BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

Order Instituting Rulemaking on the Commission's Own Motion to Consider Effectiveness and Adequacy of the Competitive Bidding Rule for Issuance of Securities and Associated Impacts of General Order 156, Debt Enhancement Features, and General Order 24-B.	Rulemaking 11-03-007 (Filed March 10, 2011)

WORKSHOP REPORT

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January 20, 2012

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WORKSHOP REPORT

I. INTRODUCTION

Pursuant to the oral requests of Commissioner Timothy Simon and Administrative Law Judge (ALJ) Sean Wilson at the January 9, 2012 Workshop in the above proceeding, Pacific Gas and Electric Company (PG&E), Southern California Edison (SCE), Sempra Energy Utilities (SEU), and Southwest Gas (SWG) hereby submit this Workshop Report on the issues presented.

II. PROCEDURAL BACKGROUND

On November 15, 2011, Assigned Commissioner Simon and ALJ Wilson issued a Scoping Memo and Ruling (Ruling) determining the scope, schedule, and need for a workshop in this proceeding to Rulemaking (R.) 11-13-007. The Ruling allowed for workshops on January 9 and 10, 2012 and ruled that parties could file and serve Pre-Workshop Statements by January 4, 2012.

On January 9, 2012, pursuant to the Ruling, the Commissioner Simon and ALJ Wilson held the first workshop in San Francisco. During the workshop parties discussed their responses to the questions listed in Attachment A of the Ruling as well as all other issues deemed pertinent to this proceeding. At the end of the proceedings on January 9, Commissioner Simon and ALJ Wilson concluded that hearings on January 10 would not

be necessary and asked the larger utility participants to work together and submit a workshop report subject to comment on the issues presented. The following is a summary of the workshop discussions. Proposed revisions to the Competitive Bidding Rule and to General Order (G.O.) 24-B are attached to this report as Appendix A. Appendix B to this report is a list of participants generated from the sign-in sheet circulated at the workshop. In preparing this report, the above-named parties attempted to capture the essence of comments, and not the exact wording. Also, some comments were duplicative and were therefore not restated.

III. OPENING REMARKS

Commissioner Simon started the proceeding by thanking everyone for attending and noting that many in attendance had come from around the country. He stated that the attendance says a lot about the commitment to the process and to making sure that the Commission is doing its best to ensure that the investor-owned utilities which go into the market under Public Utilities Code Section 816 are engaging in the best interests of the ratepayers. The Commissioner also stated that part of the best interest of the ratepayers is making sure that utilities engage many of the professionals who bring their skills into the capital markets into this process.

Commissioner Simon stated that he initiated this Rulemaking in response to his dissenting opinions in each of PG&E's and SCE's earlier financing decisions, wherein he questioned the effectiveness and adequacy of the competitive bidding rule in part based on financing approvals using long-term three year projections of capital expenditures, exemptions from the competitive bidding rule without conclusive showings that exemptions were in the best interest of ratepayers, and a lack of any showing that the utilities' financial services procurement are included in the G.O. 156 program goals.

Commissioner Simon recognized that utilities need access to capital to finance operations, upgrade facilities and for critical infrastructure projects. He also noted that numerous parties filed responses in the proceedings and that the consensus seemed to be that the competitive bidding rule is outdated.

Commissioner Simon noted that this is the first time since 1986 that anyone has taken an opportunity to amend or modify this process while noting that we cannot just get rid of the rules because they are outdated. The Commissioner stated that he would prefer to update the rules to reflect the current financial market environment without exposing the ratepayers to excessive risk. He stated that he looked forward to listening to everyone discuss how the Commission could improve the current outdated competitive bidding rule with more efficient and reasonable rules while providing opportunities for Diverse Business Enterprise (DBE) firms in financial transactions.

Commissioner Simon commended the investor-owned utilities for working with his office to change the level of DBE participation in public offerings. The Commissioner stated that, to date, California is leading the nation in creating opportunities for diverse and emerging firms. He concluded by stating that he believed this proceeding could result in a better rule, noting that the parties' commitment to the process had led to the accomplishments experienced in this part of the utility marketplace to date.

IV. WORKSHOP DISCUSSIONS

A. Competitive Bidding Rule (Rule)

1. Section 1: Competitive Bidding of Debt Issues

Gary Hayes, speaking on behalf of *SEU,* noted that the original Rule, which was drafted in 1946 and last amended in 1986, does not reflect major changes in information

flow, issuer behavior and market structure since its adoption. As a result, the current industry standard for long-term debt financing is the use of a method referred to as negotiated bidding. He further stated that competitive bidding is rarely if ever used to issue debt in today's financial markets.

Ted Wood of *SWG* added that negotiated bidding in today's financial environment is the best means for companies to achieve the concurrent goals of low-cost financing and DBE inclusion. He went on to mention that SWG is a small and infrequent issuer of debt and therefore, negotiated underwriting provides SWG with the ability to manage its existing banking relationships effectively.

Bob Boada of *SCE* pointed out that the terminology used to differentiate competitive bidding and negotiated bidding is not helpful. Negotiated bidding is actually a very competitive process. This process allows utilities and companies alike to access capital effectively and at a reasonable cost. He went on to state that unlike competitive bidding that relies on underwriter competition, negotiated bidding incorporates investor or debt-holder competition, allowing utilities to achieve the best possible terms for ratepayers.

