. On the same day, SoCal Gas filed an application for authority to increase its ROE to 10.90% from 10.82%. SDG&E, SoCalGas and PG&E also propose to change their respective capital structures while SCE proposes to maintain its currently authorized capital structure.

3. Capital Structure

Capital structure consists of long-term debt, preferred stock, and common equity.[7] Because the level of financial risk that the utilities face is determined in part by the proportion of their debt to permanent capital, or leverage, we must ensure that the utilities' adopted equity ratios are sufficient to maintain reasonable credit ratings and to attract capital.

3.1. SCE

SCE seeks a test year 2013 ratemaking capital structure of 43.00% long-term debt, 9.00% preferred stock, and 48.00% common equity. This is the same capital structure that it is currently authorized.

Except for the Federal Executive Agencies (FEA), all parties[8] concur with SCE's proposed capital structure. FEA recommends that SCE's capital structure should be set more in line with the average capital structure that SCE has

[7] Debt due within one year, short-term debt, is excluded.

[8] Parties consist of all appearances of record.

actually used over the most recent five quarters (from March of 2011 through March of 2012), a capital structure consisting of 48.00% common equity, 7% preferred stock and 45% long-term debt.

FEA's capital structure adjustment of a 2% reduction in SCE's preferred stock ratio with a corresponding increase in long-term debt is based on recorded long-term debt found in SCE's quarterly reports filed with the Securities and Exchange Commission (SEC).[9] However, FEA's capital structure analysis is flawed because recorded long-term debt is not the same long-term debt used for SCE's ratemaking capital structure.

Two adjustments must be made to the recorded long-term debt reported to the SEC to arrive at SCE's California ratemaking capital structure. These ratemaking adjustments are: (1) to exclude recorded long-term debt balances supporting nuclear fuel inventories, which is recoverable in the energy resource recovery account proceedings and excluded from ratemaking rate base; and, (2) to amortize recorded long-term debt financing issuance costs over the life of each security issued.[10] After these adjustments are made, SCE's debt ratio is in line with SCE's average and requested capital structure. We find SCE's requested capital structure reasonable and we will adopt it.

3.2. SDG&E

SDG&E seeks a test year 2013 ratemaking capital structure consisting of 45.25% long-term debt, 2.75% preferred stock, and 52.00% common equity. This is a 3.00% increase in its common equity ratio and a corresponding decrease in its

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[9] Hearing Exhibit 30 at 86 and Schedule 10 at 6.

[10] Hearing Exhibit 19 at 19.

preferred stock ratio from its currently authorized capital structure. SDG&E's requested capital structure is intended to preserve its strong "A" investment grade credit rating of long-term debt, to attract long-term debt at low costs, and to maintain financial strength for the long-term management of its capital investment program, expected to average over $1.1 billion per year during the 2013-2015 years.[11] This capital structure is also intended to support SDG&E's current credit rating while mitigating the need for SDG&E to take on more debt for its pending Application (A.) 11-05-023, which seeks authority to enter into Purchase Power Tolling Agreements with the Pio Pico Energy Center and Quail Brush Power peaker plant facilities.[12]

Except for FEA, all parties concur with SDG&E's proposed capital structure. FEA opposes SDG&E's requested 3% increase in common equity because: (1) it is not in line with the average common equity ratio of 48.60% that SDG&E has actually used over the most recent five quarters (from March of 2011 through March of 2012); (2) SDG&E's requested capital structure shifts more costs to ratepayers; (3) SDG&E can issue first mortgage debt that has an "AA" rating; and, (4) SDG&E's parent company, Sempra Energy, raised its dividend earlier this year by 25%, which represented a transfer of significant capital.[13]

FEA recommends that SDG&E's proposed 3% increase in its common equity ratio be split evenly between long-term debt and common equity, resulting in a capital structure of 46.75% long-term debt, 2.75% preferred stock and 50.5% common equity.

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[11] Hearing Exhibit 4 at 4-8.

[12] Hearing Exhibit 4 at 8.

[13] Hearing Exhibit 30 at 82 and 86-88.

Similar to its flawed capital structure analysis for SCE, FEA failed to adjust recorded long-term debt to compare SDG&E's average ratemaking capital structure to its requested capital structure. SDG&E's actual common equity ratio would have been in line with its requested common equity ratio if FEA had made the appropriate ratemaking adjustments to SDG&E's recorded long-term debt, as highlighted in the following tabulation.[14]

	FEA Recorded Debt	SDG&E Adjusted Debt	SDG&E Requested Structure
Long-term Debt	50.37%	47.16%	45.25%
Preferred Stock	1.04%	1.13%	2.75%
Common Equity	**48.60%**	**51.71%**	**52.00%**
Total	100.00%[15]	100.00%	100.00%

We find SDG&E's requested 3.00% increase in its common equity ratio and a corresponding decrease in its preferred stock ratio from its currently authorized capital structure would shift more costs to ratepayers. This is because common equity financing is more costly than long-term debt and preferred stock financing. Ratepayers receive the most benefit from the use of long-term debt financing because debt is less costly and it is tax-deductible. Preferred stock has qualities of both debt and equity financing and is treated by credit rating agencies as a hybrid of debt and equity.[16] However, as long-term debt ratios are increased, credit ratings tend to be downgraded which results in increased

[14] Hearing Exhibit 8 at Attachment A.

[15] Difference between the 100.00% total and the adding of individual percentages (100.01%) is due to rounding the percentages.

[16] Hearing Exhibit 4 at 16.

financial risks for common equity holders, thereby requiring greater returns on common equity.

SDG&E has strong investment grade credit ratings.[17] However, the dividend policy of SDG&E's parent company is not relevant in this proceeding. What is relevant is SDG&E's actual experience of paying dividends to Sempra Energy. Due to SDG&E's large capital program, its dividend plans have been suspended for several recent years. In fact, SDG&E has received more common equity inflows from its parent than it has provided in dividends since 2008. While SDG&E paid $150 million of common stock dividends in 2009, SDG&E received $200 million of common equity from Sempra Energy in 2011. SDG&E did not pay any common stock dividends in 2008, 2010, 2011, and 2012.[18]

SDG&E's current credit ratings of "A" from Standard & Poor (S&P) and A2 from Moody's are one step stronger than Division of Ratepayer Advocates' (DRA) proxy group average S&P credit rating of A-/BBB+ and average Moody's credit rating of A3/Baa1.[19]

Although S&P has imputed $182 million of debt equivalence[20] into SDG&E's long-term debt in June 2011, SDG&E expects S&P to increase imputed debt equivalence into its long-term debt ten-fold, in excess of $1.6 billion. Approximately $772 million, or almost half of the expected debt equivalence, is expected to occur as a result of future contracts pending Commission approval.[21]

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[17] Hearing Exhibit 5 at 11.

[18] Hearing Exhibit 8 at 5-6.

[19] Hearing Exhibit 5 at 11 and Exhibit 24, Attachment JRW-4 at 1.

[21] Hearing Exhibit 4 at 10.

This expected debt equivalence increase is due to including financial statement consolidation of SDG&E's pending purchase power tolling agreements pursuant to Accounting Standards Codification 810 (ASC 810), formerly referred to as Financial Accounting Standards Board Interpretation No. 46 R.[22]

Credit agencies do not use a standard method to calculate long-term debt equivalence. S&P's uses a risk factor of 50% as a generic guideline for utilities with PPAs included as an operating expense in base tariffs and lowers that risk factor to 25%, as appropriate, when purchased power costs may be recovered via a fuel-adjustment clause.[23] Moody's employs a different methodology in assessing utility PPAs. In certain cases, Moody's would not impute any debt and in other cases consider PPAs as a positive risk mitigation factor.[24] Moody's recognizes that PPAs have been used by utilities as a risk management tool. Thus, it will not automatically penalize utilities for entering into contracts for the purpose of reducing risk associated with power price and availability. Moody's look at the aggregate commercial position, evaluating the risk to a utility's purchase and supply obligations. In addition, PPAs are considered by Moody's to be similar to long-term supply contracts used by other industries and their

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[22] ASC 810 is a generally accepted accounting principal that requires an entity such as SDG&E having a controlling financial interest in another entity, such as its proposed purchase power tolling agreements, to consolidate those other entities into the financial statements of the controlling financial entity.

[23] Hearing Exhibit 24 at 3-21.

[24] Reporter's Transcript, Volume 1 at 79 lines 23-26, and 81 lines 2-7.

treatment should not therefore be fundamentally different from that other contracts of a similar nature.[25]

The Commission has previously reasoned that the utilities should be given some discretion to manage their capitalization with a view towards a balance between shareholders' interest, regulatory requirements, and ratepayers' interest.[26] In this case, SDG&E seeks a common equity ratio for its revenue requirement which is the same as its actual common equity ratio. We concur with SDG&E and find a 46.25% long-term debt, 2.75% preferred stock and 52.00% common equity capital structure reasonable and we adopt it.

