

Decision No. 25363

BEFORE THE RAILROAD COMMISSION OF THE STATE OF CALIFORNIA

In the Matter of the Application of
PACIFIC GAS AND ELECTRIC COMPANY,
a corporation, for an order of the
Railroad Commission of the State of
California authorizing applicant to
purchase shares of the capital stock
of Pacific Public Service Company
upon the terms and conditions of the
agreement between Standard Oil Company
of California, a Delaware corporation,
Pacific Lighting Corporation and ap-
plicant, and authorizing the latter
to in all respects consummate said
agreement in accordance with its terms
and conditions; and authorizing ap-
plicant to issue shares of its common
capital stock in exchange for shares
of the capital stock of Pacific Public
Service Company upon the basis of ex-
change in this application set forth,
etc.

ORIGINAL

Application No. 18322

C. P. Cutten, for applicant.

Alma M. Myers, for Kate T. Myers
and H. J. Myers, protestants.

BY THE COMMISSION:

O P I N I O N

In this proceeding the Commission is asked to enter its order authorizing Pacific Gas and Electric Company, hereinafter sometimes referred to as the Pacific Company, to issue 273,648 shares of its common capital stock of the par value of \$25. per share and of the aggregate par value of \$6,841,200.00, for the purpose of acquiring the outstanding stock of Pacific Public Service Company, hereinafter sometimes referred to as the Service Company; authorizing Pacific Gas and Electric Company to purchase, acquire and hold the shares of stock

of the Pacific Public Service Company; and authorizing Pacific Gas and Electric Company to consummate, in accordance with their terms and conditions, the agreements which are filed in this proceeding as Exhibits "B", "C" and "D".

The petition shows that as of July 1, 1932 the Pacific Public Service Company had an authorized and outstanding stock issue as follows:-

| CLASS | NO. OF SHARES AUTHORIZED | NO. OF SHARES OUTSTANDING IN HANDS OF PUBLIC |
|--------------------------------|-----------------------------|--|
| First preferred(No par value) | 1,000,000 | 420,143 |
| Second preferred(No par value) | 300,000 | 300,000 |
| Common(No par value)Non-voting | 1,000,000 | 262,142½ |
| Common(No par value)Voting | 200,000 | 200,000 |

Exhibit No. 1 shows 420,144.225 shares of first preferred, 300,000 shares of second preferred, 262,142.1125 shares of common non voting, and 200,000 shares of voting common stock.

If the proposed transfers of stock are consummated, the Service Company will either own and control, or control through stock ownership, the following corporations:-

Coast Counties Gas and Electric Company, a California corporation
 West Side Natural Gas Company, a California corporation
 Natural Gas Properties, Inc., a Delaware corporation and its subsidiary company;
 Natural Gas Corporation of California, a California corporation,
 California Consumers Company, a Delaware corporation, and its subsidiary companies including
 Los Angeles Ice and Cold Storage Company,
 Pasadena Ice Company,
 Pomona Valley Ice Company,
 Merchants Ice and Cold Storage Company of Los Angeles
 California Consolidated Water Company, a Delaware corporation,
 Coast Natural Gas Corporation, a Delaware corporation, and
 Coast Industrial Gas Company, a Delaware corporation.

The Pacific Public Service Company through its subsidiaries herein mentioned, is engaged in the business of distributing, furnishing and selling natural gas and butane gas (liquefied natural gas), the distribution and sale of electricity, ice and bottled water, and in the