Kathleen Brennan De Jesus of *SCE* used the example of the Securities and Exchange Commission's (SEC) revocation of its Rule 50 (requiring competitive bidding of financing under the Public Utility Holding Company Act) in 1994. The SEC stated at that time that there was already enough information in the marketplace to ensure competition, and therefore the rule was no longer needed.

Doreen Ludemann of *PG&E* added that from her viewpoint there is little remaining in the Rule which is of value in today's financial environment. She noted the lack of proponents who supported the retention of the Rule as proposed.

Clifford Swint and *Sidney Dillard* of *MFR Securities* and *Loop Securities,* respectively, concurred that that there was no need for the Rule in its current form. Ms. Dillard stated that the terminology is a misnomer. Supporting SCE's position, she pointed out that negotiated bids are very competitive and they result in better pricing. Further, the Trade Reporting and Compliance Engine (TRACE)[1] provides transparency regarding pricing for bonds and eliminates the need for the Rule.

Michael Turner of *Castle Oak Securities,* in response to a question from ALJ Wilson regarding whether negotiated deals are competitive, mentioned that negotiated deals lead to competition between investors. As a result of this competition, spreads tighten after an announcement as investors bid, even in a volatile environment. He went on to cite an example where in 2011, an SDG&E deal was a launched with expectations of a 90-95 basis point spread. As the deal was oversubscribed, the spread tightened to 78 basis points over the course of the day. Without negotiated bidding, he stated that the price would likely have remained at the 90-95 basis point level.

Bob Boada of *SCE* added that negotiated bids will always beat competitive bids in theory, because they are direct sales to investors, without the middleman, or brokered (underwriter), sale. He added that the middleman would want to be compensated for the risk associated with the offering, which would consequently increase the cost to

[1] On January 23, 2001, the Securities and Exchange Commission approved proposed rules requiring the Financial Industry National Regulatory Authority (FINRA) members to report over-the-counter secondary market transactions in eligible fixed income securities to FINRA and subject certain transaction reports to dissemination. In July 2002, FINRA introduced the Trade Reporting and Compliance Engine (TRACE) to facilitate this mandatory reporting, which provides increased price transparency in the U.S. corporate debt market. The system captures and disseminates consolidated information on secondary market transactions in publicly traded TRACE-eligible securities (investment grade, high yield and convertible corporate debt) - representing all over-the-counter market activity in these bonds. (Source: http://www.finra.org)

ratepayers. From an issuance perspective, he mentioned that of the 500 utility deals done since 2008, none had been competitively bid, and looking back a year before that, only one was competitively bid.

Clifford Swint of *MFR Securities* added that the pool of investor bidders provides access to trillions of dollars of capital in negotiated bids, versus billions of dollars through the big money banks in competitive bidding. He also said that investors in negotiated bids also tend to buy to hold, while underwriters in competitive bids buy to flip and make a profit. Negotiated bidding will naturally evoke the best pricing.

David Finkelstein of Williams Securities agreed that negotiated bids provide better pricing than competitive bids and stated that in negotiated bids investors compete on price to the point of pain, dropping out only when the spreads are unacceptable.

Ted Wood of *SWG* added that negotiated bids provide utilities with the flexibility to alter the size and terms of an issuance.

Commissioner Simon pointed out that that in addition to achieving low cost, there is the issue of tying in the packaging of services by banks. He mentioned that it would be helpful to the Commission to show that negotiated bids are still competitive in nature despite the current terminology. He said that the Rule is ripe for change; however, nomenclature will be critical in implementing any changes to the rule.
He acknowledged that in negotiated bidding utilities are marketing directly to investors and said this fact may actually provide the best justification for amending the rule to reflect today's market standard, since the market has clearly moved past competitive bidding.

ALJ Wilson proposed adopting a financing rule in place of the current Competitive Bidding Rule and welcomed participant comments as to what sort of new rule the Commission should adopt for financing.

2. Section 2: Competitive Bidding Rule applies to utilities with an investment grade bond rating or higher

Bob Boada of *SCE* opened by saying that any rule adopted should be based on market standards so that all utilities should be able to easily comply. The rule should state goals and leave the method to evolve along with market standards.

Kathleen Brennan de Jesus of *SCE* further recommended that the Commission adopt a principle-based rule that would be best suited to adapting to changes in the financial market environment. She went on to add that principles adopted could include promoting competition, access to capital markets at the best possible rate, enhancing the inclusion of DBEs, and market feasibility. Ms. Brennan de Jesus went on to draw an analogy to the move in the United States from the rule-based Generally Accepted Accounting Principles (GAAP) to the principle-based International Financial Reporting Standards (IFRS). She added that the SEC's laws also are very general and short, and because of this they have passed the test of time. Utilities should retain the flexibility to use a variety of mechanisms to reach the goals articulated in the rules, subject to Commission review.

Martin Mattes of *CWA* added that smaller utilities do not want to be included in these requirements; however any principle-based rules adopted could be okay. He pointed out that the current details of the Rule are burdensome to smaller utilities.

