# EQUITY RESEARCH | INSTANT INSIGHTS 25 April 2011 Daniel Ford, CFA +1 212 526 0836 dan.ford@barcap.com BCI, New York Ross A. Fowler, CFA +1 617 330 5893 ross.fowler@barcap.com BCI, New York

# PCG (2-EW / 1-Positive, \$45.18, \$53 PT)

## Details of Darbee's Departure

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Current CEO and Chairman of the Board, and President of PG&E Corporation, Peter Darbee, 58, announced late on Thursday April 21st, in what we view as a somewhat surprising move, that he would step down and retire from both positions effective April 30th, 2011. Mr. Darbee joined PG&E Corporation in 1999 as Chief Financial Officer. He was appointed CEO in 2005 and assumed the additional role of Chairman of the Board in 2006. In an 8-K the company indicated that the Board of Directors already has a search underway for Mr. Darbee's successor. Until completion of the search the Board has appointed C. Lee Cox, 70, to serve as interim Chairman of the Board, CEO, and President of PG&E Corporation. Mr. Cox has been a Director of PG&E Corporation since 1996 and non-executive Chairman of the Utility's Board of Directors since the beginning of 2008. He is also the independent lead director of PG&E Corporation and the Utility. While Mr. Cox serves in his interim roles he cannot, according to the by-laws of the company maintain his role as independent lead Director. The Board has thus appointed Maryellen C. Herringer, a current Director of the Corporation and the Utility to serve as independent lead director of both of those entities. Further, current Director Barbara L. Rambo will replace Mr. Cox as the interim Chair of the Compensation Committee. Mr. Cox has also resigned from the Finance Committee.

Since Mr. Darbee is retiring, he will not be eligible for any severance payment or other severance benefits. He will however receive the retirement and pension benefits as disclosed in the company's most recent proxy statement. The Board also approved a retention award for current President of the Utility, Christopher P. Johns for RSUs worth \$1 million with an expected grant date of May 6th, 2011. One-half of the RSUs will vest on the second anniversary of the date of grant and the remainder will vest on the third anniversary of the date of grant provided that Mr. Johns remains an employee on each vesting date. The RSUs will vest sooner if Mr. Johns dies or becomes disabled. If Mr. Johns' employment with the Utility is terminated without cause, his RSUs will vest to the extent provided under the PG&E Corporation Officer Severance Policy. The San Bruno Patch ("PG&E Corp. CEO Steps Down in Wake of Pipeline Explosion", April 22nd, 2011, by Martin Ricard, http://sanbruno.patch.com/articles/pge-corp-ceo-steps-down-in-wake-of-pipeline-explosion) quoted Darbee's retirement package as worth approximately \$35 million.

## Our Thoughts

As we noted above we view the departure of Mr. Darbee as somewhat surprising, considering the CEO role at PG&E Corp did not change during the company's bankruptcy. This to us, is indicatory of the amount of public relations and political pressure the company has come under following,

what the company states in its own press release as a "challenging year". We would note that the largest political and regulatory pressure has certainly come as a result of the San Bruno pipeline explosion last fall, but would also note that the company came under some scrutiny for a ballot initiative last year that would have required super majority votes to municipalize electricity service. Further scrutiny has been occurring around the company's Advance Smart Meter installation program, and the potential relicensing of the Diablo Canyon nuclear power plant. We would note that while this is an important and significant first step, we believe that further steps will need to be taken for PG&E to satisfy regulators, politicians, and the public.

In a San Francisco Chronicle Article ("PG&E Searches for a New CEO to Replace Peter Darbee", April 23rd, 2011, by David R. Baker, http://www.sfgate.com/cgi-

bin/article.cgi?f=/c/a/2011/04/22/BU601J64SN.DTL), Current President of the California Public Utilities Commission (CPUC) was quoted as saying, "As PG&E's Board of Directors recruits a successor, the CPUC urges the company to return to its roots by hiring the most technically competent person, someone with a long-standing history of performance in the energy industry." We are of the opinion that given the challenging history of the past year that an external candidate with a strong operational background would make the best candidate for the position and do not believe an internal candidate is currently viable. In the same San Francisco Chronicle article, Assemblyman Jerry Hill, who represents San Bruno was quoted, "It has to be someone from the outside, someone who can come in with no baggage. The utility industry and the regulators seem to have an incestuous relationship." Mark Toney, Executive Director of The Utility Reform Network, TURN, also was quoted as saying, "We've *had* someone from outside the industry running the utility. They need someone who can rebuild internally as well as rebuild their relations with the customers." The company's press release also noted that the Board would make an announcement in the "coming weeks" indicating to us that the search has probably already been underway and that the Board at the least has a short list of potential candidate.

We believe that while Mr. Darbee's departure is a albeit surprising large first step on the part of the company, that there are still several challenging catalysts ahead, including: decisions around both a potential moratorium on SmartMeters, the coming decision on the company's Electric GRC by the CPUC, a decision around and seismic studies to be conducted for the Diablo Canyon relicensing process, the hearings and conclusions both at the National Transportation Safety Board (NTSB) and the CPUC concerning the San Bruno pipeline explosion and the company's record keeping practices of acceptable operational pressures in it's pipeline network, and lastly, the process, beginning in April 2012 of determining both an ongoing methodology for determining returns on equity in California and the allowed ROEs for the 2013 calendar year.

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