3.3. SoCalGas

SoCalGas seeks a test year 2013 ratemaking capital structure of 45.60% long-term debt, 2.40% preferred stock, and 52.00% common equity. This is a 4.00% increase in its common equity ratio and a corresponding decrease in its preferred stock ratio from its currently authorized capital structure.

Except for FEA, all parties concur with SoCalGas proposed capital structure. FEA recommends that SoCalGas' requested 4% increase in common equity be split evenly between equity and debt for the same reasons it recommends an even split in SDG&E's requested common equity increase.

However, FEA's analysis of SoCalGas' capital structure contains the same flaws addressed in our prior SCE and SDG&E capital structure discussions and

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[25] Reporter's Transcript, Volume 1 at 80 at lines 2 through 81 at line 1. *See* also Exhibit 38.

[26] 33 CPUC2d (1989) 495 at 541 through 545.

will not be repeated here. It is important to note that SoCalGas' authorized capital structure with a 48% common equity ratio has not changed since 1997.[27]

The Utility Reform Network (TURN) supports SoCalGas' requested equity ratio because the requested 52% common equity ratio is well below TURN's natural gas company proxy group equity ratio.[28] SoCalGas' current "A" credit rating by S&P and "A2" credit rating by Moody's is in the same range as TURN's natural gas company proxy group, which averages an "A" credit rating by both S&P and Moody's.[29] Approval of SoCalGas' requested 52% common equity ratio will bring its capital structure closer to the gas industry average. At the same time, a lower preferred stock ratio will reduce SoCalGas' perceived financial risk because credit rating agencies treat preferred stock as a hybrid of debt and equity.[30] We find SoCalGas' requested capital structure reasonable and we adopt it.

3.4. PG&E

PG&E seeks a test year 2013 ratemaking capital structure of 47.00% long-term debt, 1.00% preferred stock, and 52.00% common equity. This is a 1.00% increase in its long-term debt ratio and a corresponding decrease in its preferred stock ratio from its currently authorized capital structure. There is no opposition to PG&E's proposed capital structure and we adopt it.

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[27] 69 CPUC2d (1996) 327 at 350.

[28] Hearing Exhibit 26 at 82 and Exhibit 27, Schedule DJL-18.

[29] Hearing Exhibit 13 at 10 and Exhibit 27, Schedule DJL-18.

[30] Hearing Exhibit 4 at 16, and Reporter's Transcript, Volume 1 at 89, lines 10-23.

3.5. Summary

The capital structures requested by SCE, SoCalGas and PG&E and SDG&E's capital structure recommended by FEA are balanced, attainable and are intended to maintain an investment grade rating and to attract capital. For these reasons, we find that the capital structures shown below are fair, consistent with law, in the public interest and should be adopted. The adopted capital structures are detailed in the following tabulation:

CAPITAL RATIO	SCE	SDG&E	SoCalGas	PG&E
Long-term Debt	43.00%	46.75%	45.60%	47.00%
Preferred Stock	9.00%	2.75%	2.40%	1.00%
Common Equity	48.00%	50.50%	52.00%	52.00%
Total	100.00%	100.00%	100.00%	100.00%

The next step in determining a fair ROE is to establish reasonable long-term debt and preferred stock costs.

4. Long-term Debt and Preferred Stock Costs

Long-term debt and preferred stock costs are based on actual, or embedded, costs. Future interest rates must be anticipated to reflect projected changes in a utility's cost caused by the issuance and retirement of long-term debt and preferred stock during the year. This is because the ROE is established on a forecast basis.

We recognize that actual interest rates do vary and that our task is to determine "reasonable" debt cost rather than actual cost based on an arbitrary selection of a past figure.[31] In this regard, we conclude that the latest available

[31] 38 CPUC2d (1990) 233 at 242 and 243.

interest rate forecast should be used to determine embedded debt cost in cost of capital proceedings. Consistent with this conclusion, the assigned Commissioner's Scoping Memo and Ruling allowed the utilities to update their long-term debt and preferred stock costs based on Global Insight's September 2012 forecasted interest rates for 2013. That update was submitted on October 9, 2012 as late-filed Exhibits 150, 151, 152 and 153 by SCE, SDG&E, SoCalGas and PG&E, respectively.

4.1. SCE

SCE projected its test year 2013 long-term debt cost to be 5.53%. SCE started with its recorded embedded costs as of the end of February 2012 and then incorporated its current projection of long-term debt to be issued through the end of 2013, consisting of $850 million of new long-term debt issuance in 2012 and $625 million of new long-term debt issuance in 2013. Embedded costs for 2013 are estimated as the average of projected embedded cost at the beginning of 2013 and the end of 2013.

Based on its late-filed exhibit that updated the impact of the most recently forecasted interest rates, SCE increased its new long-term debt issuance in 2013 to $725 million from $625 million and decreased its forecasted long-term debt cost to 5.49% from 5.53%.[32] This revised rate is 73 basis points lower than the 6.22% long-term debt cost authorized in its test year 2008 cost of capital proceeding.

SCE used that same method to calculate a preferred stock cost of 5.86%. Its forecast provided for the issuance of $400 million new preferred stock in 2012

[32] Late-filed Hearing Exhibit 150.

and $150 million of new preferred stock in 2013. Based on its late-filed exhibit that updated the impact of the most recent forecasted interest rates, SCE increased its new preferred stock issuance to $175 million from $150 million and decreased its forecasted preferred stock cost to 5.79% from 5.86%. This revised rate is 22 basis points lower than the 6.01% preferred stock cost SCE was authorized in its test year 2008 cost of capital proceeding.

4.2. SDG&E

SDG&E projected its test year 2013 long-term debt cost to be 5.09%. That 2013 forecast provides for the issuance of $250 million in new long-term debt. Based on its late-filed exhibit that updated the impact of the most recently forecasted interest rates, SDG&E decreased its forecasted long-term debt to 5.00% from 5.09%. This revised rate is 62 basis points lower than the 5.62% long-term debt cost authorized in its test year 2008 cost of capital proceeding.

SDG&E used that same method to calculate a preferred stock cost of 6.35%. Its forecast provided for an $80 million issuance of preferred stock in test year 2013. Based on its late-filed exhibit that updated the impact of the most recently forecasted interest rates, SDG&E decreased its forecast to 6.22% from 6.35%.[33] This revised rate is 103 basis points lower than the 7.25% preferred stock costs authorized in its test year 2008 cost of capital proceeding.

4.3. SoCalGas

SoCalGas projected its test year 2013 long-term debt cost to be 5.72%. This forecast takes into account $500 million of new long-term debt in 2012 and $350 million in 2013. Based on its late-filed exhibit that updated the impact of the

[33] Late-filed Hearing Exhibit 151.

most recently forecasted interest rates, SoCalGas increased its forecast to 5.77% from 5.72%.[34] This revised rate is 119 basis points lower than the 6.96% currently authorized long-term debt rate.

SoCalGas projected a preferred stock cost of 6.00%, a 117 basis points increase from its currently authorized 4.83% rate. In the absence of any projected issuances or retirements of preferred stock, the forecasted embedded cost of preferred stock is equivalent to the current actual embedded cost. Its late-filed exhibit that updated the impact of the most recently forecasted interest rates has no impact on the cost of preferred stock because its rate is based on the embedded cost of preferred stock and SoCalGas is not planning on retiring or issuing any such stock during the test year.

4.4. PG&E

PG&E projected its test year 2013 long-term debt cost to be 5.69%. PG&E started with its recorded cost of debt as of March 31, 2012, and incorporated projected changes in the amounts or costs of debt outstanding through the remainder of 2012 and 2013. Those changes included $925 million of new long-term debt in 2012 and $1.875 billion of new long-term debt in 2013.

Based on its late-filed exhibit that updated the impact of the most recently forecasted interest rates, PG&E decreased its forecast to 5.52%.[35] This revised rate is 53 basis points lower than the 6.05% long-term debt cost authorized in its test year 2008 cost of capital proceeding.

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[34] Late-filed Hearing Exhibit 152.

[35] Late-filed Hearing Exhibit 153.

PG&E projected its 2013 test year preferred stock cost in the same way it projected its embedded cost of debt. PG&E started with its recorded cost of preferred stock as of March 31, 2012 and incorporated changes for the remainder of 2012 and all of 2013. The only change impacting PG&E's cost of preferred stock is amortization of costs associated with preferred stock previously redeemed. This change results in a preferred stock cost of 5.60%, an 8 basis point decrease from its currently authorized rate of 5.68%. Therefore, the updated forecast of interest rates did not impact its test year preferred stock cost.

4.5. Summary

There is no opposition to the utilities' proposed long-term debt and preferred stock costs for the test year 2013. We have reviewed these undisputed costs which have been updated to reflect the most recent forecasted interest rates and find that the following long-term debt and preferred stock costs for the utilities are consistent with the law, in the public interest and should be adopted.

	SCE	SDG&E	SoCal Gas	PG&E
Long-term Debt	5.49%	5.00%	5.77%	5.52%
Preferred Stock	5.79%	6.22%	6.00%	5.60%

Having determined the appropriate long-term debt and preferred stock costs, we address the appropriate ROE.