3. Section 3: Utilities with $25 million or more of California annual operating revenues must make every effort to encourage, assist, recruit, and pre-qualify WMDVBEs as lead underwriter or co-manager of debt offerings

ALJ Wilson opened discussions by stating that the comments provided by parties so far indicate that there is a consensus the Rule is not necessary and the utilities are of the opinion that G.O. 156 should be pursued on a voluntary basis, since their efforts in this area have been effective to date.

Kim Hassan of *SEU* pointed out that SEU supports the tenets of G.O. 156. However, financial transactions are different in kind from other utility purchasing. G.O. 156 requirements are not necessarily efficient or necessary in the financing area. Mandates and prescriptions are not necessarily feasible as they may cause hardship and may contribute to higher costs. Furthermore, a utility may not execute a financing transaction in a given year, which may not work with G.O. 156 annual goals.

ALJ Wilson asked how the proposed Rule would differ from what utilities are already doing, if utilities are already using DBEs.

Kim Hassan of *SEU* stated that terms such as "make every effort to encourage, assist, recruit, and pre-qualify" make the proposed Rule problematic in the sense that the language could be interpreted subjectively. It also raises questions as to whether or how penalties would apply. She further pointed out that feasibility of the rule would depend on the clarity with which it would be interpreted and applied, and whether it would create delays in financing authorizations. She concluded by mentioning that banks would likely be concerned that the regulatory process could hold up potential transactions.

Bob Boada of *SCE* concurred that requirements such as pre-qualifying firms could be problematic. He added that SCE, PG&E, SEU, and SWG believe the proposed reporting requirements contained in this Rule are workable. However, it is preferable to

keep these requirements in the G.O. 156 context along with other DBE issues, and not include DBE reporting as part of a utility's financing application.

Stephanie Chen of *Greenlining* recommended that utilities update their DBE reporting in financing applications. She went on to inquire whether the Commission envisioned that including this information would affect the treatment and outcomes of financing applications.

Nick Bijur of *PG&E* added that pre-qualification done in advance would not provide any value, and reporting on DBE use would be more appropriate as part of the utilities' G.O. 156 annual reporting. Given that financing activity provides the capital that is the lifeblood of utilities, any rule adopted should ensure timely approval of financing applications. This process is critical to utility operations.

Doreen Ludemann of PG&E added that the three-year horizon for financing applications is appropriate, given the time required to process applications at the Commission and utility capital expenditure planning. As such, it would not be appropriate to shorten the forecast period.

Johnny Pong of *SEU* questioned how revisions to the Rule would advance the goals of the Commission given the fact that utilities would continue to seek exemptions from the Rule and that all parties seemed to agree negotiated bidding was the market standard.

ALJ Wilson asked the parties to think of how feasible it would be for the G.O. 156 issue on DBE inclusion and reporting to be adopted as separate rule, if not as part of utilities financing applications. PG&E, SEU, and SCE were open to that idea. Greenlining agreed with reporting in the context of G.O. 156 but wanted to focus on how the issue would be reviewed in connection with a utility's financing application.

Martin Mattes of CWA added that if there is a separate rule in lieu of the Rule, water utilities would still need an exemption.

Commissioner Simon pointed out that his goal is to ensure that utilities institutionalize their DBE efforts in the finance arena and continue to engage and include DBEs in their debt issuances. This will result in these efforts continuing, irrespective of changes in company management or at the Commission. He added that utilities have in the past demonstrated that efforts to include DBEs in their debt financing have been favorable to ratepayers, as demonstrated by the low coupons achieved in recent financings. Ultimately, it would be the goal of the Commission to ensure that transactions are liquid, transparent, and seamless, and that any rule adopted would balance reporting and ensure diversity.

4. Section 4: Notification requirement to solicit bids is shortened to one hour

The participants generally acknowledged that this section is not necessary unless the Rule is retained.

5. Section 5: Electronic communication is allowable for competitive bidding

Participants discussed communication and transparency, and the means by which transaction information is available to the market.

Nick Bijur of *PG&E* inquired whether the focus was on investor or banker access to this information.

Michael Turner of *Castle Oak* Securities stated that once deals are formally launched, they are posted on Bloomberg's Squawk Box for use by bank sales forces, and thus this information is readily available to all users. In determining rules around

communication, he raised the importance of preserving the confidentiality of potential transactions.

Commissioner Simon pointed out that the issue is how the Commission can ensure that utilities are doing their best to open the market to bankers.

Bob Boada of *SCE* responded that this would occur when utilities file their financing applications, which allows the market notice of their intention to seek financing. Bankers respond by setting up meetings with the Utilities to make pitches regarding their capabilities to participate in those financings.

Nick Bijur of *PG&E* clarified that it is not workable for utilities to issue a request for proposal and inform the entire financial market of the specific transactions being considered. Any communication on this scale would create an environment that would allow for adverse arbitrage. As such, in order to keep vital information confidential, utilities only notify the lead banks in advance of the deal, and they wait a day or two before a potential transaction before notifying the other banks. In some instances, this notification is done the day of transaction. With respect to public disclosure of information, he noted that utilities often discuss potential ranges of future debt offerings in our earnings calls, investor presentations, and SEC reports, so there is already public disclosure of information.