operation of cold storage facilities. It is of record that electricity is distributed and sold at retail and/or wholesale in 56 communities and surrounding rural territory in Monterey, Santa Clara, Santa Cruz and San Benito Counties. Except for a small quantity of electric energy generated by Coast Counties Gas and Electric Company, all of such energy is purchased from the Pacific Gas and Electric Company. Natural gas is supplied to domestic, commercial and small industrial consumers in 50 communities in the above named counties, and in Contra Costa County. The natural gas used in the Contra Costa County area is transported by means of a high pressure gas transmission pipeline, varying in diameter from 16 inches to 26 inches, and extending approximately 200 miles from the Kettleman Hills oil and gas fields to the City of Richmond and owned by the Standard-Pacific Gas Line, Incorporated. Five-fourteenths ($5/14$) of the capital stock of the Standard-Pacific Gas Line, Incorporated, is owned by Coast Natural Gas Company, a subsidiary of the Service Company, two-fourteenths ($2/14$) by the Standard Oil Company of California, and seven-fourteenths ($7/14$) by the Pacific Gas and Electric Company. Through wholly owned subsidiaries the Service Company operates a bottled spring and distilled water business supplying, according to the record, approximately 55 per cent of the bottled water used in Los Angeles and surrounding territory, and serving the entire southwestern portion of California from San Luis Obispo to the Mexican border. It also supplies a substantial part of the ice used in Los Angeles, Pasadena, Pomona, Hollywood, El Monte, Monrovia and San Bernardino, and cold storage facilities used in and about Los Angeles, and operates a refrigeration pipe line traversing a portion of the business district of the City of Los Angeles.

In Exhibit No. 1 the earnings of the Pacific Public Service Company are reported as follows:-

| I T E M | :Year ended :June 30, 1932 | :Year ended :Dec. 31, 1931 | :Year ended :Dec. 31, 1930 | :Year ended :Dec. 31, 1929 |
|---|-------------------------------|-------------------------------|-------------------------------|-------------------------------|
| | :\$ | :\$ | :\$ | :\$ |
| Operating revenue..... | 5,548,396.29 | 5,676,231.40 | 5,298,687.82 | 5,452,558.89 |
| Operating expenses and maintenance..... | 3,410,349.11 | 3,527,291.04 | 3,444,449.42 | 3,663,517.44 |
| Net operating income... | 2,138,047.18 | 2,148,940.36 | 1,854,238.40 | 1,789,041.45 |
| Nonoperating revenue... | 116,204.95 | 138,307.86 | 148,151.32 | 214,035.74 |
| Gross corporate income | 2,254,252.13 | 2,285,248.22 | 2,002,389.72 | 2,003,077.19 |
| DEDUCTIONS: | | | | |
| Interest deductions.... | 792,650.52 | 723,641.52 | 424,395.83 | 531,095.81 |
| Amortization of debt discount and expense : | 135,396.47 | 110,018.98 | 33,626.47 | 54,564.83 |
| Federal taxes | 58,454.97 | 56,049.78 | 79,735.43 | 112,545.81 |
| Depreciation..... | 462,715.05 | 490,937.26 | 370,548.26 | 383,105.76 |
| Total deductions.. | 1,449,217.01 | 1,380,647.54 | 908,305.99 | 1,081,312.21 |
| Net income available for dividends..... | 805,035.12 | 904,600.68 | 1,094,083.73 | 921,764.98 |
| Dividends on preferred stocks of subsidiary companies | 327,258.14* | 329,399.88 | 324,557.58 | 328,725.03 |
| Net profit to surplus | \$ 477,776.98 | \$ 575,200.80 | \$ 769,526.15 | \$ 593,039.95 |

*Includes provision for cumulative preferred stock dividends of subsidiary company in arrears in the amount of \$25,460.75.

The above figures do not include \$157,472.33 of losses of Natural Gas Corporation of California to December 31, 1931, because in the exhibits filed such losses have been charged to intangible capital.

For the six months ended June 30, 1932 the Service Company in Exhibit No. 1 shows a net profit to surplus of \$110,663.49.

In reporting its earnings the Service Company reduced the depreciation charges of the subsidiary companies to an amount which, together with its maintenance expenses, aggregates 12-1/2 percent of the company's operating revenue. If the depreciation charges had not been adjusted the net profits to surplus of the Service Company would have been as follows:-

| | |
|--|--------------|
| Year ended December 31, 1929 | \$520,600.17 |
| Year ended December 31, 1930 | 657,639.98 |
| Year ended December 31, 1931 | 512,718.26 |
| Year ended June 30, 1932 | 404,217.89 |
| Six months ended June 30, 1932 | 54,787.10 |

The adjustments were made because of a provision in the Articles of Incorporation of the Service Company which provide that the charges for maintenance and depreciation shall not be less than 12-1/2 percent of the gross operating revenue from electric, gas and other business.