5. Return on Common Equity

The legal standard for setting the fair rate of return has been established by the United States Supreme Court in the Bluefield and Hope cases.[36] The

[36] The Federal Power Commission v. Hope Natural Gas Company, 320 U.S. 591 (1944) and Bluefield Water Works & Improvement Company v. Public Service Commission of the State of Virginia, 262 U.S. 679 (1923).

Bluefield decision states that a public utility is entitled to earn a return upon the value of its property employed for the convenience of the public and sets forth parameters to assess a reasonable return.[37] Such return should be equal to that generally being made at the same time and in the same general part of the country on investments in other business undertakings attended by corresponding risks and uncertainties. That return should also be reasonably sufficient to ensure confidence in the financial soundness of the utility, and adequate, under efficient management, to maintain and support its credit and to enable it to raise the money necessary for the proper discharge of its public duties.

The Hope decision reinforces the Bluefield decision and emphasizes that such returns should be sufficient to cover operating expenses and capital costs of the business. The capital cost of business includes debt service and stock dividends. The return should also be commensurate with returns available on alternative investments of comparable risks. However, in applying these parameters, we must not lose sight of our duty to utility ratepayers to protect them from unreasonable risks including risks of imprudent management.

We attempt to set the ROE at a level of return commensurate with market returns on investments having corresponding risks, and adequate to enable a utility to attract investors to finance the replacement and expansion of a utility's facilities to fulfill its public utility service obligation. To accomplish this objective, we have consistently evaluated analytical financial models as a starting point to arrive at a fair ROE.

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[37] Hope held that the value of a utility's property could be calculated based on the amount of prudent investment minus depreciation.

5.1. Proxy Groups

To enhance comparability of the financial modeling results among the parties in energy utilities ROE proceedings, the Commission adopted the Value Line Investment Survey (Value Line) electric industry classifications (includes combination electric and gas companies) for use in energy utilities' ROE proceedings where the financial models require the use of a proxy group.[38] Three basic screens were also adopted in selecting a comparable proxy group. Those screens are: (1) to exclude companies that do not have investment grade credit ratings; (2) exclude companies that do not have a history of paying dividends; and, (3) exclude companies undergoing a restructure or merger. Additional screens are acceptable to the extent that justification is provided.

SCE, SDG&E, SoCalGas, and PG&E started with the Value Line gas and electric utility industry group lists to establish proxy groups of companies for their financial models. PG&E used Value Line's non-utility companies' list for its second proxy group. The utilities then screened those companies to ensure that they were compatible to their respective utility.

The intervenors[39] also used Value Line's gas and electric utility industry group list to establish their respective proxy groups. L. Jan Reid used a total of seven different proxy groups including: all Value Line utilities including water utilities; all Value Line energy utilities; all Value Line western electric and

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[38] Ordering Paragraph 4 of Decision (D.) 07-12-049.

[39] Named intervenors are: the DRA, Energy Producers and Users Coalition (EPUC), FEA, Reid, and TURN.

combination utilities; and the comparable groups used by SCE, SDG&E, SoCalGas and PG&E.[40]

The following tabulation compares the number of entities included in each party's proxy group.

	SCE	SDG&E	SoCalGas	PG&E
Utility	26 Electric	31 Electric 14 Utilities[41]	31 Electric 7 Gas	14 Electric 12 Non-Utility[42]
DRA	34 Electric 8 Gas	34 Electric 8 Gas	34 Electric 8 Gas	34 Electric 8 Gas
EPUC	Same as Utility	not applicable	not applicable	Same as Utility
FEA	16 Electric 7 Gas	16 Electric 7 Gas	16 Electric 7 Gas	16 Electric 7 Gas
Reid	not applicable	not applicable	not applicable	64 Electric, Gas, Water
TURN	Same as Utility	Same as Utility	Same as Utility	Same as Utility

A proxy, by common definition, is a substitute. Hence, companies selected as a proxy group of a utility should have characteristics similar to that utility. In order to ensure comparability and reasonableness of financial modeling results, the utilities and companies selected in the proxy group should be exposed to similar risks.

However, the parties (excluding TURN and EPUC) used different companies for their proxy groups making it difficult to determine which intervenor financial modeling results are comparable to SCE, SDG&E, SoCalGas,

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[40] Hearing Exhibit 33 at 14 and 15.

[41] SDG&E's 14 combined electric and gas company proxy group consists of Value Line's Western utility group.

[42] PG&E used its non-utility proxy group results to demonstrate that the end result of its electric proxy group was consistent with competitive non-utility markets. (Reporter's Transcript, Volume 2 at 197.)

and PG&E financial modeling results. It is further difficult due to the individual parties utilizing numerous variations of the individual financial models which tend to skew a party's individual financial modeling result. For example, SDG&E utilized nine variations while TURN utilized 14.[43] Four of SDG&E's modeling variations were related to the Discounted Cash Flow (DCF) Model, two of the variations were related to including a different number of companies in gas and electric utilities proxy groups. The remaining variations were due to different sources of forecasts, and different projected earnings per share growth forecast.[44] Eight of TURN's modeling variations for SDG&E were applicable to the DCF Model. SoCalGas used the identical number of companies, sources of forecasts, projected earnings per share growth forecasts, and modeling results as SDG&E.[45]

5.1.1. Non-Utility Proxy Group

PG&E utilized a non-utility proxy group to corroborate the results of its energy utility proxy group. In doing so it reasoned that relative risk, not a particular business activity or degree of regulation, should be the salient criteria in establishing a meaningful benchmark to evaluate a fair rate of return.[46]

However, a 250 basis point DCF modeling result differential between its average utility and average non-utility proxy groups leads us to question whether the non-utility proxy group is actually comparable to its utility proxy

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[43] Hearing Exhibit 1 at 65 and Exhibit 26 at 70.

[44] Hearing Exhibit 1 at RAM-2 and RAM-3.

[45] Compare Exhibit 1 at RAM-2 to Exhibit 12 at RAM-4 and Exhibit 1 at RAM 4 to Exhibit 12 at RAM-5.

[46] Hearing Exhibit 21 at 2-15.

group and to PG&E.[47] This is especially true given that non-utility earnings are dependent on the extent of competition and ability to price products or services at rates a buyer is willing to pay while maintaining a competitive edge in comparison to utility earnings being dependent on a fair return on investments with reasonable pricing of utility services, irrespective of what a buyer is willing to pay for a product or service for which they may have no alternative. Therefore, we decline to consider the financial modeling results from PG&E's non-utility proxy group.

We next review the financial models used by the parties to assess the comparability and reasonableness of their results.

5.2. Financial Models

The financial models commonly used in ROE proceedings are the Capital Asset Pricing Model (CAPM), Risk Premium Model (RPM), and DCF Model.[48] Each methodology requires the exercise of considerable judgment on the reasonableness of the assumptions underlying the method and on the reasonableness of the proxies used to validate the theory and apply the method.[49] Detailed descriptions of these financial models are contained in the record and are not repeated here.

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[47] Hearing Exhibit 21 at 2-28 and 2-29 simple average of PG&E's four utility proxy group average DCF modeling results compared to the simple average of its four non-utility proxy group average DCF modeling results.

[48] Evidence was presented on the use of an additional financial model, *Fama French*, which was considered and rejected by the Commission in D.07-12-049 and D.05-12-043. (Hearing Exhibit 33 at 13-15).

[49] Hearing Exhibit 12 at 15.

The application of these financial models is applied to a proxy group of companies comparable to the respective utility. A contributing factor resulting in a wide range of financial modeling results is the parties' difference in the time period and the availability of subjective inputs. While financial modeling results from the utilities were due on April 20, 2012, as part of their applications, intervenors had access to more recent data to use for their subjective inputs because their financial modeling results were not due until three and a half months later on August 6, 2012. It is the result of differences in subjective inputs used in models that result in a wide range of ROEs being recommended by the parties.

5.2.1. Flotation Costs

SDG&E and SoCalGas were the only parties that included flotation costs[50] as a subjective input into their respective financial models, resulting in an upward adjustment in its financial models of approximately 25 basis points.[51] While PG&E did not make an explicit flotation cost adjustment in its financial models, it recommended that such an adjustment be considered in evaluating a ROE for PG&E from within the results of its financial models.[52] The inclusion of flotation costs in the various financial models is not a new issue.

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[50] Flotation costs commonly includes underwriter costs for marketing, consulting, printing and distribution, legal costs and discounts that must be provided to place a new common stock in the open market.

[51] Reporter's Transcript, Volume 1 at 166.

[52] Hearing Exhibit 21 at 2-24. One method identified by PG&E in which a flotation adjustment can be calculated is to make a 5% to 10% upward adjustment to the ROE. This method is based on Roger Morin's "New Regulatory Finance" finance literature, the same person who recommended an approximate 25 basis point adjustment for SDG&E and SoCalGas in this proceeding.