David Finkelstein of *Williams Securities* noted that this type of noticing procedure is standard among all their clients in all industries. The current communication protocols do not provide special treatment or mistreatment to DBEs.

Commissioner Simon went on to note that through a utility's Section 816 filings, the bankers who follow the market and are earnest participants in the California market would be adequately noticed. He, however, went on to pose a question on who selects

the banks at all levels for a given transaction. In response, *Mr. Boada of SCE* explained that the utilities make this decision independently; it is not made by the lead banks.

*ALJ Wilson a*sked parties whether they experienced any problems in getting access to the utilities for participating in financings.

Clifford Swint of *MFR Securities* in response stated that any bank that wants to participate in a California utility's financing is aware of each utility's issuance calendar.

Sidney Dillard of *Loop Securities* added that bankers committed to the California market will keep track of utility offerings, and that there have not been problems gaining access to the utilities. She noted that the utilities have an open-door practice.

Clifford Swint of *MFR Securities* agreed with the characterization of the utilities having open doors, noted that limited advance notification to bankers is standard in the market and creates no difficulties or barriers.

Commissioner Simon stated that the Commission is looking for comments on a general financing rule that is framed around a negotiated process while ensuring competition. There is adequate support for removing the Rule, but there is also a need to strike a balance between transparency and avoiding market manipulation. He seeks a level of transparency to show that involving bankers in developing deals is the best option, and that this process is not the equivalent of a private deal. Commissioner Simon also expressed his desire that that selection of banks should be less "clubby." He prefers a best-practices approach, and looks to the participants to make the case for a revised rule.

Stephanie Chen of *Greenlining* added that the onus is on the Commission to institutionalize an emphasis on DBE participation.

Ray O'Connor of *Ramirez* stated that the barrier to entry in calling yourself a "banking firm" is not that high. There should be recognition that not all participants who designate themselves as banking firms can provide the same level of service to utilities and therefore requiring utilities to provide access to all firms would be unfair.

Charles Sorkin of SCM indicated that the answer is that while there may be indications of inefficient pricing of credit products by banks, there is limited, if any harm to ratepayers under the current framework of utility financing activities. Moreover, if the Commission were to implement a quantitative methodology to underwriter selection in debt financing transactions, there could in fact be potential to raise overall funding costs for utility debt issuers, and effectively, ratepayers.

The reasoning for this assertion is that a single transaction approach to examining utility debt financing does not take into account that pricing of traditional bank credit products, such as credit lines, letters of credit, deposit, and custody services tend to be priced based on an expected level of business that a securities issuer may execute in the capital markets, and that if lenders do not expect that they will be able to earn investment banking fees in such transactions, they are prone to re-price their credit products at more expensive levels.

He stated that, in his opinion, the Commission should not apply additional reporting requirements or disclosures with respect to underwriter selection because it could interfere with the ability of utility treasury officers to negotiate the most optimal terms with their lenders. Further, he stated that there may be insufficient data available to determine the degree to which financing costs could rise as a result of pressuring lenders to "unbundle" banking services from securities underwriting activity.

Commissioner Simon followed up on the tying issue raised by Mr. Sorkin by stating that he was aware of the issue and reiterating that issuers could be inclined to use large money-center banks to the exclusion of smaller participants/emerging firms. The goal of the Commission in this case would be to create incentives that would ensure the inclusion of DBEs/emerging firms in utility financing transactions.

6. Section 6: Debt Enhancement Features

Kim Hassan of SEU noted that Section 6.a is problematic because certain debt enhancement features may reduce risk but not necessarily lower the cost of financing. With respect to the cost/benefit analysis, it is not useful or feasible because utilities cannot determine cost effectiveness until the time of the transaction. Although not always used, debt enhancements provide utilities with financing flexibility, are consistent with market practices, and are prudent business and financial mechanisms for hedging risk or reducing cost. She inquired as to whether the proposed rule arose from concerns about the financial crisis in 2008, because it is important to note that utilities enter into these debt enhancements in connection with a financing and not as a separate speculative investment; they are not trying to make a profit but rather, trying to limit risk or lower cost in the transaction.

Nick Bijur of PG&E explained that there are two types of debt enhancements: first, those that are used to hedge risk (swaps, rate locks, puts, calls, etc.); and second, features such as letters of credit, accounts receivable, tax-exempt financing and bond insurance, which are structures used to lower financing costs. The Commission has an opportunity in the cost of capital review to confirm that these instruments were used prudently.

Doreen Ludemann of PG&E said that the financing application indicates that the utility will use the enhancements in connection with a financing transaction and not as a separate speculative investment. Utilities need the flexibility to select among these options at the time of the transaction to achieve the most cost-effective mix.

Gary Hayes, speaking on behalf of SEU, stated that detailed information on debt components is included in the cost of capital proceeding in the embedded cost of debt testimony. This includes detailed calculations as well as written testimony from the embedded cost witness.

