

# Independent panel releases report on San Bruno and PCG

**Bank of America  
Merrill Lynch** 

**Steve Fleishman** +1 646 855 2906  
Research Analyst  
MLPF&S  
steven.fleishman@baml.com

**Naaz Khumawala** +1 713 247 7313  
Research Analyst  
MLPF&S  
naaz.khumawala@baml.com

## Independent review panel releases recommendations

An independent review panel appointed by the California Public Utilities Commission (CPUC) released recommendations on pipeline safety, PCG practices and the CPUC oversight. The report was critical of gas operations at PCG, citing a lack of oversight of the safety of the gas transmission system and lack of standalone gas operations. For the PUC, the panel recommended the PUC move to a performance based regulatory oversight of utility pipeline safety and increased staff, including consultants to provide technical oversight.

## Recommendations to PCG both operational and managerial

The panel's recommendations to PCG include 1) undertaking a thorough review of integrity management; 2) commission an independent audit of the gas transmission and distribution functions; 3) establish multi-year program to collect and correct operating data for the gas transmission system; and 4) ensure gas transmission management have thorough gas transmission operations knowledge. The panel also was critical of PCG's proposed Pipeline 2020 program saying that it needed to be better reasoned.

## CPUC passes OIR pipeline plan

CPUC passed the ALJ proposed decision for the OIR on natural gas safety. The decision orders PCG and SRE to file a comprehensive plan to cost effectively replace or test all gas pipeline that have not been pressure tested. The plan must include a prioritized schedule, cost estimates and proposed ratemaking. PCG only, must include a proposed cost sharing mechanism between ratepayers and shareholders. For more information please see "[ALJ on nat gas safety plan.](#)"

## Believe our estimates reflect a reasonable worst case

We believe our current estimates (2012-2013: \$3.60/sh area) reflect a reasonable worst case scenario for PCG for the San Bruno disaster. We assume \$450M of San Bruno costs each year in 2011 and 2012. We assume \$400M of equity in 2011 and \$700M of equity in 2012 to fund capex and San Bruno costs. We currently do not assume any upside from potential recovery of pipeline capex spend related to San Bruno. That said, we continue to believe San Bruno and its ramifications will likely get worse before it gets better.

## Next steps; CEO search outstanding

A pipeline testing implementation plan is due within 60 days for both PCG and SRE. The NTSB investigation is expected to issue a final report this Fall. The Order Instituting an Investigation (OII) will likely result in fines by year-end or early 2012. The CEO search remains ongoing.

## Stock Data

|                          |                |
|--------------------------|----------------|
| Price                    | US\$41.96      |
| Price Objective          | US\$48.00      |
| Date Established         | 12-Apr-2011    |
| Investment Opinion       | A-1-7          |
| Volatility Risk          | LOW            |
| BofAML Ticker / Exchange | PCG / NYS      |
| Bloomberg / Reuters      | PCG US / PCG.N |

BofA Merrill Lynch does and seeks to do business with companies covered in its research reports. As a result, investors should be aware that the firm may have a conflict of interest that could affect the objectivity of this report. Investors should consider this report as only a single factor in making their investment decision.

Refer to important disclosures on page 3 to 6. Analyst Certification on Page 2. Price Objective Basis/Risk on page 2. Link to Definitions on page 2. 11058764

## **Price objective basis & risk**

### **PG&E Corporation (PCG)**

Our \$48 price objective assumes a P/E of 13.25x 2013E earnings. This is a modest premium to the industry average as we expect likely upside to our estimates. Risks to our outlook are: 1) liability related to the San Bruno explosion, 2) approval of the settlement in the 2011 general rate case and 3) Any unforeseen changes to California regulation.

