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Decision No. 88612 MAR 21 1978

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BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

Application of SAN DIEGO GAS &)
ELECTRIC COMPANY, to issue and sell)
not exceeding \$60,000,000 of bonds)
and to execute a supplemental)
indenture.)

Application No. 57871
(Filed February 15, 1978)

O P I N I O N

San Diego Gas & Electric Company (SDG&E) seeks an order authorizing it (a) to issue and sell not exceeding \$60,000,000 aggregate principal amount of First Mortgage Bonds, Series R, Due 2008, and (b) to execute and deliver a Nineteenth Supplemental Indenture.

SDG&E is a California corporation engaged principally in the business of providing electric service in portions of Imperial and Orange Counties, and electric, gas and steam service in portions of San Diego County. For the year 1977, the utility reported total operating revenues of \$508,039,259 and net income of \$60,247,232 representing an increase of 13.5% and 19.4%, respectively, over the prior year's results.

As of December 31, 1977, SDG&E had outstanding \$112,960,000 of short-term debt, the proceeds of which were used for capital additions and improvements.

SDG&E's capital budget through December, 1977 amounted to \$1,065,028,000, of which \$504,481,000 has been spent, and \$560,547,000 remains to be expended in the future. The utility estimates it will spend \$235,736,000 for capital construction in 1978.

SDG&E reports that as of December 31, 1977, its unreimbursed construction expenditures amounted to \$63,667,959, as set forth in Exhibit C, attached to the application and summarized as follows:

<u>March 31, 1921 to December 31, 1977</u>	<u>Amount</u>
Net Construction Expenditures	\$1,494,413,521
Par Value of Redeemed Securities	<u>128,348,630</u>
Total	<u>\$1,622,762,151</u>
 Deductions:	
Amount Not Bondable Per Decision No. 10032	\$ 45,116
Proceeds from Sale of Securities	1,244,142,176
Depreciation Reserve	<u>314,906,900</u>
Total	<u>\$1,559,094,192</u>
 Unreimbursed Construction as of December 31, 1977	 <u>\$ 63,667,959</u>

SDG&E proposes to issue and sell not exceeding \$60,000,000 aggregate principal amount of its bonds. The utility would use the net proceeds, exclusive of accrued interest, for the retirement of a portion of its outstanding short-term loans and commercial paper issued for temporary financing of additions to its utility plant, and the balance, if any, would be applied toward the reimbursement of the company's treasury for capital expenditures. The accrued interest received would be used for general corporate purposes.

The Series R Bonds would be secured by an existing indenture as previously amended and supplemented, and as further supplemented by a proposed Nineteenth Supplemental Indenture, which is attached to the application as Exhibit E.

The utility's capital ratios as of December 31, 1977, and as adjusted to reflect the sale of 1,000,000 shares of Preference Stock (estimated proceeds of \$26,500,000) authorized on February 7, 1978 by the Commission in Decision No. 88474, the proposed sale of \$60,000,000 of bonds, and the anticipated sale of 2,500,000 shares of common stock (estimated proceeds of \$37,500,000) involved in Application No. 57866 filed on February 10, 1978, are as follows:

<u>Component</u>	<u>December 31, 1977</u>	<u>Pro Forma</u>
First Mortgage Bonds	42.5%	43.1%
Debentures	2.2	2.0
Other Long-Term Debt	4.9	4.4
Preferred and Preference Stock	16.3	16.7
Common Stock Equity	<u>34.1</u>	<u>33.8</u>
	<u>100.0%</u>	<u>100.0%</u>

The Finance Division has calculated SDG&E's after-tax coverage at December 31, 1977 as 2.24 times for interest on debt and 1.75 times for combined coverage of interest plus dividends on preferred and preference stock.

SDG&E proposes to issue and sell the bonds on a negotiated basis through a nationwide group of underwriters represented by Merrill Lynch, Pierce, Fenner & Smith Incorporated and Blyth Eastman Dillon & Co. Incorporated, who will agree to purchase all of the bonds pursuant to an underwriting agreement. On or about April 4, 1978, the utility expects to complete negotiations with the underwriters for determining the terms of the proposed offering including (a) price of bonds, (b) interest rate, (c) aggregate principal amount, (d) maturity date, (e) sinking fund requirements (if any), (f) call protection, (g) other redemption provisions, and (h) underwriting commissions.

SDG&E requests an exemption for the proposed issue and sale of the bonds from the Commission's competitive bidding rule established by Commission Decision No. 38614, dated January 15, 1946, as amended from time to time in Case No. 4761. The utility's reasons for requesting an exemption from competitive bidding requirements are fully set forth in the application and in Exhibit F, attached to the application. They are summarized in the following paragraph of this decision. Additional reasons for requesting an exemption are also contained in a letter from the utility's principal underwriter to the Finance Division staff. The letter from Mr. R. G. Hildreth, Jr., Vice President & Managing Director, Merrill Lynch Pierce Fenner & Smith Inc., is marked as Exhibit 1 in this proceeding.