The balance sheet of the Pacific Public Service Company (Exhibit No. 1) after the write-off of Natural Gas Corporation of Oregon and Washington properties, which are excluded from the proposed transaction, shows the following assets and liabilities:-

| <u>A S S E T S</u> | |
|--|-------------------------|
| Fixed capital in service | \$25,504,349.62 |
| Fixed capital under construction | 355,013.11 |
| Investments | 3,282,883.24 |
| Subscribers to preferred stock | 364.44 |
| Current assets | 4,373,170.42 |
| Prepaid and deferred debits (includes \$374,615.54 preferred stock sales expense, 800,835.12 bond discount and expense, 231,368.59 extraordinary deferred charges, and 23,376.64 stock discount and expense) | 1,537,578.04 |
| Total assets and other debits..... | <u>\$35,053,358.87</u> |
| <u>L I A B I L I T I E S</u> | |
| Preferred stocks of subsidiaries | \$ 5,155,500.00 |
| Cumulative dividends in arrears thereon | 25,460.75 |
| Long term debt | 15,222,500.00 |
| Capital stock subscribed | 603.50 |
| Current and accrued liabilities | 2,280,335.23 |
| Deferred credits | 79,596.17 |
| Reserves (includes \$3,994,386.86 for depreciation and \$310,294.35 for uncollectible accounts) | 4,695,784.37 |
| Surplus and capital stock of parent company | 7,593,578.85 |
| Total liabilities and other credits | <u>\$ 35,053,358.87</u> |

Since the date of the balance sheet, \$1,500,000.00 of notes payable have been cancelled and special deposits, included in current assets, reduced by a like amount.

The fixed capital in service appearing in the balance sheet reflects in part the original cost and in part an appraisal of some of the properties.

In Exhibit No. 2, as modified by the testimony of Chas. Gransky, the undepreciated cost of the fixed properties of the Service Company is reported at \$27,527,054.00. This figure includes

\$11,490,732.00 which represents reproduction cost appraisals of properties by Sanderson and Porter during 1927 and 1928. No adjustments were made in such figures because of the decline in prices since the date of the appraisals, nor were any witnesses called to justify the appraisal figures. No figures were submitted showing the historical cost of the properties appraised by Sanderson and Porter. John E. Cooper, valuation engineer for the Commission, testified that the historical cost would be less than the reproduction cost reported by Sanderson and Porter. The remainder of the \$27,527,054.00 is said to reflect the historical cost of the properties. It includes, however, \$157,472.33 for development costs of the Natural Gas Corporation of California, which represents losses of that company to December 31, 1931, and \$463,620.00 of estimated interest during construction and other overheads of Coast Counties Gas and Electric Company, which have not been charged to capital account from 1921 to 1928. The record does not show that these costs were actually incurred. Exhibit No. 1 shows a depreciation reserve of \$3,994,386.86.

Both the Service Company and the California Consumers Company have passed their dividends on their preferred stock.

Pacific Gas and Electric Company desires permission to issue 70,000 fully paid shares of its common stock of the par value of \$25. per share and of the aggregate par value of \$1,750,000.00 to the Standard Oil Company of California and Pacific Lighting Corporation, to acquire the following stocks of Pacific Public Service Company:-

1. 300,000 shares of second preferred stock.
2. 43,396 shares of non-voting common stock (16.55% of total outstanding)
3. 200,000 shares of voting common stock.

This stock is to be issued as of October 1, 1932.

For each share of outstanding first preferred stock of the Service Company(420,143 shares outstanding) the Pacific Company would issue forty-five hundredths of one share of its common stock, which shall be issued as of October 1, 1932; and for each share of outstanding non-voting common stock, other than that mentioned above (218,746½ shares) it would issue one fifteenth of one share of its common stock, said stock to be issued and delivered as of July 1, 1933. For these two purposes the Pacific Company asks permission to issue 203,648 shares of its common capital stock of the par value of \$25. per share, having a par value of \$5,091,200.00. In the aggregate Pacific Gas and Electric Company would issue a total of \$6,841,200.00 par value of its common capital stock. At the current rate of dividend, the annual dividend charge on this proposed stock issue is \$547,296.00.

