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Decision No. 74513

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

In the Matter of the Application of SOUTHERN CALIFORNIA EDISON COMPANY, a corporation, for authority to issue and sell not to exceed 3,000,000 shares of Preference Stock, ____% Convertible Series, $25 Par Value, and to issue shares of Common Stock upon conversion of such Preference Stock, and for the exemption of such proposed issue of Preference Stock from the requirements of the competitive bidding rule established in this Commission's Decisions Nos. 38614 and 49941.

Application No. 50375
(Filed July 8, 1968)

Rollin E. Woodbury, Harry W. Sturges, Jr., Robert J. Cahall and H. Robert Barnes, by Robert J. Cahall and H. Robert Barnes, and O'Melveny & Myers, by James E. Cross, for Southern California Edison Company, applicant.
Russell J. Leonard, for the Commission staff.

O P I N I O N

In its application the applicant, Southern California Edison Company, is seeking (1) authority to issue and sell not to exceed 3,000,000 shares of its preference stock, of the par value of $25 per share, (2) authority to issue shares of its common stock upon conversion of such preference stock, and (3) an exemption of the issue of the preference stock from the Commission's competitive bidding rule established by Decisions No. 38614 and No. 49941. The applicant requests that the Commission's order be made effective five days after the date thereof.

After due notice a public hearing in this matter was held before Examiner Cline in Los Angeles on July 19, 1968. At the conclusion of the hearing the matter was taken under submission. The Finance and Accounts Division, through its representative, participated at the hearing and at its conclusion recommended the granting of the application. There were no protests to the granting of the application.

Applicant's financial vice president testified that applicant's net construction expenditures for the years 1968-1969 are estimated to be about $695,000,000. Of this amount approximately $453,000,000 must be provided from new permanent financing and the balance of $242,000,000 will be provided from internal sources.

Applicant proposes to use the $75,000,000 proceeds of the sale of the 3,000,000 shares of preference stock at $25 per share, after payment and discharge of obligations incurred for expenses incident to their issuance and sale including compensation payable to the several underwriters in connection therewith, for the following purposes:

(a) To retire and discharge promissory notes, drafts and/or bills of exchange which may be outstanding, the principal amount of which is estimated to aggregate approximately $55,000,000 to $57,000,000 at the time the proceeds from the sale of the preference stock are expected to be received. An amount at least equal to the proceeds from said notes, drafts or bills of exchanges has been, or by the time that such retirement and discharge have been effected will have been, obtained for the use and used for the acquisition of property and for the construction, completion, extension or improvement of applicant's facilities, exclusive of maintenance of service and replacements.

(b) To apply the remainder of such proceeds from the preference stock to reimburse applicant for monies actually expended by applicant from income or other monies in the treasury of applicant not secured by or obtained from the issue of stocks

> or stock certificates or other evidences of interest or ownership or bonds, notes or other evidences of indebtedness, for the acquisition of property, or for the construction, completion, extension or improvement of its facilities, exclusive of maintenance of service and replacements. Any such amount so reimbursed will become a part of the general treasury funds of applicant.

Applicant proposes to issue the common stock which is the subject of this application for the purpose of exchanging said stock for and upon the conversion and retirement of the preference stock.

Applicant's capital ratios as of May 31, 1968, and as adjusted to give effect to the proposed issuance of 3,000,000 shares of the preference stock at the price of $25 per share are as follows:

	May 31, 1968		Pro Forma	
Mortgage bonds	51.9%		50.3%	
Convertible debentures	3.2		3.1	
Total long-term debt		55.1%		53.4%
Preferred stock		8.1		7.8
Preference stock		-		3.1
Common stock equity		36.8		35.7
Total		100.0%		100.0%

Applicant's witness testified that if applicant were to increase its long-term debt with a $75 to $100 million bond issue before issuing equity, it would severely limit the financial alternatives available to it in the future, since the total debt ratio would rise to almost 57 percent. A debt ratio of much above 55 percent would place applicant's Aa bond rating in jeopardy. In addition the fact that the applicant's earnings available for fixed charges are rapidly declining in the opinion of the witness precludes the issuance of additional debt at this time.

The witness further testified that a sale of common stock would appear to be unwise since applicant is still absorbing the dilutive effect of the 1.5 million shares sold in January of 1968. The sale of a straight preferred would be expensive. Convertible preference stock, a class not presently outstanding, would not only add to applicant's equity base, but, because of the convertible feature, should also result in a lower dividend cost than that of a preferred which is not convertible.

Because of the junior status in applicant's capital structure, the issue of preference stock will not adversely affect the investment standing or dividend coverage of applicant's outstanding cumulative preferred stock. An additional advantage of a convertible issue is that, by fixing the conversion price above the current market price for the common stock, applicant is, in effect, selling common stock at a price higher than the current market conditions would warrant.

Applicant contemplates that the issue of shares of preference stock will be underwritten by a nationwide group of investment banking firms which, under the terms and conditions of a proposed written agreement with applicant, will agree to purchase all of the shares of preference stock. Applicant requests exemption from the competitive bidding requirements of the Commission for the following reasons:

(1) Negotiation will result in a larger number of underwriters and should enable a greater local distribution of the preference stock than would a competitive offering.

(2) Negotiation will enable applicant to obtain maximum flexibility in arranging the terms and conditions and in timing of the sale.

(3) Negotiation will encourage the underwriters better to prepare the market in advance of the offering and, therefore, increase the possibility of a quick reception by the investing public at a cost to the applicant which may well be lower than that which would result from competitive bidding.