SDG&E's reasons for requesting an exemption from competitive bidding requirements are summarized as follows:

1. Recent increases in interest rates have had and may continue to have a decided adverse effect on utilities with credit ratings comparable to SDG&E's (Moody's Baa and Standard and Poor's BBB).
2. The rapid rise in interest rates increases the possibility of encountering rate levels of 10% or higher for Baa/BBB rated bonds. This, in turn, raises the issue of California's usury law and its adverse effect on the saleability of debt instruments bearing an interest rate of 10% or more.
3. The current uncertainties surrounding SDG&E's power supply situation, particularly in light of the possible termination of the Sundesert project, and the extent to which the utility would be able to recover the \$89 million thus far invested in the project if it were terminated.

4. The uncertainties pertaining to the utility's ability to meet continuously its interest coverage requirements and to finance adequately its construction program.

In view of the foregoing uncertainties, the marginal rating of SDG&E's bonds (Baa/BBB), and the magnitude of its current financing program (approximately \$200 million for 1978), SDG&E believes and the Finance Division staff concurs that it is essential to have the flexibility and marketing strength provided by a negotiated offering. Additional marketing advantages can also be derived if SDG&E is able to offer the bonds on a negotiated basis concurrently with the offering of its common stock being requested by Application No. 57866 filed February 10, 1978. The Operations Division advises that the funds are needed for the purpose specified in the application.

SDG&E points out that in view of recent increases in interest rates and the utility's current bond ratings ("BBB" by Standard & Poor's Corporation and "Baa" by Moody's Investors Service, Inc.) it is possible that market conditions at the time of the proposed sale may necessitate that the bonds, if they are to be sold, bear an interest rate in excess of 10% per year. A rate in excess of 10% would exceed the limitation contained in Article XV, Section 1 (Interest Rates) of the California Constitution. The utility, therefore, requests that the Commission make appropriate findings consistent with Decisions Nos. 83411 and 85983,^{1/} to the effect that the Commission has the necessary authority to regulate and authorize the utility's proposed bond issue irrespective of the limitations otherwise imposed by the California usury law.

^{1/} Decision No. 83411, dated September 4, 1974 in Application No. 55080 - Southern California Gas Company.

Decision No. 85983, dated June 22, 1976 in Application No. 56490 - San Diego Gas & Electric Company.

In Decisions Nos. 83411 and 85983, among others, the Commission held that in exercising its authority to regulate public utility debt securities, it is not restricted by the California Usury Law and its ramifications.^{2/} We reaffirm this holding and conclude that if the interest limitation of the California Usury Law is exceeded in connection with the proposed bond offering, but it is determined that the transaction is the best the utility can obtain because of market conditions, then the public interest requires this Commission to authorize the issuance and sale of the bonds.

After consideration the Commission finds that:

1. SDG&E's First Mortgage Bonds are presently rated BBB by Standard & Poor's Corporation and Baa by Moody's Investors Service, Inc.
2. The proposed Nineteenth Supplemental Indenture would not be adverse to the public interest.
3. The proposed bonds would be for proper purposes.
4. SDG&E has need for external funds for the purposes set forth in this proceeding.
5. The sale of the proposed bonds should not be required to be through competitive bidding.
6. The money, property or labor to be procured or paid for by the bonds herein authorized is reasonably required for the purposes specified herein, which purposes, except as otherwise authorized for accrued interest, are not, in whole or in part, reasonably chargeable to operating expenses or to income.
7. If prevailing market conditions necessitate that SDG&E's proposed bonds be issued and sold with a rate of interest exceeding the limitations provided in Article XV of the California Constitution, then the public interest requires that this Commission authorize said issuance and sale irrespective of limitations contained in the California Usury Law.

^{2/} The Commission on page 8 of Decision No. 83411 discusses the legal rationale and judicial basis of this holding.