We concluded in D.92-11-047 that any merit to a flotation adjustment would apply only to existing common stock at the time of actual new issuances. We also concluded in that decision that a flotation adjustment is not applicable to sales in the secondary market, and that such an adjustment is inappropriate as long as utility stocks are trading significantly above their book value. We further concluded in that decision that any reconsideration of a flotation adjustment in a future proceeding would require a showing of theoretical, practical, utility and market specific data, and a showing that a flotation cost adjustment does not shift the burden of the transaction costs from investors to ratepayers.[53]

The utilities proposing a flotation adjustment have: (1) not identified any of their actual flotation costs; (2) not identified any new common stock issuances in the test year; and, (3) not demonstrated that their utility stocks are trading at, or below, their book value. Consistent with the reasons set forth in D.92-11-047, we reject consideration of a flotation adjustment in this proceeding. The following financial modeling results and discussions of SDG&E and SoCalGas exclude their flotation adjustments.

5.2.2. CAPM

The CAPM is a risk premium approach that gauges an entity's cost of equity based on the sum of an interest rate on a risk-free bond and a risk premium. Two primary variations to the CAPM were used by the parties, traditional and empirical CAPMs. The empirical CAPM (ECAPM) is designed to include the relationship between *beta*[54] and security returns, which the traditional

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[53] 46 CPUC2d (1992) 319 at 362 and 406.

[54] The term "beta" refers to - a company specific multiplier of general market risk.

CAPM does not. However, the ECAPM tends to produce higher overall cost of capital estimates because adjusting electric utilities' *betas*, which tend to have low *betas*, upward guarantees a higher ROE.[55]

Each party utilized different subjective inputs into their CAPM. For example, the average risk free rate utilized by parties ranged from 2.48% to 4.20% and market risk premium ranged from 5.01% to 9.70%.[56] The following tabulation summarizes the simple average result of the CAPM variations calculated by the individual parties using subjective inputs.[57]

	SCE	SDG&E	SoCalGas	PG&E
Utility	10.70%[58]	10.50 %[59]	10.20%[60]	11.10%
DRA	7.60%	7.60%	7.60%	7.60%
EPUC	8.40%	not applicable	not applicable	8.40%
FEA	7.80%	7.80%	7.80%	7.80%
REID	not applicable	not applicable	not applicable	7.10%
TURN	9.20%	9.20%	9.10%	9.10%

[55] 1 CPUC3d (1999) 146 at 168-169.

[56] Hearing Exhibit 35-A.

[57] All financial modeling results are rounded to a tenth (.001) of a percent.

[58] Excludes SCE's after-tax weighted average cost of capital (ATWACC) adjustments identified in Exhibit 17 at 68-71. Although SCE is not proposing that its ATWACC adjustments be used to directly determine its cost of capital and acknowledges that the Commission rejected ATWACC adjustments (D.04-12-047, mimeo, 40-42 and D.99-06-057 (1 CPUC3d 146 at 169-170)), it nevertheless calculated ATWACC adjustments.

[59] SDG&E's 25 basis point flotation adjustment is excluded. (Reporter's Transcript, Volume 1 at 165-166.)

[60] SoCal Gas' 25 basis point flotation adjustment is excluded. (Reporter's Transcript, Volume 1 at 165-166.)

5.2.3. RPM

Similar to the CAPM, the RPM measures a company's cost of equity capital by adding a risk premium to a risk-free long-term treasury or utility bond yield. A risk premium is derived by an assessment of historic utility stock and bond returns, a historical RPM. A variation to the historical RPM is an allowed RPM which estimates the common equity allowed by regulatory commissions over a period of time in relationship to the level of long-term Treasury bond yield.

Each party utilized different subjective inputs into their RPMs. For example, the average risk premium used by parties ranged from 3.31% to 5.95%, and return on low risk asset from 2.48% to 5.88%.[61] The following tabulation summarizes the simple average result of the RPM variations calculated by the individual parties using subjective inputs.[62]

	SCE	SDG&E	SoCalGas	PG&E
Utility	8.80%[63]	10.20%[64]	10.00%[65]	11.10%
DRA	8.10%	8.10%	8.10%	8.10%
EPUC	9.10%	not applicable	not applicable	9.10%
FEA	7.80%	7.80%	7.80%	7.80%
REID	not applicable	not applicable	not applicable	6.70%
TURN	9.60%	9.60%	9.60%	9.60%

5.2.4. DCF

The DCF model is used to estimate an equity return from a proxy group by adding estimated dividend yields to investors' expected long-term dividend

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[61] Hearing Exhibit 35-A.

[62] All financial modeling results are rounded to a tenth (.001) of a percent.

[63] SCE's result excludes its ATWACC identified in Exhibit 17 at 68-71.

[64] SDG&E's 30 basis point flotation adjustment is excluded. (Exhibit 1 at 52.)

[65] SoCal Gas' 30 basis point flotation adjustment is excluded. (Exhibit 12 at 46-47.)

growth rate. Several DCF variations were used by the parties. These variations included analysts' growth,[66] constant growth,[67] sustainable growth,[68] and multi-stage growth.[69]

Each party utilized different subjective inputs into their various DCF models. For example, the average dividend yield ranged from 3.88% to 4.65% and average growth rate ranged from 4.62% to 5.23%.[70] The following tabulation summarizes the simple average result of different versions of the DCF model calculated by the individual parties using subjective inputs.[71]

	SCE	SDG&E	SoCalGas	PG&E
Utility	9.70%[72]	10.10%[73]	9.10%[74]	9.60%
DRA	8.50%	8.50%	8.50%	8.50%
EPUC	9.10%	not applicable	not applicable	9.30%
FEA	8.90%	8.90%	8.80%	8.90%
REID	not applicable	not applicable	not applicable	8.40%
TURN	9.20%	9.40%	9.20%	9.30%

[66] This is a consensus of analysts 'projections of the annual rate of increase in earnings per share.

[67] The growth rate investors expect over the long term.

[68] Based on percentage of a utility's earnings that is retained and reinvested in utility plant and equipment.

[69] Multi-stage growth reflects the possibility of non-constant growth for a company over time.

[70] Hearing Exhibit 35-A.

[71] All financial modeling results are rounded to a tenth (.001) of a percent.

[72] SCE's ATWACC adjustments identified in Exhibit 17 at 68-71 is excluded.

[73] SDG&E's 21 to 23 basis point flotation adjustment is excluded. (Exhibit 1 at 30–32.)

[74] SoCal Gas' 20 basis point flotation adjustment is excluded. (Exhibit 12 at 25-28.)

5.2.5. Summary

From the results of these broad financial models which are dependent on subjective inputs, the parties advance arguments in support of their respective analyses and in criticism of the input assumptions used by other parties. These arguments will not be addressed extensively in this opinion, since they do not materially alter the modeling results. However, it should be noted that none of the parties agreed with the financial modeling results of the others.

In the final analysis, it is the application of informed judgment, not the precision of financial models, which is the key to selecting a specific ROE estimate. We affirmed this view in D.89-10-031, noting that it is apparent that all these models have flaws and, as we have routinely stated in past decisions, the models should not be used rigidly or as definitive proxies for the determination of the investor-required ROE. Consistent with that skepticism, we found no reason to adopt the financial modeling of any one party. The models are only helpful as rough gauges of the realm of reasonableness.

5.3. Additional Risk Factors

We also consider additional risk factors not specifically included in the financial models. Those additional risk factors fall into three categories: financial, business and regulatory. Of the four utilities, only SDG&E and SoCalGas have requested that a premium be added to their financial modeling results to compensate them for increased financial, business and regulatory risks. SDG&E seeks a 10 basis point premium for changing business and capital investments, to maintain a strong credit rating and continued supportive regulatory environment. SoCalGas seeks a 90 basis point premium to compensate it for a higher risk profile, and increased financial, business and regulatory risks. Both SCE and PG&E reflect the impact of any perceived

increased financial, business and regulatory risk in their selection of specific ROEs within the range of their financial modeling results.

5.3.1. Financial Risk

Financial risk is tied to the utility's capital structure. The proportion of its debt to permanent capital determines the level of financial risk that a utility faces. As a utility's debt ratio increases, a higher return on equity may be needed to compensate for that increased risk. However, in this proceeding, there is minimal change in financial risk because the debt ratios being adopted in this proceeding are not materially changed from the utilities' last authorized debt ratios.[75]

Debt equivalence, raised as a financial risk by the utilities, does have an impact on the financial risk of SCE, SDG&E, SoCalGas, and PG&E.[76] As recognized in D.04-12-047, debt equivalence has been reflected in the utilities' credit ratings since at least 1990. In D.05-12-043, we affirmed that debt equivalence would be assessed on a case-by-case basis along with other financial, regulatory and operational risks in setting a balanced capital structure and fair ROE. Our goal in so doing was, and continues to be, to provide reasonable confidence in the utilities' financial soundness, to maintain and support investment-grade credit ratings, and provide utilities the ability to raise money necessary for the proper discharge of their public duty. We have no reason to change that goal. Debt equivalence is considered in arriving at an overall ROE.