The outstanding securities of the Pacific Public Service Company and its subsidiaries in the hands of the public, plus the common stock which the Pacific Gas and Electric Company desires to issue, aggregates \$27,219,950.00 segregated as follows:-

| | | |
|---|-------------------------------------|-----------------------|
| A. <u>FUNDED DEBT</u> : | | \$15,222,500. |
| Five year 5 percent gold notes of Pacific Public Service Company due 1936 | \$7,794,000. | |
| Thirty year 5 percent bonds of Coast Counties Gas and Electric Company due 1960 | 4,000,000. | |
| Twenty year 6 percent bonds California Consumers Company due 1948 | <u>3,428,500.</u> | |
| B. <u>PREFERRED STOCKS</u> : | | 5,155,350. |
| Coast Counties Gas and Electric Company first preferred | 3,699,900. | |
| California Consumers Company first preferred | 1,454,900. | |
| Inland Empire Gas Company first preferred | <u>550.</u> | |
| C. <u>COMMON STOCK</u> | Inland Empire Gas Company | 900. |
| D. <u>COMMON STOCK</u> | of Pacific Gas and Electric Company | <u>6,841,200.</u> |
| | TOTAL..... | <u>\$ 27,219,950.</u> |

It is urged that the application should be granted because certain economies can be effected through the transfer of the control of the Service Company properties to the Pacific Gas and Electric Company, and that Pacific Gas and Electric Company will under the agreement filed as Exhibit "C" obtain valuable gas priorities.

It is of record that it is not the intention of the Pacific Gas and Electric Company to translate whatever economies may be effected, into lower rates. What benefits may flow from the consolidation will be retained by the Pacific Gas and Electric Company to support the dividend on the stock proposed to be issued by it.

We come now to the gas rights contract filed as Exhibit "C" in this proceeding. It is of record that Pacific Gas and Electric Company now has contracts with Standard Oil Company of California, under which it is presently purchasing from that company about 40 per cent of gas requirements. When applicant reaches a point where it will be purchasing an average of about 70,000,000 cubic feet of gas per day, it must purchase half of its gas from Standard Oil Company of California. Under present contracts, applicant can obtain 40 per cent of the gas which Standard Oil Company of California may produce in the North Dome, and 30 percent in the Middle Dome of Kettleman Hills. Under the proposed contract applicant will get a priority to 50 percent of the gas which Standard Oil Company of California may produce in Kern County on lands now or hereafter owned by it; it also acquires priorities to an additional 23 percent of gas produced in the North Dome and to 3 percent in the Middle Dome of Kettleman Hills; it also gets a priority to gas allocated to Service

Company, and gets a priority on all gas produced by Standard Oil Company of California north of Tehachapi Mountains and north of Santa Barbara County, except Kern County and Kettleman Hills. The contract does not give applicant an option to purchase gas, but grants it certain priorities. It permits Standard Oil Company of California to sell gas to others if applicant does not need the gas allotted to it under the contract and provides that if Standard Oil Company of California does not own more than fifty percent of an oil or gas field north of the fourth parallel south, applicant can buy in that field up to 20,000,000 cubic feet per day. Such gas is not to be included in determining its obligation to buy gas from Standard Oil Company of California. The gas contract provides that it shall not become effective unless the stock purchase contract (Exhibit "B") is consummated.

The agreement recites that the Pacific Gas and Electric Company is entering into the contract (Exhibit "B") to acquire stock of Pacific Public Service Company upon the express consideration that Standard Oil Company of California will enter into this contract (Exhibit "C") with Pacific Gas and Electric Company, and would not otherwise enter in said contract (Exhibit "B") with Standard Oil Company of California and Pacific Gas and Electric Company.