## **Link to Definitions**

### **Energy**

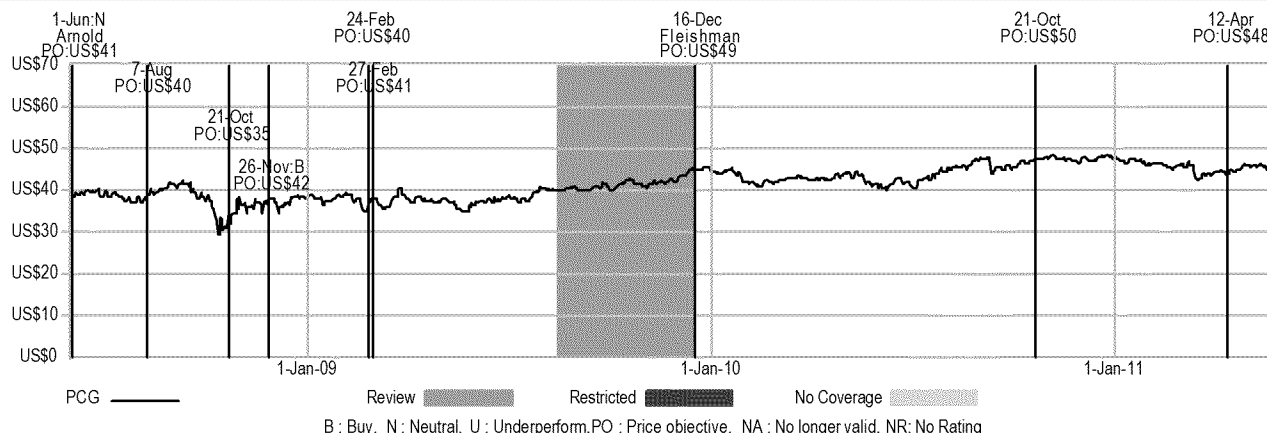
Click [here](#) for definitions of commonly used terms.

## **Analyst Certification**

I, Steve Fleishman, hereby certify that the views expressed in this research report accurately reflect my personal views about the subject securities and issuers. I also certify that no part of my compensation was, is, or will be, directly or indirectly, related to the specific recommendations or view expressed in this research report.

## Important Disclosures

### PCG Price Chart



The Investment Opinion System is contained at the end of the report under the heading "Fundamental Equity Opinion Key". Dark grey shading indicates the security is restricted with the opinion suspended. Medium grey shading indicates the security is under review with the opinion withdrawn. Light grey shading indicates the security is not covered. Chart is current as of [May 31, 2011] or such later date as indicated.

#### Investment Rating Distribution: Utilities Group (as of 01 Apr 2011)

| Coverage Universe | Count | Percent | Inv. Banking Relationships* | Count | Percent |
|-------------------|-------|---------|-----------------------------|-------|---------|
| Buy               | 77    | 42.08%  | Buy                         | 33    | 47.83%  |
| Neutral           | 53    | 28.96%  | Neutral                     | 33    | 68.75%  |
| Sell              | 53    | 28.96%  | Sell                        | 18    | 38.30%  |

#### Investment Rating Distribution: Global Group (as of 01 Apr 2011)

| Coverage Universe | Count | Percent | Inv. Banking Relationships* | Count | Percent |
|-------------------|-------|---------|-----------------------------|-------|---------|
| Buy               | 2009  | 53.66%  | Buy                         | 912   | 49.89%  |
| Neutral           | 955   | 25.51%  | Neutral                     | 439   | 50.93%  |
| Sell              | 780   | 20.83%  | Sell                        | 257   | 35.11%  |

\* Companies in respect of which BofA Merrill Lynch or one of its affiliates has received compensation for investment banking services within the past 12 months. For purposes of this distribution, a stock rated Underperform is included as a Sell.

**FUNDAMENTAL EQUITY OPINION KEY:** Opinions include a Volatility Risk Rating, an Investment Rating and an Income Rating. **VOLATILITY RISK RATINGS**, indicators of potential price fluctuation, are: A - Low, B - Medium and C - High. **INVESTMENT RATINGS** reflect the analyst's assessment of a stock's: (i) absolute total return potential and (ii) attractiveness for investment relative to other stocks within its Coverage Cluster (defined below). There are three investment ratings: 1 - Buy stocks are expected to have a total return of at least 10% and are the most attractive stocks in the coverage cluster; 2 - Neutral stocks are expected to remain flat or increase in value and are less attractive than Buy rated stocks and 3 - Underperform stocks are the least attractive stocks in a coverage cluster. Analysts assign investment ratings considering, among other things, the 0-12 month total return expectation for a stock and the firm's guidelines for ratings dispersions (shown in the table below). The current price objective for a stock should be referenced to better understand the total return expectation at any given time. The price objective reflects the analyst's view of the potential price appreciation (depreciation).

| Investment rating | Total return expectation (within 12-month period of date of initial rating) | Ratings dispersion guidelines for coverage cluster* |
|-------------------|---|---|
| Buy               | ≥ 10%   | ≤ 70%   |
| Neutral           | ≥ 0%  | ≤ 30%   |
| Underperform      | N/A   | ≥ 20%   |

\* Ratings dispersions may vary from time to time where BofA Merrill Lynch Research believes it better reflects the investment prospects of stocks in a Coverage Cluster.