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[75] SDG&E's long-term debt ratio is being increased 1.5% and PG&E's 1.0%.

[76] A discussion of the credit agencies different methods of calculating debt equivalence is addressed in our prior Section 3.2 discussion of SDG&E's capital structure discussion.

5.3.2. Business Risk

Business risk pertains to *new* uncertainties resulting from competition and the economy. An increase in business risk can be caused by a variety of events that include capital investments, electric procurement, and catastrophic events. Each of these business risks overlap into financial and regulatory risk. Capital investment risk is addressed in our subsequent authorized ROE risk discussion (Section 5.3.3.1.) and Electric procurement risk in our cost recovery risk discussion (Section 5.3.3.2.).

SCE and SDG&E identified the 2007 Southern California wildfire as an example of a catastrophic event resulting in a need to further compensate investors through a higher ROE because of heightened perceived business risk.[77] However, none of the credit agencies reporting on the creditworthiness of either SCE or SDG&E mentioned any risks associated with wildfires.[78]

While the anticipation of catastrophic events may expose investors to added risks, such events are not limited to California. These business risks are already captured in the parties' financial modeling results. Any upward adjustment to the financial modeling results being adopted due to business risks would be redundant and possibly excessive. For example, S&P has given SCE a business risk profile of excellent which reflects its utility operations that are subject to limited competition in the provision of essential public service.[79] While its generation portfolio lacks diversity, S&P acknowledges that SCE's purchased

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[77] Hearing Exhibit 17 at 32 and Hearing Exhibit 3 at 13, respectively.

[78] Hearing Exhibit 28 at 35.

[79] Hearing Exhibit 136 at 4.

power supplies offers some diversification benefits and that comprehensive regulation of its business activities provides substantial financial support.

5.3.3. Regulatory Risk

Regulatory risk pertains to *new* risks that investors may face from future regulatory actions that we, and other regulatory agencies, might take. Regulatory risk assessment is also used by rating agencies to set utility bond ratings.[80] Each of the utilities maintains an investment grade bond rating. For example, SCE has an S&P bond rating of BBB, SDG&E an A, SoCalGas an A, and PG&E a BBB.[81] The A ratings are considered by S&P to be upper medium investment grade level and BBB to be medium investment grade level.[82] These investment grade ratings are a good indication that California regulatory risks are low. SDG&E and SoCalGas' financial modeling witness also acknowledged the existence of a favorable regulatory climate in California.[83] Nevertheless, we will address the parties' regulatory risk testimony, which fall into three categories: (1) authorized ROE; (2) cost recovery; and, (3) regulatory lag.

5.3.3.1. Authorized ROE Risk

An authorized ROE has risk when it does not adequately compensate a utility for the risk that investors must assume.[84] California is generally perceived as having a constructive regulatory environment. However, the utilities are

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[80] Hearing Exhibit 74.

[81] Hearing Exhibits 18, 5, 13, and 25, respectively.

[82] S&P has four investment grade levels, the lowest level is medium grade (BBB-, BBB, and BBB+ ratings), upper grade (A-, A, and A+), high grade (AA-, AA, and AA+), and highest grade of AAA.

[83] Reporter's Transcript, Volume 1 at 163.

[84] Hearing Exhibit 3 at 15, and Exhibit 11 at 18.

concerned that a lower ROE could potentially harm their credit profile and increase their cost of capital during a time when they need to spend substantial amounts on capital investment projects, above their historic norm.

California utilities are not the only utilities experiencing an increase of capital investment projects.[85] Therefore, the parties' financial modeling results derived from various proxy groups already include the impact of increasing capital investment by utilities outside of California. Further, the utilities authorized ROE risk concern is without merit because we consistently set the rate of return at a level that meets the test of reasonableness as set forth in the Bluefield and Hope cases and we will continue to do so.

5.3.3.2. Cost Recovery Risk

Cost recovery risk occurs when a utility is precluded from having the ability to fairly and consistently recover its cost in a timely manner. Identified cost recovery issues included: (1) power procurement commitments; (2) balancing and memorandum accounts; and, (3) revenue decoupling. There are opposing sides to this risk argument. The intervenors assert that these cost recovery mechanisms should be reflected as risk reductions in establishing the utilities' ROEs, while the utilities assert that these mechanisms do not make them any less risky than the utilities in their comparable proxy groups.[86]

Since the late 1990s, California energy utilities have transitioned from owning and operating most of their electric generation needs to purchasing generation from other parties under PPAs, the Renewable Auction Mechanism

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[85] Hearing Exhibit 30 at 78-80.

[86] Hearing Exhibits 3 at 70-71, and 23 at 2-2, respectively.

Program, Solar Photovoltaic Program and, the California Renewable Energy Small Tariff. Today's procurement risk is lower than under the regulatory structure during the California energy crisis, when retail rates to customers were fixed and wholesale energy rates were allowed to vary significantly without those cost being passed onto customers.[87]

Current regulation requires the energy utilities to purchase at least 33% of their generation needs from renewable sources by 2020, thereby reducing their ability to earn a return on their generation investments. Instead, they recover costs on a pass-through basis.[88] While the utilities have pre-approval authority to enter into long-term transactions, they continue to face cost recovery risk associated with procurement. This is due to a substantial increase in the number of procurement transactions the utilities are entering into. For example, SCE signed 110 PPAs with renewable generators in the first seven months of 2012.[89] It is also due to being required to regularly justify contract administration, compliance with upfront standards, increasing complexity of procurement contracts, and litigation. Although procurement risk is lower than that existed during the energy crisis such risk does continue to exist today in California and other states and is reflected in the parties' financial modeling results.

In regards to balancing and memorandum accounts, the evidence shows that the potential for disallowance of operating expenses and rate base additions are low given the utilities' ability to recover a substantial portion of their revenue

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[87] Hearing Exhibit 19 at 48.

[88] Other states are looking at a 20% renewable standard in the 2015 through the 2020 period.

[89] Hearing Exhibit 19 at 48.

requirements through balancing and memorandum accounts. For example, SCE recovers 45.24% of its revenue requirements through these mechanisms, SDG&E 44.09%, SoCalGas 54.45%, and PG&E 40.00%.[90] Disallowances from these balancing and memorandum accounts have not been material.

The utilities acknowledge that these cost recovery mechanisms are a benefit. However, they point out that the remainder of their costs is still subject to variability.[91] Moreover, they face uncertainty related to their decisions prior to receiving clear cost-recovery from the Commission.[92] However, rating agencies do recognize the benefit of California balancing and memorandum accounts. For example, S&P stated in its December 15, 2011 Global Portal that a strength of PG&E is the supportive regulatory mechanisms approved by the Commission that allow PG&E timely and certain recovery of costs.[93]

While types of balancing and memorandum account comparisons were made between those used in California and other states, there was no evidence on what percentage of revenues out-of-state utilities recover through those mechanisms.[94] Clearly, the impact of balancing and memorandum accounts is captured in the various financial modeling results. Any adjustment to the financial modeling results being adopted due to cost recovery mechanisms would be redundant or uncertain.

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[90] Hearing Exhibits 18, 5, 13, and 22, respectively.

[91] Hearing Exhibit 3 at 7.

[92] Hearing Exhibit 7 at 13.

[93] Hearing Exhibit 102 at 2.

[94] *See* for example, Hearing Exhibit 23A at Attachment 1.

The third regulatory risk category is revenue decoupling. Decoupling is the regulatory practice of separating authorized base rate revenue from the actual revenues of the utility. It holds base revenue constant and assures that the adopted base revenue requirement will be collected. However, it does not guarantee that the adopted revenue requirement will be sufficient to cover costs. Irrespective, SDG&E concurs with TURN that risk mitigating mechanisms such as decoupling reduce SDG&E's risk.[95]

Revenue decoupling is not unique to California. PG&E has identified 13 utilities in its proxy group that have various stages (partial and full) of revenue decoupling.[96] While the risk associated with revenue decoupling varies between utilities, the financial modeling results already reflect degrees of revenue decoupling risks.

5.3.3.3. Regulatory Lag Risk

Regulatory Lag is commonly defined to be a delay in a utility's ability to recover costs in a timely manner. The utilities contend that they need to be compensated for increased regulatory lag because of extended periods of uncertain outcomes from Commission proceedings which extend beyond the statutory 18 month period.

SCE testified that it takes longer to process general rate cases (GRCs) in California than it does in other states and that time delays in California have

[95] Reporter's Transcript, Volume 1 at 67.

[96] Hearing Exhibit 23 at 2-2.

increased from 367 days in the 1983-1999 period to 589 days since 1998.[97] SCE identified its current GRC as a particularly egregious example of regulatory lag.

SCE filed its test year 2012 GRC in November of 2010. However, SCE failed to acknowledge that its November 2010 filing was for rates to become effective approximately 420 days later, beginning January 1, 2012. Regulatory lag does not exist prior to the requested effective date. While a final decision has yet to be issued, SCE was authorized to maintain a GRC Revenue Requirement Memorandum Account (GRC RRMA) to track the change in revenue requirement ultimately adopted in its GRC during the period between January 1, 2012 and the date a final decision is adopted.[98] We acknowledge that this delay in recovering test year revenue requirements adversely impacts its cash flow. However, the interest being accrued to the RC RRMA compensates SCE for its loss of cash flow.