PG&E, SCE, SEU, and SWG generally agreed with Section 6.b of the draft revised rule in that debt enhancement features should not be considered separate debt for purposes of calculating financing authorization. They also agreed that they were comfortable with Section 6.c of the draft revised rule, and noted again that review of transactions can be undertaken in the cost of capital proceeding.

7. Exemptions to the Rule

Martin Mattes of *CWA* explained that small offerings do not attract investor interest, and mentioned that the current exemption threshold is outdated. CWA proposed that the Commission as part of the new rule change the threshold level from $20 million to $200 million for the small issuance exemption.

Ted Wood of *SWG* questioned whether the exemption would be needed if the Commission was moving to a general financing rule which would provide flexibility to accommodate other methods of issuance such as private placements and best efforts/sales agent underwriting.

Sarah DeYoung of CALTEL discussed whether a separate exemption for Competitive Local Exchange Carriers (CLECs) was necessary given section 1d of the

rule. She advocated for an exemption because the CLECs were made respondents to the Rulemaking.

Mark Schreiber of SureWest and small ILECs stated his support for adding an express exemption for loans from the Rural Utilities Service if the Rule is retained or if a new rule is adopted in its place.

B. G.O. 24-B

Ted Wood of *SWG* stated that the filing requirement under G.O. 24-B should be increased to 60 days following the end of the quarter. This change will afford utilities the opportunity to coincide their reporting on G.O. 24-B with SEC and other reporting requirements, making it a more efficient and less time-consuming process.

Martin Mattes of *CWA* on the other hand requested that the Commission change the rule for smaller entities to provide for annual reporting. He made this suggestion based on the fact that smaller entities have a low volume of financings.

Doreen Ludemann of *PG&E* stated that PG&E's primary concern is that Subsection C requires utilities to maintain a separate bank account. From PG&E's perspective, this requirement does not reflect current banking and liquidity practices and would lead to increased costs for ratepayers. PG&E's current internal controls and accounting systems can track the source and use of funds and can demonstrate that disbursements were consistent with Public Utilities Code Section 817 purposes.

ALJ Wilson in response asked whether the utilities were currently in compliance with G.O. 24-B.

Doreen Ludemann of *PG&E* acknowledged that while PG&E's current practice has evolved away from the four corners of the rule, PG&E is confident that they can demonstrate through banking and accounting records that funds are deposited and

disbursed consistent with Section 817, the purpose for which section C of G.O. 24-B was developed.

Nick Bijur of *PG&E* added that cash is fungible, explaining that utilities don't put a billion dollars into a bank account and let it sit. Typically, proceeds are used to repay commercial paper and new commercial paper is issued at the time funds are needed for purposes such as capital expenditures. This has proven to be far more cost-effective than maintaining the funds in a segregated account.

Ted Wood of *SWG* stated that utilities could demonstrate compliance with Section 817 by submitting a sources and uses statement as part of the G.O. 24-B report.

ALJ Wilson also inquired on whether the Commission could compare actual sources and uses to the projections made in the financing applications.

Commissioner Simon stated that it is the goal of the Commission to focus on how to make the rule going-forward reflect current conditions and best practices.

Nick Bijur of *PG&E* supported the Commissioner statement and added that Sections A and B of G.O. 24-B do not provide information useful to the Commission under current market practice because, for example, an entire securities issuance might be reflected in a single certificate held by the Depository Trust Corporation (DTC). In response, the Commissioner and the ALJ acknowledged that it might be helpful to incorporate by reference in the G.O. 24-B report further information about the financing that would be contained in the prospectus.

C. Proceeding Schedule and Workshop Report

ALJ Wilson then concluded the workshop by establishing a case schedule, later confirmed by e-mail to the parties, as follows:

January 20, 2012	Joint Utilities Submit Draft Workshop Report

February 3, 2012	Opening Comments on Draft Workshop Report
February 13, 2012	Reply Comments on Draft Workshop Report

The Opening and Reply Comments on the Draft Workshop Report will replace the Opening and Reply Briefs to be filed on February 3 and 13, respectively, which were discussed in the Revised Scoping Memo issued November 15, 2011.

Respectfully submitted on behalf of utilities below pursuant to Rule 1.8(d),

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January 20, 2012

APPENDIX A

REVISED DRAFT COMPETITIVE BIDDING RULE

AND

REVISED DRAFT GENERAL ORDER 24-B

#569565

UTILITY LONG-TERM DEBT FINANCING RULE
Public Utilities Commission of the
State of California

Preamble to Proposed Revisions to the Competitive Bidding Rule and G.O. 24-B

In Decision (D.) 38614, dated January 15, 1946, the California Public Utilities Commission (Commission) adopted the Competitive Bidding Rule, which required California public utilities to issue security debt using competitive bids. The Commission's goal in adopting the Competitive Bidding Rule was to reduce the cost of debt for utilities, and ultimately reduce costs to utility ratepayers.[1] From time to time, the Commission has reviewed its policy regarding the Competitive Bidding Rule based on prevailing circumstances and has subsequently amended the Competitive Bidding Rule in D.49941 (1954), D.75556 (1969), D.81908 (1973), Resolution No. F-591 (1981), and Resolution No. F-616 (1986). On March 10, 2011, the Commission initiated a rulemaking to reexamine its policy regarding competitive bidding to determine the effectiveness and adequacy of the Rule for issuance of debt and equity securities and to consider the associated impacts of General Order (G.O.) 156, debt enhancement features, and G.O. 24-B. [2]