**INCOME RATINGS**, indicators of potential cash dividends, are: 7 - same/higher (dividend considered to be secure), 8 - same/lower (dividend not considered to be secure) and 9 - pays no cash dividend. Coverage Cluster is comprised of stocks covered by a single analyst or two or more analysts sharing a common industry, sector, region or other classification(s). A stock's coverage cluster is included in the most recent BofA Merrill Lynch Comment referencing the stock.

Price charts for the securities referenced in this research report are available at <http://pricecharts.ml.com>, or call 1-800-MERRILL to have them mailed. MLPF&S or one of its affiliates acts as a market maker for the equity securities recommended in the report: PG&E Corp. The company is or was, within the last 12 months, an investment banking client of MLPF&S and/or one or more of its affiliates: PG&E Corp. MLPF&S or an affiliate has received compensation from the company for non-investment banking services or products within the past 12 months: PG&E Corp. The company is or was, within the last 12 months, a non-securities business client of MLPF&S and/or one or more of its affiliates: PG&E Corp. MLPF&S or an affiliate has received compensation for investment banking services from this company within the past 12 months: PG&E Corp. MLPF&S or an affiliate expects to receive or intends to seek compensation for investment banking services from this company or an affiliate of the company within the next three months: PG&E Corp. MLPF&S or one of its affiliates is willing to sell to, or buy from, clients the common equity of the company on a principal basis: PG&E Corp.

BofA Merrill Lynch Research personnel (including the analyst(s) responsible for this report) receive compensation based upon, among other factors, the overall profitability of Bank of America Corporation, including profits derived from investment banking revenues.

MLPF&S is affiliated with an NYSE Designated Market Maker (DMM) that specializes in one or more securities issued by the subject companies. This affiliated NYSE DMM makes a market in, and may maintain a long or short position in or be on the opposite side of orders executed on the Floor of the NYSE in connection with one or more of the securities issued by these companies: PG&E Corp.

## Other Important Disclosures

MLPF&S or one of its affiliates has a significant financial interest in the fixed income instruments of the issuer. If this report was issued on or after the 8th day of a month, it reflects a significant financial interest on the last day of the previous month. Reports issued before the 8th day of a month reflect a significant financial interest at the end of the second month preceding the date of the report: PG&E Corp.

Officers of MLPF&S or one or more of its affiliates (other than research analysts) may have a financial interest in securities of the issuer(s) or in related investments.

**BofA Merrill Lynch Global Research policies relating to conflicts of interest are described at <http://www.ml.com/media/43347.pdf>.**

**"BofA Merrill Lynch" includes Merrill Lynch, Pierce, Fenner & Smith Incorporated ("MLPF&S") and its affiliates. Investors should contact their BofA Merrill Lynch representative or Merrill Lynch Global Wealth Management financial advisor if they have questions concerning this report.**