No party presented any evidence to substantiate that regulatory lag does not exist in other states or that GRC delays are a new risk. Therefore, we conclude, as SCE and PG&E did, that impacts from regulatory lag are reflected in the financial modeling results. Investors' perceived California regulatory risks do not warrant any upward adjustment to the base ROE range being adopted in this proceeding.

5.3.3.4. Other Regulatory Risks

Other regulatory risks identified by the parties include changes in government laws and regulations and municipalization of regulated utilities.

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[97] Hearing Exhibit 19 at 39.

[98] A.10-11-015 Scoping Memo and Ruling of Assigned Commissioner, dated March 1, 2011. *See* also SCE Advice Letter 2596-E.

These changes have occurred and are expected to continue. To the extent that investors expect government laws and regulations to change and municipalization of regulated utilities to occur, such expectations should already be captured in the financial modeling results.

5.4. Summary

The utilities are being increasingly driven by financial, business and regulatory factors that include energy availability, ability to attract capital to raise money for the proper discharge of their public utility duties and to maintain investment-grade creditworthiness, all of which are important components of the Hope and Bluefield decisions. Based on the above financial, business and regulatory risks discussion we conclude that the ROE ranges being adopted in this proceeding from the various financial models adequately compensates the utilities for these risks.

Having addressed the generic factors used in setting an ROE we now address a fair and reasonable return for the individual utilities. We also consider the utilities credit ratios and how debt equivalency impacts those credit ratios. The attached Appendix A is used as a guide to compare the anticipated range of credit ratio impact between the ROEs requested by the utilities and the lowest recommended ROE by intervenors.

5.5. SCE's Return on Equity

The following tabulation summarizes the average results of different versions of the individual financial models used by the parties including the

simple weighted average[99] of the financial modeling results and proposed test year ROE for SCE:

	CAPM	RPM	DCF	Weighted Average[100]	Proposed ROE
SCE	10.70%	8.80%	9.70%	9.70%	11.10%
DRA	7.60%	8.10%	8.50%	8.20%	8.75%
EPUC	8.40%	9.10%	9.10%	8.90%	10.05%[101]
FEA	7.80%	7.80%	8.80%	8.30%	9.00%
TURN	9.20%	9.60%	9.20%	9.30%	9.40%

SCE's requested 11.10% ROE is based on the upper end of the 9.73% to 11.71% range of its CAPM financial modeling results, a level that would compensate it for increased financial, business and regulatory risks.[102] SCE placed no reliance on its RPM and DCF financial modeling results on the basis that the historical risk premium model assumes that relative risk is unchanged between electric utility stocks and "Aa" public utility bonds. It also contends that constant stable market-to book and price/earnings ratios required by the DCF model are not present during this highly volatile market.[103]

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[99] Simple weighted average consists of ¼ CAPM, ¼ RPM, and ½ DCF. The CAPM and RPM financial models are risk premium related and given no more than equal weight. The DCF financial model is investor related and assesses the equity returns based on dividend yields and growth.

[100] Weighted average is defined in Section 5.5, SCE's Return on Equity. Each party's proposed ROE is higher than the weighted average of their financial model results.

[101] EPUC, in light of all of the record evidence, revised its recommended 9.10% ROE for SCE to 10.50%, as set forth in Exhibit 31 at 3 and in its opening and reply briefs, respectively.

[102] Hearing Transcript 17 at 7 and 54.

[103] Hearing Exhibit 17 at 54.

After considering the evidence on market conditions, trends, creditworthiness, interest rate forecasts, quantitative financial models, additional risk factors, and interest coverage presented by the parties and applying our informed judgment, we arrive at a base ROE range of 9.8%% to 10.6%. From that range we conclude that the adopted ROE should be set at the upper end of the adopted ROE range found just and reasonable. We find that SCE's authorized test year 2013 ROE should be 10.45%. This ROE is reasonably sufficient to assure confidence in the financial soundness of the utility and to maintain investment grade credit ratings while balancing the interests between shareholders and ratepayers. As a reality check, we observe that the 10.45% authorized ROE is comparable to the 10.36% average ROEs granted United States electric utilities during the first six months of 2012.[104]

5.6. SDG&E's Return on Equity

The following tabulation summarizes the average results of different versions of the individual financial models used by the parties including the simple weighted average of the financial modeling results and proposed test year ROE for SDG&E:

	CAPM	RPM	DCF	Weighted Average[105]	Proposed ROE
SDG&E[106]	10.50%	10.20%	10.10%	10.20%	11.00%

[104] Hearing Exhibit 53.

[105] Weighted average is defined in Section 5.5, SCE's Return on Equity. Except for TURN, each party's proposed ROE is higher than the weighted average of their financial model results.

[106] Financial modeling results exclude flotation adjustments while the proposed ROE includes the impact of flotation adjustments.

DRA	7.60%	8.10%	8.50%	8.20%	8.50%
FEA	7.80%	7.80%	8.80%	8.30%	8.75%
TURN	9.20%	9.60%	9.40%	9.40%	9.40%

SDG&E's requested 11.00% ROE is based on the 10.40% midpoint of its 9.60% to 11.30% combined CAPM, RPM and DCF financial modeling results, which includes flotation adjustments.[107] Added to that 10.40% are 50 basis points (.5%) for perceived risks resulting from differences in the betas between the average electric utility company and SDG&E, and 10 basis points (.1%) for increased business risk.

After considering the evidence on market conditions, trends, creditworthiness, interest rate forecasts, quantitative financial models, additional risk factors, and interest coverage presented by the parties and applying our informed judgment, we arrive at a base ROE range of 9.60% to 10.40%. This includes the impact of excluding flotation costs, recognition of a 3% increased equity ratio, and an investment grade credit rating of "A". From that range we conclude that the adopted ROE should be set at the upper end of the adopted ROE range found just and reasonable. We find that SDG&E's authorized test year 2013 ROE should be 10.30%. This ROE is reasonably sufficient to assure confidence in the financial soundness of the utility and ability to maintain investment grade credit ratings while balancing the interests between shareholders and ratepayers. We observe that the 10.30% ROE is slightly below the 10.36% average ROEs granted United States electric utilities during the first six months of 2012.

[107] Exhibit 1 at 65.

5.7. SoCalGas' Return on Equity

The following tabulation summarizes the average results of different versions of the individual financial models used by the parties including the simple weighted average of the financial modeling results and proposed test year ROE for SoCalGas:

	CAPM	RPM	DCF	Weighted Average[108]	Proposed ROE
SoCalGas[109]	10.20%	10.00%	9.10%	9.60%	10.90%
DRA	7.60%	8.10%	8.50%	8.20%	8.50%
FEA	7.80%	7.80%	8.80%	8.30%	8.75%
TURN	9.10%	9.60%	9.20%	9.30%	9.25%

SoCalGas' requested 10.90% ROE is based on the average, median and truncated[110] averages of its 9.10% to 10.70% financial modeling results (which includes its flotation adjustments of 20 to 25 basis points) with a midpoint of 9.90% after removing the low 8.40% DCF Natural Gas Utilities Value Line Growth financial modeling result .[111] To the 10.10% SoCalGas concluded reasonable, it added 40 basis points (.4%) for a higher risk profile based on four risk indicators,[112] and an additional 40 basis points (.4%) for prospective business and regulatory risk pressures.

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[108] Weighted average is defined in Section 5.5, SCE's Return on Equity. Except for TURN, each party's proposed ROE is higher than the weighted average of their financial model results.

[109] Financial modeling results exclude flotation adjustments while the proposed ROE includes the impact of flotation adjustments.

[110] The truncated mean is obtained by removing the low and high results and averaging the remaining results.

[111] Hearing Exhibit 12 at 59.

[112] The four risk indicators are: 1) market value ratios, 2) the Commission has allowed SoCalGas a higher return compared to the national average, 3) differences in risk

Footnote continued on next page

After considering the evidence on market conditions, trends, creditworthiness, interest rate forecasts, average results of the financial models, quantitative financial models, additional risk factors, and interest coverage presented by the parties and applying our informed judgment, we arrive at a base ROE range of 9.40% to 10.30%. This includes the impact of excluding flotation costs, an "A" investment grade credit rating, recognition of a 4% increased equity ratio that brings SoCalGas more in line with comparable gas utilities, and recognition that gas utilities are less risky than electric utilities as acknowledged in Reporter's Transcript, Volume 1 at 42. From that range we conclude that the adopted ROE should be set near the middle of the adopted ROE range found just and reasonable. We find that SoCalGas' authorized test year 2013 ROE should be 10.10%, upper middle range of the 9.50% to 10.40% ROE approved for United States gas utilities in the second quarter of 2012 and above the 9.75% average ROE approved during the first six months of 2012.[113] This ROE is reasonably sufficient to assure confidence in the financial soundness of the utility and ability to maintain investment grade credit ratings while balancing the interests between shareholders and ratepayers.