[1] In support of the Rule, the Commission cited In Re Competitive Bidding in the Sale of Securities, 257 I.C.C. 129, an Interstate Commerce Commission (ICC) decision, issued on May 8, 1944, which required railroad companies to competitively bid bonds. However, in 1985, the ICC repealed the competitive bidding requirements promulgated in In Re Competitive Bidding in Sale of Securities, finding that "the need for our oversight of railroad securities has decreased as a result of changed circumstances and recent Congressional action." Exemption of Railroads from Securities Regulation under 49 U.S.C 11301, 1985 ICC LEXIS 492, at *2 (April 1, 1985). The Commission also cited to Rule U-50 of the Securities and Exchange Commission (SEC) Public Utility Holding Company Act of 1935, adopted April 7, 1941, which required registered holding companies and their subsidiaries to use competitive bidding in the issuance or sale of securities. However, the SEC, in 1994, rescinded Rule U-50 based on its opinion "that the rule is no longer necessary in view of the extensive reporting requirements imposed by the Public Utility Holding Company Act and other federal securities laws." Public Utility Holding Company Act Rules, SEC Release No. 35-26031, 1994 SEC LEXIS 1176 at *20 (April 20, 1994).

[2] "Rulemaking to Consider Effectiveness and Adequacy of the Competitive Bidding Rule for Issuance of Debt and Equity Securities and Associated Impacts of General Order 156, Debt Enhancement Features and General Order 24-B. Rulemaking (R.) 11-03-007. The OIR was initiated in response to Commissioner Simon's dissenting opinions to Pacific

Footnote continued on next page

Based on opening comments and reply comments filed in the proceeding, as well as statements made at the pre-hearing conference, filed pre-workshop statements, and discussions at the January 9, 2012 workshop, there is a consensus amongst parties that competitive bidding is no longer the market standard and that the Competitive Bidding Rule is outdated and should be replaced with a new rule that reflects current financial market best practices and conditions. In addition, parties present at the workshop agreed that any new rule should promote utility efforts to include the participation of Women Minority Disabled Veteran Owned Business Enterprises (WMDVBE) in financing transactions. Finally, there was general agreement among parties present at the workshop that G.O. 24-B reporting requirements should also be revised to reflect current financial reporting and cash management standards and practices.

Accordingly, and consistent with the consensus of parties to the proceeding, below are proposed revisions to the draft revised rule and draft revised G.O. 24-B that were circulated by Administrative Law Judge (ALJ) Seaneen Wilson on December 15, 2011.[3] The proposed revisions to the draft revised rule replace the outdated competitive bidding process with a more general, principles-based goal to require utilities to conduct financings in a competitive and transparent manner that achieves the lowest cost of capital, while also encouraging the use of WMDVBEs. This

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Gas and Electric Company's D.08-10-013 and Southern California Edison Company's D.08-10-014, and D.08-10-015 which authorized the utilities to issue a total of $8 billion in debt and preferred stock. The dissenting opinions questioned the effectiveness and adequacy of the Rule in part because of financing approvals based on long-term (three-year) projections of capital expenditure requirements, exemptions from the Rule without any conclusive showings by the utilities that those exemptions were in the ratepayers best interest, and lack of any showing that the utilities financial services procurements are included in their G.O. 156 program goals. The OIR was also initiated in response to Commission concern in D.09-09-046 about the level of transparency with regard to the volume of debt enhancement features being used by the utilities and notice to the utilities that their debt issuance practices may be evaluated in a future review of the Rule.

[3] *See* Administrative Law Judge's Ruling Adding Items for Discussion at the January 9 and 10, 2012 Workshop, and Adding an Evidentiary Hearing on January 10, 2012.

approach will: 1) reflect current market practices and standards, 2) provide utility flexibility to take advantage of market opportunities and adjust pricing, in order to obtain low-cost debt financing, 3) allow utilities to take better advantage of market competition, and 4) facilitate utility efforts to provide WMDVBEs with meaningful opportunities to participate in utility financing transactions. The proposed revisions reflect technological advances in information flow and revise archaic terms in the draft revised rule. The proposed revisions to the G.O. 24-B reporting requirements: 1) extend the time by which utilities must file G.O. 24-B statements with the Commission to coincide with the utilities' SEC disclosure filings, 2) modify language to reflect current market terms, practices and standards, and 3) modify language to reflect current utility record maintenance practices.

Utility Long-Term Debt Financing Rule

~~**Draft Revised Competitive Bidding Rule**~~

1. Public utility long-term debt issues shall be conducted in a prudent manner consistent with market standards that encompass competition and transparency, with the goal of achieving the lowest long-term cost of capital for ratepayers.