**Information relating to Non-US affiliates of BofA Merrill Lynch and Distribution of Affiliate Research Reports:**

MLPF&S distributes, or may in the future distribute, research reports of the following non-US affiliates in the US (short name; legal name): Merrill Lynch (France): Merrill Lynch Capital Markets (France) SAS; Merrill Lynch (Frankfurt): Merrill Lynch International Bank Ltd., Frankfurt Branch; Merrill Lynch (South Africa): Merrill Lynch South Africa (Pty) Ltd.; Merrill Lynch (Milan): Merrill Lynch International Bank Limited; MLI (UK): Merrill Lynch International; Merrill Lynch (Australia): Merrill Lynch Equities (Australia) Limited; Merrill Lynch (Hong Kong): Merrill Lynch (Asia Pacific) Limited; Merrill Lynch (Singapore): Merrill Lynch (Singapore) Pte Ltd.; Merrill Lynch (Canada): Merrill Lynch Canada Inc; Merrill Lynch (Mexico): Merrill Lynch Mexico, SA de CV, Casa de Bolsa; Merrill Lynch (Argentina): Merrill Lynch Argentina SA; Merrill Lynch (Japan): Merrill Lynch Japan Securities Co., Ltd.; Merrill Lynch (Seoul): Merrill Lynch International Incorporated (Seoul Branch); Merrill Lynch (Taiwan): Merrill Lynch Securities (Taiwan) Ltd.; DSP Merrill Lynch (India): DSP Merrill Lynch Limited; PT Merrill Lynch (Indonesia): PT Merrill Lynch Indonesia; Merrill Lynch (Israel): Merrill Lynch Israel Limited; Merrill Lynch (Russia): Merrill Lynch CIS Limited, Moscow; Merrill Lynch (Turkey): Merrill Lynch Yatirim Bankasi A.S.; Merrill Lynch (Dubai): Merrill Lynch International, Dubai Branch; MLPF&S (Zürich rep. office): MLPF&S Incorporated Zürich representative office; Merrill Lynch (Spain): Merrill Lynch Capital Markets Espana, S.A.S.V.; Merrill Lynch (Brazil): Banco Merrill Lynch de Investimentos S.A.

This research report has been approved for publication and is distributed in the United Kingdom to professional clients and eligible counterparties (as each is defined in the rules of the Financial Services Authority) by Merrill Lynch International and Banc of America Securities Limited (BASL), which are authorized and regulated by the Financial Services Authority and has been approved for publication and is distributed in the United Kingdom to retail clients (as defined in the rules of the Financial Services Authority) by Merrill Lynch International Bank Limited, London Branch, which is authorized by the Central Bank of Ireland and is subject to limited regulation by the Financial Services Authority – details about the extent of its regulation by the Financial Services Authority are available from it on request; has been considered and distributed in Japan by Merrill Lynch Japan Securities Co., Ltd., a registered securities dealer under the Financial Instruments and Exchange Act in Japan; is distributed in Hong Kong by Merrill Lynch (Asia Pacific) Limited, which is regulated by the Hong Kong SFC and the Hong Kong Monetary Authority; is issued and distributed in Taiwan by Merrill Lynch Securities (Taiwan) Ltd.; is issued and distributed in India by DSP Merrill Lynch Limited; and is issued and distributed in Singapore by Merrill Lynch International Bank Limited (Merchant Bank) and Merrill Lynch (Singapore) Pte Ltd. (Company Registration No.'s F 06872E and 198602883D respectively) and Bank of America Singapore Limited (Merchant Bank). Merrill Lynch International Bank Limited (Merchant Bank) and Merrill Lynch (Singapore) Pte Ltd. are regulated by the Monetary Authority of Singapore. Merrill Lynch Equities (Australia) Limited (ABN 65 006 276 795), AFS License 235132 provides this report in Australia in accordance with section 911B of the Corporations Act 2001 and neither it nor any of its affiliates involved in preparing this research report is an Authorised Deposit-Taking Institution under the Banking Act 1959 nor regulated by the Australian Prudential Regulation Authority. No approval is required for publication or distribution of this report in Brazil. Merrill Lynch (Dubai) is authorized and regulated by the Dubai Financial Services Authority (DFSA). Research reports prepared and issued by Merrill Lynch (Dubai) are prepared and issued in accordance with the requirements of the DFSA conduct of business rules.

Merrill Lynch (Frankfurt) distributes this report in Germany. Merrill Lynch (Frankfurt) is regulated by BaFin.

This research report has been prepared and issued by MLPF&S and/or one or more of its non-US affiliates. MLPF&S is the distributor of this research report in the US and accepts full responsibility for research reports of its non-US affiliates distributed to MLPF&S clients in the US. Any US person receiving this research report and wishing to effect any transaction in any security discussed in the report should do so through MLPF&S and not such foreign affiliates.