Under the terms of the agreement filed herein as Exhibit "D", Standard Oil Company of California agrees to supply to Pacific Gas and Electric Company for operation of butane plants, now owned by subsidiaries of Pacific Public Service Company, butane at the following prices, effective January 1, 1932;-one cent per gallon for two years, two cents per gallon for three years thereafter, and at the market price thereafter for an additional five years. During

said periods Pacific Gas and Electric Company agrees to buy all butane necessary for the operation of said plants from Standard Oil Company of California. The difference between the amount paid by Pacific Gas and Electric Company to Standard Oil Company of California during said first period of five years for butane for any of said plants and the price of three cents per gallon shall be payable to Standard Oil Company of California out of earnings, if any, during each^{year} of the ten year period, from all said butane plants while owned and operated as butane plants by Pacific Gas and Electric Company, or its subsidiaries taken as a group, after deduction of the usual operating expenses, taxes, depreciation, uncollectible bills, rentals, and six percent on the capital investment in such plants, as shown by the books of the Pacific Public Service Company, or its subsidiaries engaged in the operation of such plants for such years. The agreement recites that Pacific Gas and Electric Company is entering into an agreement with Pacific Lighting Corporation and Standard Oil Company of California to acquire stock of Pacific Public Service Company upon consideration, among other things, that Standard Oil Company of California will furnish butane at the above mentioned prices and for said purposes.

Applicant asks that the Commission grant and confer upon Pacific Gas and Electric Company all necessary permission and authority in all respects to consummate, in accordance with their terms and conditions, the agreements filed in this proceeding as Exhibits "B", "C" and "D". While it appears that the agreements filed as Exhibits "C" and "D" are part of the consideration which Pacific Gas and Electric Company receives for issuing its stock in exchange for stock of Pacific Public Service Company, the execution of

these contracts is a matter which need not be authorized by the Commission. Applicant, as well as other public utilities engaged in the sale of natural gas, has entered into many gas purchase contracts without submitting them to the Commission for approval. The law does not require the Commission to approve such contracts.

We are not ready to recognize in the gas priority contract (Exhibit "C") any value that can be used as a basis for the issue of stock or for any other purpose. There is no definite evidence before us that this contract will result in increased earnings of Pacific Gas and Electric Company.

During his oral argument, counsel for applicant stated that it was the policy of applicant to continue the payment of eight percent dividend on its common stock. The payment of dividend on common stock, assuming it is earned, is a matter that rests with the Boards of Directors of public utilities. However, when, as in this instance, the Commission is asked to authorize a public utility to issue stock to acquire control of properties, whose earnings are inadequate to pay the dividends which it is proposed to pay on such stock, the Commission has an interest in the matter. The logical thing to do would be to reduce the stock issue so as to be in line with the cost and/or the earnings of the properties to be acquired. But it is urged that the earnings of Pacific Public Service Company will improve with a change in economic conditions and that the situation can be worked out in a satisfactory manner. We are inclined to give applicant an opportunity to demonstrate this and if it is successful in its endeavor, consider a modification of the order herein. In the meantime, however, we believe that applicant should be permitted to issue the \$6,841,200.00 of stock only upon

condition that it transfer \$5,000,000.00 from its earned surplus now invested in properties to Account 251, "Appropriations for additions and betterments," and file with the Commission a resolution of its Board of Directors agreeing that it will not capitalize such amount through the issue of stock or evidences of indebtedness until and unless the earnings of the Pacific Public Service Company properties are sufficient to pay the annual dividends on the \$6,841,200.00 of stock and accumulate a surplus of \$5,000,000.00 from earnings or the sale of properties at a price in excess of that being paid by the Pacific Gas and Electric Company for their control.

It should be understood that the Commission has made no final determination of what Pacific Gas and Electric Company may charge to fixed capital or other asset accounts, if it acquires the properties of Pacific Public Service Company or its subsidiaries. This proceeding does not raise that issue. When this matter comes before us, we will review the appropriation of said \$5,000,000.00 and determine whether the same should be increased or decreased.