~~1. All debt issues must be competitively bid unless:~~

~~a. Competitive Bidding is inapplicable pursuant to these rules;~~

~~b. Competitive Bidding is not cost effective;~~

~~i. In it's financing application, a utility must provide support showing that competitive bidding is not currently cost effective, including but not limited to:~~

~~1. At least three years of the utility's actual coupon rates of debt issued (identify method of issuance), compared to:~~

~~a. The actual market rate of similarly rated public utilities operating in the United States; and~~

~~b. The coupon rates of similarly rated public utility debt issuances (identify method of issuance).~~

~~c. A utility debt issuance is exempted pursuant to the exemptions below; or~~

~~d. Competitive Bidding is inapplicable pursuant to another California Public Utilities Commission order, decision, or rule.~~

2. Public utilities shall determine the financing terms of their debt issues with due regard for their financial condition and requirements and current and anticipated market conditions.

~~2. The Competitive Bidding Rule is only applicable to utilities with an investment grade bond rating or higher.~~

3. Utilities with $25 million or more of California operations annual operating revenues, requesting financing authority, ~~must~~ shall ~~make~~use their ~~every~~best efforts to encourage, assist, and recruit~~, and pre-qualify~~ Women Minority Disabled Veteran Owned Business Enterprises (WMDVBE)[4] in being appointed as lead underwriter, ~~or~~ co-manager, or in other roles in ~~of~~ debt securities ~~issuance~~ offerings.

[4] Pursuant to G. O. 156 and D.11-05-019, definitions of Women, Minority, and Disabled Veterans Owned Business Enterprises are as follows:
1.3.2. "Women-owned business" means (1) a business enterprise (a) that is at least 51% owned by a woman or women or (b) if a publicly owned business, at least 51% of the stock of which is owned by one or more women; and (2) whose management and daily business operations are controlled by one or more of those individuals.
1.3.3. "Minority-owned business" means (1) a business enterprise (a) that is at least 51% owned by a minority individual or group(s) or (b) if a publicly owned business, at least 51 % of the stock of which is owned by one or more minority groups, and (2) whose management and daily business operations are controlled by one or more of those individuals. The

Footnote continued on next page

a. Utilities ~~must~~ shall report on their efforts in their G.O. 156 Annual Reports~~each time they file an application for financing authority~~, including but not limited to:

i. Number of WMDVBE firms that have been appointed as lead underwriter, ~~or~~ co-manager, or other roles ~~of~~in debt securities ~~issuance~~ offerings ~~since the utility's last financing application~~within the reporting period.

1. The position(s) held by the WMDVBE firms.

2. The percentage of each debt issue allocated to each WMDVBE firms.

~~2.~~3. The dollar amount of these debt securities issuances.

b. Appointment of WMDVBE as lead underwriter, ~~or~~ co-manager, or other role ~~must~~shall be cost effective, so as not to increase financing costs to the ratepayers.

~~b.~~c. Consistent with Section 6 of G.O. 156, utilities shall retain the authority to use their legitimate business judgment in selecting firms for a particular debt securities offering.

~~4. The notification requirement to solicit bids is shortened to one hour.~~

~~5. Any form of electronic communication available to the general public is allowable for competitive bidding.~~

~~6.~~4. Debt Enhancement Features ~~must be shown to be cost effective~~shall only be used in connection with debt securities ~~offerings~~financings, ~~. Such features~~and may include but are not limited to: put options, call options, sinking funds, swaptions, caps, collars, currency swaps, credit enhancements, capital replacement, interest deferral, special-purpose entity transactions, delayed drawdown, ~~hedging strategies,~~ treasury lock, treasury options, and interest rate swaps~~, and long hedges~~.

a. For each Debt Enhancement Feature requested in a financing application, the utility shall provide a brief description and rationale for the potential use of a debt

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contracting utility shall presume that minority includes, but is not limited to, Black Americans, Hispanic Americans, Native Americans, Asian Pacific Americans, and other groups, as defined herein.

1.3.4. "WMBE" means a women-owned or minority-owned business enterprise; under these rules, the women and/or minorities owning such an enterprise must be either U.S. citizens or legal aliens with permanent residence status in the United States.

1.3.5. Black Americans-persons having origins in any black racial groups of Africa.

1.3.6. Hispanic Americans-all persons of Mexican, Puerto Rican, Cuban, South or Central American, Caribbean, and other Spanish culture or origin.

1.3.7. Native Americans-persons having origin in any of the original peoples of North America or the Hawaiian Is-lands, in particular, American Indians, Eskimos, Aleuts, and Native Hawaiians.

1.3.8. Asian Pacific Americans-persons having origins in Asia or the Indian subcontinent, including, but not limited to, persons from Japan, China, the Philippines, Vietnam, Korea, Samoa, Guam, the U.S. Trust Territories of the Pacific, Northern Marianas, Laos, Cambodia, Taiwan, India, Pakistan, and Bangladesh.

1.3.9. Other groups, or individuals, found to be disadvantaged by the Small Business Administration pursuant to Section 8(a) of Small Business Act as amended (15 U.S.C. 637 (a)), or the Secretary of Commerce pursuant to Section 5 of Executive Order 11625.

1.3.10. Disabled Veteran-a veteran of the military, naval or air service of the United States with a service-connected disability who is a resident of the State of California.

enhancement or the risk management properties associated with the potential use of a derivative instrument to hedge risk exposures.