### General Investment Related Disclosures:

This research report provides general information only. Neither the information nor any opinion expressed constitutes an offer or an invitation to make an offer, to buy or sell any securities or other financial instrument or any derivative related to such securities or instruments (e.g., options, futures, warrants, and contracts for differences). This report is not intended to provide personal investment advice and it does not take into account the specific investment objectives, financial situation and the particular needs of any specific person. Investors should seek financial advice regarding the appropriateness of investing in financial instruments and implementing investment strategies discussed or recommended in this report and should understand that statements regarding future prospects may not be realized. Any decision to purchase or subscribe for securities in any offering must be based solely on existing public information on such security or the information in the prospectus or other offering document issued in connection with such offering, and not on this report.

Securities and other financial instruments discussed in this report, or recommended, offered or sold by Merrill Lynch, are not insured by the Federal Deposit Insurance Corporation and are not deposits or other obligations of any insured depository institution (including, Bank of America, N.A.). Investments in general and, derivatives, in particular, involve numerous risks, including, among others, market risk, counterparty default risk and liquidity risk. No security, financial instrument or derivative is suitable for all investors. In some cases, securities and other financial instruments may be difficult to value or sell and reliable information about the value or risks related to the security or financial instrument may be difficult to obtain. Investors should note that income from such securities and other financial instruments, if any, may fluctuate and that price or value of such securities and instruments may rise or fall and, in some cases, investors may lose their entire principal investment. Past performance is not necessarily a guide to future performance. Levels and basis for taxation may change.

This report may contain a short-term trading idea or recommendation, which highlights a specific near-term catalyst or event impacting the company or the market that is anticipated to have a short-term price impact on the equity securities of the company. Short-term trading ideas and recommendations are different from and do not affect a stock's fundamental equity rating, which reflects both a longer term total return expectation and attractiveness for investment relative to other stocks within its Coverage Cluster. Short-term trading ideas and recommendations may be more or less positive than a stock's fundamental equity rating.

BofA Merrill Lynch is aware that the implementation of the ideas expressed in this report may depend upon an investor's ability to "short" securities or other financial instruments and that such action may be limited by regulations prohibiting or restricting "shortselling" in many jurisdictions. Investors are urged to seek advice regarding the applicability of such regulations prior to executing any short idea contained in this report.

Foreign currency rates of exchange may adversely affect the value, price or income of any security or financial instrument mentioned in this report. Investors in such securities and instruments, including ADRs, effectively assume currency risk.

UK Readers: The protections provided by the U.K. regulatory regime, including the Financial Services Scheme, do not apply in general to business coordinated by BofA Merrill Lynch entities located outside of the United Kingdom. BofA Merrill Lynch Global Research policies relating to conflicts of interest are described at <http://www.ml.com/media/43347.pdf>.

Officers of MLPF&S or one or more of its affiliates (other than research analysts) may have a financial interest in securities of the issuer(s) or in related investments.

MLPF&S or one of its affiliates is a regular issuer of traded financial instruments linked to securities that may have been recommended in this report. MLPF&S or one of its affiliates may, at any time, hold a trading position (long or short) in the securities and financial instruments discussed in this report.

BofA Merrill Lynch, through business units other than BofA Merrill Lynch Global Research, may have issued and may in the future issue trading ideas or recommendations that are inconsistent with, and reach different conclusions from, the information presented in this report. Such ideas or recommendations reflect the different time frames, assumptions, views and analytical methods of the persons who prepared them, and BofA Merrill Lynch is under no obligation to ensure that such other trading ideas or recommendations are brought to the attention of any recipient of this report.

In the event that the recipient received this report pursuant to a contract between the recipient and MLPF&S for the provision of research services for a separate fee, and in connection therewith MLPF&S may be deemed to be acting as an investment adviser, such status relates, if at all, solely to the person with whom MLPF&S has contracted directly and does not extend beyond the delivery of this report (unless otherwise agreed specifically in writing by MLPF&S). MLPF&S is and continues to act solely as a broker-dealer in connection with the execution of any transactions, including transactions in any securities mentioned in this report.