5.8. PG&E's Return on Equity

The following tabulation summarizes the average results of different versions of the individual financial models used by the parties including the simple weighted average of the financial modeling results and proposed test year ROE for PG&E:

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between Western utilities and Eastern/Central utilities, and 4) *beta* difference between SoCalGas and its parent company.

[113] Hearing Exhibit 53.

	CAPM	RPM	DCF	Weighted Average[114]	Proposed ROE
PG&E	11.10%	11.10%	9.60%	10.40%	11.00%
DRA	7.60%	8.10%	8.50%	8.20%	8.75%
EPUC	8.40%	9.10%	9.30%	9.00%	9.90%[115]
FEA	7.80%	7.80%	8.80%	8.30%	9.00%
REID	7.10%	6.70%	8.40%	7.70%	9.00%
TURN	9.10%	9.60%	9.30%	9.30%	9.40%

PG&E requested a 11.00% ROE, which is at the upper end of the 10.20% to 11.40% range it finds fair and reasonable.[116] This range is based on its 10.80% to 11.40% CAPM, 10.80% to 11.50% RPM, and 9.10% to 11.0% DCF financial modeling results. PG&E selected the upper end of its ROE range to compensate it for increased financial, business and regulatory risks.

After considering the evidence on market conditions, trends, creditworthiness, interest rate forecasts, quantitative financial models, additional risk factors, and interest coverage presented by the parties and applying our informed judgment, we arrive at a base ROE range of 9.80% to 10.60%. From that range we conclude that the adopted ROE should be set at the upper end of the adopted ROE range found just and reasonable. We find that PG&E's authorized test year 2013 ROE should be 10.40%. This ROE is reasonably sufficient to assure confidence in the financial soundness of the utility and to maintain investment grade credit ratings while balancing the interests between shareholders and

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[114] Weighted average is defined in Section 5.5, SCE's Return on Equity. Each party's proposed ROE is higher than the weighted average of their financial model results.

[115] EPUC, in light of all of the record evidence, revised its recommended 9.2% ROE for PG&E to 9.9%, as set forth in Exhibit 32 at 3 and its opening and reply briefs, respectively.

[116] Hearing Exhibit 21 at 1-3.

ratepayers. As a reality check, we observe that the 10.40% authorized ROE is also comparable to the 10.36% average ROEs granted United States electric utilities during the first six months of 2012.

6. Implementation

SCE shall consolidate the revenue requirement change being authorized in this decision with revenue changes from other SCE applications through a Tier 1 advice letter filing to become effective January 1, 2013.

SDG&E shall consolidate the revenue requirement changes being authorized in this decision with other electric and gas rate changes which are filed at the end of December 2012 to become effective January 1, 2013.

SoCalGas shall consolidate the revenue requirement changes being authorized in this decision with other gas rate changes which are filed at the end of December 2012 to become effective January 1, 2013.

Consistent with PG&E's implementation proposal, the change in total electric and gas rates will be implemented on January 1, 2013. Changes applicable to Direct Access rates for electric service would be made at the same time as changes in bundled electric customer rates. As authorized under current tariffs, PG&E will record the gas distribution, gas transmission and storage, electric distribution, and electric generation revenue requirements reflecting the 2013 cost of capital in the appropriate balancing and memorandum accounts as of January 1, 2013. Rates for each of these revenue requirements will be set based on the then-current approved revenue allocation and rate design method separately approved for each revenue requirement.

7. Procedural Matters

The utilities requested that their respective ROE application be categorized as a ratesetting proceeding within the meaning of Rule 1.3(e). By Resolution

ALJ 176-3293, dated May 10, 2012, the Commission preliminarily determined that the applications of SCE, SDG&E, SoCalGas and PG&E were ratesetting proceedings and that hearings were expected

The applications were consolidated, pursuant to Rule 7.4 of the Commission's Rules of Practice and Procedure. The consolidation of these applications does not necessarily mean that a uniform ROE should be applied to each of the utilities. This is because each of these utilities has unique factors and differences that need to be considered in arriving at a reasonable return. These unique factors and differences encompass three distinct areas: capital structure, long-term debt and preferred stock costs, and return on common equity.

A Prehearing Conference (PHC) was held on June 4, 2012 to identify issues and a hearing schedule. Following the PHC, Commissioner Ferron issued a Scoping Memo and Ruling setting a schedule that included evidentiary hearings. The Scoping Memo also bifurcated the proceeding with the first phase to address the utilities' test year 2013 cost of capital and the second phase to address the cost of capital mechanism.

That Scoping Memo and Ruling, among other matters, designated Administrative Law Judge (ALJ) Galvin as the presiding officer, established a bifurcated evidentiary hearing schedule and determined the issues of this proceeding. The issues to be addressed in the first series of evidentiary hearings encompassed all matters impacting the utilities' test year 2013 cost of capital including capital structure, costs of long-term debt and preferred stock, return on common equity and related revenue requirement recovery. The second set of evidentiary hearings will address the appropriateness of continuing with or modifying the uniform multi-year Cost of Capital Mechanism and the

appropriateness of SoCalGas continuing with, modifying or replacing its Market-Indexed Capital Adjustment Mechanism.

The first series of evidentiary hearings were held on September 14, 21, 24 and 28, 2012. Additional hearings were held on October 2 and 3, 2012. Each of the utilities, DRA, EPUC, FEA, Reid, and TURN submitted testimony, evidence, and opening and reply briefs. A total of 153 exhibits were received into evidence and 22 witnesses testified. Public Participation Hearings (PPH) were held in San Bernardino, San Diego, and Fresno on October 4, 5, and 9, 2012, respectively. Sixty-six of the 171 customers who attended the PPHs provided statements on the utilities. Cost of capital applications. Almost uniformly, the speakers supported a 9.40% ROE (TURN'S recommended ROE) for the utilities. However, three speakers supported the utilities request and seven speakers expressed other ideas such as a moratorium on shut-offs for low income customers below 200% of the federal poverty line during the summer months.

The utilities' test year 2013 cost of capital issues were submitted on October 22, 2012 upon the filing of reply briefs and receipt of late-filed exhibits that updating the utilities' test year costs of long-term debt and preferred stock based on Global Insight's September 2012 forecast. This proceeding remains open to address the appropriateness of continuing with and modifying the energy utilities' uniform multi-year Cost of Capital Mechanism and the appropriateness of Southern California Gas Company continuing with, modifying or replacing its Market-Indexed Capital Adjustment Mechanism.

8. Comments on Proposed Decision

The proposed decision of ALJ Galvin in this matter was mailed to the parties in accordance with Section 311 of the Public Utilities Code and comments were allowed under Rule 14.3 of the Commission's Rules of Practice and

Procedure. Comments were filed on December 10, 2012 by SCE, SDG&E, SoCalGas, PG&E, EPUC, FEA, Reid and TURN. Reply comments were filed on December 17, 2012. These comments resulted in two substantive changes to the proposed decision.

The first substantive change is the adoption of SDG&E's proposed 3% increase in its common equity ratio from the proposed decision's 1½% common equity ratio increase. This change is made to bring its ratemaking common equity ratio in line with its actual common equity ratio. This results in a SDG&E capital structure of 45.25% long-term debt, 2.75% preferred stock and 52.00% common equity and a 7.79% return on rate base for the test year 2013.

The second substantive change is an increase in SCE's ROE to 10.45% from 10.40%, resulting in a 7.90% return on rate base for the test year 2013. This change in SCE's ROE is made to adequately compensate it for its risks.

To the extent such comments required discussion or changes to the proposed decision the discussion or changes have been incorporated into the body of this decision.

9. Assignment of Proceeding

Mark J. Ferron is the assigned Commissioner and Michael J. Galvin is the assigned ALJ in this proceeding.

Findings of Fact

1. Applicants are public utilities subject to the jurisdiction of this Commission.
2. SCE seeks to reduce its test year 2013 ROE to 11.10% from 11.50%.
3. SDG&E seeks to reduce its test year 2013 ROE to 11.00% from 11.10%.
4. SoCalGas seeks to increase its test year 2013 ROE to 10.90% from 10.82%.
5. PG&E seeks to reduce its test year 2013 ROE to 11.00% from 11.35%.

6. SCE, SDG&E, SoCalGas and PG&E's applications were consolidated pursuant to Rule 7.4.

7. SCE does not propose any change to its authorized capital structure.

8. SDG&E, SoCalGas and PG&E propose minor changes to their currently authorized capital structures.

9. SDG&E expects approximately $772 million of debt equivalency to occur as a result of future contracts pending Commission approval.

10. S&P and Moody's use different methods to determine a utility's debt equivalency.

11. SCE, SDG&E, SoCalGas and PG&E submitted late-filed hearing exhibits to update their cost of long-term debt and preferred stock.