Applicant's witness stated that he was of the opinion that, unless there is a major upheaval in market conditions before August 20, the redemption price schedule and voluntary liquidation preferences to be fixed for the new series of preference stock will be substantially as set forth in the Certificate of Determination of Preferences of Preference Stock which is Exhibit "E" to the application. At the hearing an amended Exhibit "E" was received in evidence as Exhibit No. 8 which embodied changes in paragraphs (3) and (12) of subdivision (B). These changes relate to the so-called "antidilution provisions" protecting the conversion rights of the holders of the preference stock from certain events which might happen in the future which would otherwise depreciate the value of the conversion right conferred. In general these provisions call for the adjustment of the initial conversion price in the case of the split or combination of the common stock, in the case of the declaration of common stock dividends, and in the case of certain other events, including the issuance of common stock for a consideration less than the conversion price then in effect, but no adjustment is to be made until cumulative adjustments amount to at least 50 cents.

Applicant's witness testified that he anticipated the dividend rate on the preference stock will not exceed 6 percent, the underwriting compensation will not exceed 2-3/4 percent of par or 68.75 cents per share, and the initial conversion price will range between 105 percent and 120 percent of the then current market price of the applicant's common stock.

The low for applicant's common stock during 1968 is $31 per share. Using the lower limit of 105 percent and a price of $31 per share for the common stock as a basis for conversion of the $25 preference stock, applicant's witness determined that 2,304,147 shares of common stock would have to be authorized for issuance upon conversion of the preference stock.

The witness testified that applicant has selected August 20 as a desirable date for the execution of the underwriting agreement covering the proposed issue of preference stock provided this Commission issues its order granting the necessary authority on or before August 13. In such case applicant would expect to receive the proceeds from the sale of the preference stock to the underwriters on Wednesday, August 28.

Based upon the record in this proceeding the Commission finds as follows:

1. The proposed preference stock issue and common stock issue are for proper purposes.

2. Applicant has need for funds from external sources for the purposes set forth in this proceeding.

3. The issue and sale of the proposed issue of preference stock should not be required to be through competitive bidding.

4. The dividend rate on the preference stock should not exceed 6 percent per annum.

5. The initial conversion price of the preference stock should not be less than 105 percent nor more than 120 percent of the market price of applicant's common stock at the close of the day preceding the execution of the underwriting agreement.

6. The terms and conditions of the Certificate of Determination of Preferences of Preference Stock should be substantially as set forth in Exhibit No. 8 in this proceeding.

7. The underwriting compensation on the preference stock should not exceed 2-3/4 percent of the $25 par value or 68.75 cents per share.

8. The terms and conditions of the underwriting agreement should be substantially as set forth in Exhibit "F" attached to the application in this proceeding.

9. The money, property or labor to be procured or paid for by the issue of the preference stock and the common stock herein authorized is reasonably required for the purposes specified herein, which purposes are not, in whole or in part, reasonably chargeable to operating expenses or to income.

On the basis of the foregoing findings we conclude that the application should be granted.

In issuing our order herein, we place applicant and its shareholders on notice that we do not regard the number of shares outstanding, the total par value of the shares nor the dividends paid as measuring the return applicant should be allowed to earn on its investment in plant and that the authorization herein granted is not to be construed as a finding of the value of applicant's stock or properties nor as indicative of amounts to be included in proceedings for the determination of just and reasonable rates.

ORDER

IT IS ORDERED that:

1. The issue and sale by Southern California Edison Company of not to exceed 3,000,000 shares of the new series of preference stock referred to in this proceeding are hereby exempted from the Commission's competitive bidding rule set forth in Decision No. 38614, dated January 15, 1946, as amended by Decision No. 49941, dated April 20, 1954, in Case No. 4761.

2. Southern California Edison Company may issue and sell not to exceed 3,000,000 shares of its preference stock of the par value of $25 per share at a price of $25 per share subject to the following conditions:

(a) The dividend rate shall not exceed 6 percent per annum.

(b) The initial conversion price of the preference stock shall not be less than 105 percent nor more than 120 percent of the market price of the common stock of Southern California Edison Company at the close of the day preceding the execution of the underwriting agreement referred to in ordering paragraph 2(e) below.

(c) The terms and conditions of the Certificate of Determination of Preferences of Preference Stock shall be substantially as set forth in Exhibit No. 8 in this proceeding.

(d) The underwriting compensation on the preference stock shall not exceed 2-3/4 percent of the $25 or 68.75 cents per share, or an aggregate total of $2,062,500 on the 3,000,000 shares.

(e) The terms and conditions of the underwriting agreement shall be substantially as set forth in Exhibit "F" attached to the application in this proceeding.

3. Southern California Edison Company may issue such number of shares of its common stock, in exchange for and upon retirement of preference stock, upon conversion of shares of preference stock, as may be required from time to time for such purpose pursuant to the provisions governing such conversions to be set forth in the Certificate of Determination of Preferences under which the preference stock is to be issued.

4. Southern California Edison Company shall use the proceeds from the sale of said preference stock for the purposes specified in this proceeding.

5. Within thirty days after the issue and sale of any of the preference stock herein authorized, Southern California Edison Company shall file with the Commission three copies of its prospectus pertaining to said stock.

6. Within three months after such issue and sale of preference stock, Southern California Edison Company shall file

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with the Commission a statement, in lieu of a report under General Order No. 24-B, disclosing the purposes for which the preference stock proceeds were used.

The effective date of this order shall be five days after the date hereof.

Dated at San Francisco, California, this 6th day of AUGUST, 1968.

William Symons Jr.
President

Peter E. Mitchell

William M. Bennett

A. W. Gatov

Fred P. Morrissey
Commissioners