**Copyright and General Information regarding Research Reports:**

Copyright 2011 Merrill Lynch, Pierce, Fenner & Smith Incorporated. All rights reserved. iQmethod, iQmethod 2.0, iQprofile, iQtoolkit, iQworks are service marks of Merrill Lynch & Co., Inc. iQanalytics®, iQcustom®, iQdatabase® are registered service marks of Merrill Lynch & Co., Inc. This research report is prepared for the use of BofA Merrill Lynch clients and may not be redistributed, retransmitted or disclosed, in whole or in part, or in any form or manner, without the express written consent of BofA Merrill Lynch. BofA Merrill Lynch Global Research reports are distributed simultaneously to internal and client websites and other portals by BofA Merrill Lynch and are not publicly-available materials. Any unauthorized use or disclosure is prohibited. Receipt and review of this research report constitutes your agreement not to redistribute, retransmit, or disclose to others the contents, opinions, conclusion, or information contained in this report (including any investment recommendations, estimates or price targets) without first obtaining expressed permission from an authorized officer of BofA Merrill Lynch.

Materials prepared by BofA Merrill Lynch Global Research personnel are based on public information. Facts and views presented in this material have not been reviewed by, and may not reflect information known to, professionals in other business areas of BofA Merrill Lynch, including investment banking personnel. BofA Merrill Lynch has established information barriers between BofA Merrill Lynch Global Research and certain business groups. As a result, BofA Merrill Lynch does not disclose certain client relationships with, or compensation received from, such companies in research reports. To the extent this report discusses any legal proceeding or issues, it has not been prepared as nor is it intended to express any legal conclusion, opinion or advice. Investors should consult their own legal advisers as to issues of law relating to the subject matter of this report. BofA Merrill Lynch Global Research personnel's knowledge of legal proceedings in which any BofA Merrill Lynch entity and/or its directors, officers and employees may be plaintiffs, defendants, co-defendants or co-plaintiffs with or involving companies mentioned in this report is based on public information. Facts and views presented in this material that relate to any such proceedings have not been reviewed by, discussed with, and may not reflect information known to, professionals in other business areas of BofA Merrill Lynch in connection with the legal proceedings or matters relevant to such proceedings.

This report has been prepared independently of any issuer of securities mentioned herein and not in connection with any proposed offering of securities or as agent of any issuer of any securities. None of MLPF&S, any of its affiliates or their research analysts has any authority whatsoever to make any representation or warranty on behalf of the issuer(s). BofA Merrill Lynch Global Research policy prohibits research personnel from disclosing a recommendation, investment rating, or investment thesis for review by an issuer prior to the publication of a research report containing such rating, recommendation or investment thesis.

Any information relating to the tax status of financial instruments discussed herein is not intended to provide tax advice or to be used by anyone to provide tax advice. Investors are urged to seek tax advice based on their particular circumstances from an independent tax professional.

The information herein (other than disclosure information relating to BofA Merrill Lynch and its affiliates) was obtained from various sources and we do not guarantee its accuracy. This report may contain links to third-party websites. BofA Merrill Lynch is not responsible for the content of any third-party website or any linked content contained in a third-party website. Content contained on such third-party websites is not part of this report and is not incorporated by reference into this report. The inclusion of a link in this report does not imply any endorsement by or any affiliation with BofA Merrill Lynch. Access to any third-party website is at your own risk, and you should always review the terms and privacy policies at third-party websites before submitting any personal information to them. BofA Merrill Lynch is not responsible for such terms and privacy policies and expressly disclaims any liability for them.

Subject to the quiet period applicable under laws of the various jurisdictions in which we distribute research reports and other legal and BofA Merrill Lynch policy-related restrictions on the publication of research reports, fundamental equity reports are produced on a regular basis as necessary to keep the investment recommendation current.

Certain outstanding reports may contain discussions and/or investment opinions relating to securities, financial instruments and/or issuers that are no longer current. Always refer to the most recent research report relating to a company or issuer prior to making an investment decision.

In some cases, a company or issuer may be classified as Restricted or may be Under Review or Extended Review. In each case, investors should consider any investment opinion relating to such company or issuer (or its security and/or financial instruments) to be suspended or withdrawn and should not rely on the analyses and investment opinion(s) pertaining to such issuer (or its securities and/or financial instruments) nor should the analyses or opinion(s) be considered a solicitation of any kind. Sales persons and financial advisors affiliated with MLPF&S or any of its affiliates may not solicit purchases of securities or financial instruments that are Restricted or Under Review and may only solicit securities under Extended Review in accordance with firm policies.

Neither BofA Merrill Lynch nor any officer or employee of BofA Merrill Lynch accepts any liability whatsoever for any direct, indirect or consequential damages or losses arising from any use of this report or its contents.