Alma M. Myers, appearing for H. J. Myers, a stockholder of Pacific Gas and Electric Company, and Kate T. Myers, a consumer of gas and electricity supplied by Pacific Gas and Electric Company, protest the granting of this application. The Commission is asked to dismiss the application on the ground that it was not prepared in accordance with the rules of procedure of the Commission. We believe that applicant in presenting its evidence fully met the requirements of the Commission in a proceeding of this character. The motion to dismiss the application will therefore be denied. Protestants' reasons for the denial of the application will be rejected because we fail to see wherein this proceeding involves ^{or} the capitalization of a contract for consolidation, how the public interest is adversely affected if the purchase of the stock is

consummated under the provisions of the following order, nor do we believe that under such order any stock is being issued against an operating deficit.

O R D E R

Pacific Gas and Electric Company having asked the Commission to enter its order, as indicated in the foregoing opinion, a public hearing having been held before Examiner Fankhauser, the Commission being of the opinion that Pacific Gas and Electric Company should be permitted to issue \$6,841,200.00 par value of its common capital stock for the purposes indicated in this order under the terms and conditions set forth herein, that the money, property or labor to be procured or paid for by the issue of such stock is reasonably required by applicant, and that the expenditures for the purposes herein authorized are not in whole or in part reasonably chargeable to operating expenses or to income, and that this application insofar as it involves the request to confer and to grant upon applicant authority to execute the agreement filed in this proceeding, Exhibits "C" and "D" should be dismissed without prejudice, therefore,

IT IS HEREBY ORDERED as follows:-

1. Pacific Gas and Electric Company may, after the effective date hereof, purchase, acquire and hold all of the shares of the outstanding capital stock of Pacific Public Service Company.
2. For the purpose of acquiring the outstanding capital stock of Pacific Public Service Company and to reimburse its treasury on account of surplus earnings invested in its properties, Pacific Gas and Electric Company may, after the effective date hereof, issue

273,648 shares of fully paid common capital stock of the aggregate par value of \$6,841,200.00 and may sell and deliver said stock for the purpose of acquiring the outstanding stock of Pacific Public Service Company, in accordance with the terms and conditions of the contract filed in this proceeding as Exhibit "B".

3. The authority herein granted to acquire stock of the Pacific Public Service Company and to issue common stock in exchange therefor, will become effective, except as otherwise herein stated, when Pacific Gas and Electric Company has filed with the Commission, in form satisfactory to the Commission, a duly and legally executed resolution of its Board of Directors in which said Pacific Gas and Electric Company agrees that it will, prior to the issue of any of the stock herein authorized, transfer from Account No. 261 "Unappropriated surplus" to Account No. 251 "Appropriations for additions and betterments", the sum of \$5,000,000.00, and agrees that it will not claim the right to issue stock or evidences of indebtedness against said \$5,000,000.00, until and unless the earnings of the Pacific Public Service Company properties are sufficient to pay the annual dividends on the \$6,841,200.00 of stock herein authorized to be issued ^{there has been} and/accumulated ^a surplus of \$5,000,000.00 from earnings or the sale of properties, at a price in excess of that being paid for their control. The said \$5,000,000.00 shall be carried in Account 251 "Appropriations for additions and betterments" until the Commission has authorized said amount or a part thereof to be transferred to another account.

4. This application insofar as it involves requests for permission to execute the contracts filed in this proceeding as Exhibits "C" and "D", is hereby dismissed without prejudice.

5. Pacific Gas and Electric Company shall keep such record of the issue and delivery of the stock herein authorized and of the disposition of the proceeds as will enable it to file on or before the 25th day of each month a verified report, as required by the Railroad Commission's General Order No. 24, which order insofar as applicable, is made a part of this order.

6. Notwithstanding anything to the contrary herein stated, the authority granted in this order will not become effective until twenty(20) days after the date hereof.

DATED at San Francisco, California, this 14th day of November, 1932.

O. C. Seaver
Leon O. Whiteley
W. A. Cunn
M. B. Harris
Fred G. Stewart

Commissioners.