8. Pursuant to plenary powers granted to the Legislature by Article XII, Section 5 of the California Constitution, the Legislature is authorized to confer additional consistent powers upon this Commission as it deems necessary and appropriate, unrestricted by any other provisions of the California Constitution.
9. The Legislature has conferred upon this Commission the authority to regulate the issuance of public utility securities, including evidences of indebtedness, and to prescribe restrictions and conditions as it deems reasonable and necessary (Sections 816 et seq. of the Public Utilities Code).
10. Pursuant to the plenary powers granted to the Legislature in Article XII, Section 5 of the California Constitution, it conferred upon this Commission comprehensive and exclusive power over the issuance of public utility securities, including evidences of indebtedness, and the California Usury Law cannot be applied as a restriction on this Commission's regulation of such issuances of public utility securities, including the establishment of a reasonable rate of interest.
11. In addition to the plenary powers granted to the Legislature by the California Constitution pursuant to which the Legislature conferred upon this Commission exclusive authority to regulate the issuance of bonds by public utilities (Sections 816 et seq. of the Public Utilities Code), irrespective of the Usury Law, judicial interpretation of the California Usury Law has exempted corporate bonds of public utilities from operation of the Usury Law.
12. If the usury limitation contained in Article XV of the California Constitution and the Usury Law Initiative Act is exceeded, but the transaction is authorized by this Commission and is the best SDG&E can obtain because of market conditions, SDG&E, its assignees or successors in interest, will have no occasion to and cannot assert any claim or defense under the California Usury Law; further, and necessarily, because of lawful issuance by applicant of bonds in compliance with authorization by this Commission, persons collecting interest on such authorized bonds are not subject to the Usury Law sanctions.

There is no known opposition and there is no reason to delay granting the authority requested in the application. On the basis of the foregoing findings we conclude that the application should be granted. A public hearing is not necessary. As set forth in said Decisions Nos. 83411 and 85983, among others, we further conclude that the usury limitations on interest contained in Article XV, Section 1, of the California Constitution and the Usury Law Initiative Act do not apply to the issuance of public utility securities, including evidences of indebtedness, such as the bonds, lawfully authorized by the Public Utilities Commission. The authorization herein granted is for the purpose of this proceeding only, and is not to be construed as indicative of the amounts to be included in proceedings for the determination of just and reasonable rates.

SDG&E is hereby placed on notice that if the Commission believes that the negotiated price or interest rate pertaining to the proposed bond issue will result in an excessive effective interest cost, it will take into consideration in rate proceedings only that which it deems reasonable.

This decision is not intended to modify the competitive bidding rule initially established in Decision No. 38614 as amended by the Commission in subsequent decisions in Case No. 4761.

O R D E R

IT IS ORDERED that:

1. The sale by San Diego Gas & Electric Company of not exceeding \$60,000,000 aggregate principal amount of its First Mortgage Bonds, Series R, is hereby exempted from the Commission's competitive bidding rule set forth in Decision No. 38614, dated January 15, 1946, as amended, in Case No. 4761.

2. San Diego Gas & Electric Company may execute and deliver a Nineteenth Supplemental Indenture in substantially the same form as Exhibit E attached to the application, with the modification or insertion of such terms and conditions as interest rate, principal amounts, maturity date, place and manner of payment, choice of law, sinking fund (if any), call protection and other redemption provisions and redemption restrictions as may be contemplated by the application.

3. San Diego Gas & Electric Company may issue and sell not exceeding \$60,000,000 aggregate principal amount of its First Mortgage Bonds, Series R, on terms and conditions to be negotiated as contemplated by the application.

4. An interest rate for San Diego Gas & Electric Company's First Mortgage Bonds, Series R, may exceed the maximum annual interest rate otherwise permitted under the California Usury Law, as contained in Article XV of the California Constitution and the Usury Law Initiative Act, if market conditions so require.

5. Neither San Diego Gas & Electric Company, nor anyone purporting to act on its behalf, shall at any time assert in any manner, or attempt to raise as a claim or defense in any proceeding, that the interest on its First Mortgage Bonds, Series R, exceeds the maximum permitted to be charged under the California Usury Law or any similar law establishing the maximum rate of interest that can be charged to or received from a borrower.

6. San Diego Gas & Electric Company shall use the net proceeds from the sale of said bonds for the purposes referred to in the application.

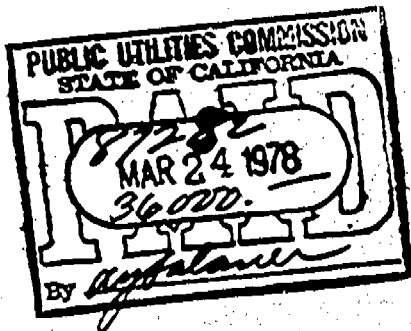
7. Upon determining the price, interest rate and other terms pertaining to the bonds herein authorized, San Diego Gas & Electric Company shall notify the Commission thereof in writing.

8. As soon as available, San Diego Gas & Electric Company shall file with the Commission three copies of its final prospectus pertaining to said bonds.

9. San Diego Gas & Electric Company shall file with the Commission a report, or reports, as required by General Order No. 24-B, which order, insofar as applicable, is hereby made a part of this order.

10. This order shall become effective when San Diego Gas & Electric Company has paid the fee prescribed by Section 1904(b) of the Public Utilities Code, which fee is \$36,000.

Dated at San Francisco, California, this 21st day of MARCH 1, 1978.



Robert Bateman
President
William [unclear]
Virginia [unclear]
[unclear]
Clare T. DeWitt
Commissioners