12. There is no opposition to SCE, SDG&E, SoCalGas or PG&E's long-term debt or preferred stock costs.

13. An ROE is set at a level of return commensurate with market returns on investments having corresponding risks, and adequate to enable a utility to attract investors to finance the replacement and expansion of a utility's facilities to fulfill its public utility obligation.

14. The parties used variations of the CAPM, DCF and RPM financial models to support their respective ROE recommendations.

15. SCE, SDG&E, SoCalGas and PG&E used electric utility industry group lists from Value Line to establish proxy groups to be used in their financial models.

16. SCE, SDG&E and PG&E screened the companies in their proxy groups to exclude companies that are not investment grade, do not have a history of paying dividends, and are undergoing a restructure or merger.

17. DRA and FEA used proxy groups that were different than the proxy groups used by the utilities. Reid used a total of seven different proxy groups.

18. PG&E utilized two proxy groups in its financial models, one consisting of utility companies and the other consisting of non-utility companies.

19. The parties used different companies for their proxy groups and, at times, excluded companies from their proxy group when using the CAPM, RPM, and DCF financial models.

20. Each party used different subjective inputs and variations of the CAPM, RPM and DCF financial models as a basis for their recommended ROEs.

21. A flotation cost adjustment to the financial models was rejected by the Commission in D.07-12-049 and D.05-12-043.

22. Financial risk is tied to the utility's capital structure.

23. Debt equivalence has been reflected in the utilities' credit ratings since at least 1990.

24. Business risk pertains to new uncertainties resulting from competition and the economy.

25. Regulatory risk pertains to new risks that investors may face from future regulatory actions.

26. SCE has an investment grade rating of BBB from S&P.

27. SDG&E has an investment grade rating of A from S&P.

28. SoCalGas has an investment grade rating of A from S&P.

29. PG&E has an investment grade rating of BBB from S&P.

30. Quantitative financial models are commonly used as a starting point to estimate a fair ROE.

31. The average ROE authorized for electric and gas utilities in the United States for the first six months of 2012 were 10.36% and 9.75%, respectively.

32. Two important components of the Hope and Bluefield decisions are that the utilities have the ability to attract capital to raise money for the proper discharge of their public utility duties and to maintain creditworthiness.

Conclusions of Law

1. The consolidation of these applications does not mean that a uniform ROE should be applied to each of the utilities.

2. The legal standard for setting the fair ROE has been established by the United States Supreme Court in the Bluefield and Hope cases.

3. The capital structures proposed by SCE, SDG&E, SoCalGas and PG&E should be adopted because they are balanced, attainable, and intended to maintain an investment grade rating and attract capital.

4. The utilities' costs of long-term debt and preferred stock as updated by late-filed hearing exhibits are reasonable and should be adopted.

5. Companies selected for a proxy group should have basic characteristics similar to the utility that the companies are selected to proxy.

6. Companies within a proxy group should not deviate from financial model to financial model.

7. PG&E has not substantiated that investment risks of its proxy group of non-utility companies is comparable to its proxy group of utility companies or to PG&E.

8. The financial modeling results from PG&E's proxy group of non-utility companies should not be considered in this proceeding.

9. Value Line electric industry classifications should continue to be used in ROE proceedings where financial models require the use of a proxy group.

10. Companies within a proxy group should continue to be screened to ensure that the included companies have investment grade credit ratings, a history of paying dividends and are not undergoing a restructure or merger.

11. The financial modeling results should exclude flotation adjustments for the reasons set forth in D.92-11-047.

12. Although the quantitative financial models are objective, the results are dependent on subjective inputs.

13. It is the application of informed judgment, not the precision of quantitative financial models, which is the key to selecting a specific ROE.

14. Company-wide factors such as risks, capital structures, debt costs and credit ratings are considered in arriving at a fair ROE.

15. Debt equivalence should be considered along with other risks in arriving at a fair and reasonable ROE.

16. There should be no adjustment to the financial modeling results for other financial, business or regulatory risks because the financial modeling results already include those risks.

17. A test year 2013 ROE range from 9.80% to 10.60% is just and reasonable for SCE.

18. A test year 2013 ROE range from 9.70% to 10.40% is just and reasonable for SDG&E.

19. A test year 2013 ROE range from 9.40% to 10.30% is just and reasonable for SoCalGas.

20. A test year 2013 ROE range from 9.80% to 10.60% is just and reasonable for PG&E.

21. A test year 2013 ROE of 10.45% and ROR of 7.90% is just and reasonable for SCE.

22. A test year 2013 ROE of 10.30% and ROR of 7.79% is just and reasonable for SDG&E.

23. A test year 2013 ROE of 10.10% and ROR of 8.02% is just and reasonable for SoCalGas.

24. A test year 2013 ROE of 10.40% and ROR of 8.06% is just and reasonable for PG&E.

25. The utilities' ROE applications should be granted to the extent provided for in the following order.

O R D E R

IT IS ORDERED that:

1. Southern California Edison Company's cost of capital for its test year 2013 operations is as follows:

	Capital Ratio	Cost Factor	Weighted Cost
Long-term Debt	43.00%	5.49%	2.36%
Preferred Stock	9.00%	5.79%	.52%
Common Equity	48.00%	10.45	5.02%
Return on Rate Base			7.90%

2. San Diego Gas and Electric Company's cost of capital for test year 2013 electric and gas operations is as follows:

	Capital Ratio	Cost Factor	Weighted Cost
Long-term Debt	45.25%	5.00%	2.26%
Preferred Stock	2.75%	6.22%	.17%
Common Equity	52.00%	10.30%	5.36%
Return on Rate Base			7.79%

3. Southern California Gas Company's cost of capital for its test year 2013 gas operations is as follows:

	Capital Ratio	Cost Factor	Weighted Cost
Long-term Debt	45.60%	5.77%	2.63%
Preferred Stock	2.40%	6.00%	.14%
Common Equity	52.00%	10.10%	5.25%
Return on Rate Base			8.02%

4. Pacific Gas and Electric Company's cost of capital for its test year 2013 electric and gas operations is as follows:

	Capital Ratio	Cost Factor	Weighted Cost
Long-term Debt	47.00%	5.52%	2.59%
Preferred Stock	1.00%	5.60%	.06%
Common Equity	52.00%	10.40%	5.41%
Return on Rate Base			8.06%

5. Value Line Investment Survey electric industry classification shall continue to be used in return on equity proceedings where financial models require the use of a proxy group. Three basic screens shall be used in selecting a comparable proxy group. Those screens are to exclude companies that do not have investment grade credit ratings, exclude companies that do not have a history of paying dividends and exclude companies undergoing a restructure or merger. Additional screens may be used to the extent that justification is provided.

6. Southern California Edison Company, San Diego Gas & Electric Company, Southern California Gas Company and Pacific Gas and Electric Company shall implement the revenue requirement changes authorized by this decision as set forth in Section 6 of this decision. Tariffs in those filings shall be subject to review by the Energy Division in accordance with General Order 96-B.

7. Applications 12-04-015, 12-04-016, 12-04-017 and 12-04-018 remain open to consider the appropriateness of continuing with or modifying the uniform multi-year Cost of Capital Mechanism and the appropriateness of Southern California Gas Company continuing with, modifying or replacing its Market-Indexed Capital Adjustment Mechanism.

This order is effective today.

Dated December 20, 2012, at San Francisco, California.

MICHAEL R. PEEVEY
President
TIMOTHY ALAN SIMON
MICHEL PETER FLORIO
CATHERINE J.K. SANDOVAL
MARK J. FERRON
Commissioners

APPENDIX A
TEST YEAR 2013 CREDIT RATIOS INCLUDING DEBT EQUIVALENCE

	CASH FLOW TIMES (x) INTEREST COVERAGE	DEBT/ CAPITAL	CASH FLOW/ DEBT
S&P Utility Group Financial Targets			
Indicative Ratings			
A	6.0x – 4.0x	40%- 25%	60% - 40%
A -	4.5x - 3.0x	50% - 35%	45% - 25%
BBB -	3.5x – 2.0x	60% - 45%	30% - 10%
SCE (current S&P rating of BBB)			
@ Requested 11.10% ROE	5.0x	57.8%	22.3%
@ Lowest Recommended ROE - 8.75%	4.9x	58.6%	21.1%
SDG&E[1] (current S&P rating of A)			
@ Requested 11.00% ROE[2]	4.0x	58.7%	15.6%
@ Lowest Recommended ROE – 8.50%	3.8x	58.9%	14.8%
SoCalGas[3] (current S&P rating of A)			
@ Requested 10.90%	5.1x	51.2%	25.1%
@ Lowest Recommended ROE – 8.50%	4.8x	51.8%	23.4%
PG&E (current S&P rating of BBB)			
@ Requested 11.00% ROE	4.0x	58.2%	17.2%
@ Lowest Recommended ROE – 8.75%	3.8x	58.2%	15.8%

(END OF APPENDIX A)

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[1] Ratios are based on SDG&E's requested capital structure.

[2] Existing, approved and pending PPA debt equivalency is included.

[3] Ratios are based on SoCal Gas' requested capital structure.