~~a. All Debt Enhancement Features must lower the cost of financing and benefit the ratepayers.~~

b. Debt Enhancement Features are not considered as separate debt for purposes of calculating a financing authorization.

c. Swap and hedging transactions are restricted as follows:

i. Utilit~~y~~ies ~~must~~ shall separately report ~~all~~any interest income and expense arising from all swaps and hedging transactions in ~~its~~their quarterly G.O. 24-B reports to the Commission ~~regular annual report to the Commission~~.

ii. Swap and hedging transactions ~~will~~shall not exceed 20% at any time~~,~~ of a utility's total long-term debt outstanding.

iii. All costs associated with hedging transactions are subject to review in a utility's next regulatory proceeding addressing its cost of capital ~~proceeding~~.

iv. Hedging transactions carrying potential counterparty risk must have counterparties with investment grade credit ratings.

v. If a utility elects to terminate a swap or hedging transaction before the original maturity or the swap or hedging partner terminates the agreement, all costs associated with the termination are subject to review in a utility's next regulatory proceeding addressing its cost of capital ~~proceeding~~.

vi. ~~The utility~~Utilities ~~wi~~shall provide the following to Commission ~~s~~Staff within 30 days of receiving any written ~~a~~ request: (i) all terms, conditions, and other details of swap and hedge transactions; (ii) rationale(s) for the swap and hedge transactions; (iii) estimated costs for the "alternative" or un-hedged transactions; and (iv) copy of the swap and hedge agreements and associated documentation.

~~**Exemptions:**~~

~~1. Requests for exemption from the competitive bidding rule will only be granted upon a compelling showing by a utility.~~

~~2. Debt issues for which competitive bidding are not viable or available, or due to the size of the issue, are exempt.~~

~~3. Bond issues of $20 million or less are exempt from the competitive bidding rule.~~

~~4. Tax exempt or government debt issues are exempt from the competitive bidding rule.~~

~~5. Debt issues, such as the Safe Drinking Water Bond Act loans, Rural Utility Service loans, and pollution control loans, are exempt from the competitive bidding rule.~~

~~6. Debt issues made through an affiliate that provides debt issuance services to all affiliates of the same parent are exempt from the competitive bidding rule if such debt accounts for less than five percent (5%) of the financing affiliates annual issuances.~~

~~7. Debt issues for those utilities with no debt rating are exempt from the competitive bidding rule.~~

~~8. For multi-state utilities operating in California, if your operating revenues from California operations represent less than five percent (5%) of the entire utility's total operating revenues for the most current calendar year, the utility is exempt from the competitive bidding rule.~~

Draft Revised

GENERAL ORDER No. 24-~~C~~B
Public Utilities Commission of the
State of California

IN THE MATTER OF THE PREPARATION OF QUARTERLY REPORTS SHOWING RECEIPTS AND DISBURSEMENTS FROM THE. SALE OF STOCKS, BONDS AND OTHER EVIDENCES OF INDEBTEDNESS OF PUBLIC UTILITIES, WHICH HAVE BEEN AUTHORIZED TO BE ISSUED BY THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA, UNDER SECTION 824 OF THE PUBLIC UTILITIES CODE.

On or before the ~~25th~~ 60th day following each quarter, the information required by Sections A and B ~~of the month following each quarter, the following statements~~ for the preceding quarter, certified by an ~~responsible officer~~authorized representative of the corporation issuing stocks, bonds or other evidences of indebtedness, or by the partnership or individual authorized to issue bonds or other evidences of indebtedness shall be filed with the Commission.

The Commission ~~s~~Staff may request such information on a monthly basis.

A. RECEIPTS

1. A ~~list~~description of the ~~certificates of~~ stock issued during the quarter under the authority of the Commission, ~~which shall show~~including:
   a. The ~~numbers of the certificates issued~~principal amount of the issuance;
   b. ~~To whom it was issued~~The number of shares issued;
   ~~c. Number of shares represented by each certificate;~~
   ~~d~~c. The par value, if any, of each ~~certificate~~share;
   ~~e~~d. The ~~brokerage or commissions if any, paid for sale of stock represented by each certificate~~commissions paid; and
   ~~f~~e. The ~~consideration received for each certificate in money, or the cash value of labor or property, if any~~total proceeds received.~~.~~
2. The total amount of stock issued under the order of the Commission and outstanding at the end of the quarter, which shall show:
   a. The total number of ~~certificates~~shares ~~so~~ issued; and
   ~~b. The total number of shares represented by such certificates;~~
   ~~e~~b. The total par value, if any, of such shares~~;~~.
   ~~d. The total brokerage or commissions paid for sale of such shares to date;~~
   ~~e. The total consideration received for such certificates in money, and the total cash value of labor or property, if any.~~
3. A ~~list~~ description of the bon~~u~~ds or other evidences of indebtedness, issued during the quarter, under the authority of the Commission, ~~which shall show~~including:
   a. The principal ~~numbers~~amount of ~~such bonds or other evidences of indebtedness issued~~ the issuance;
   b. ~~To whom it was issued~~The commissions paid; and

c. The ~~face value of such bonds or other evidences of indebtedness~~total proceeds received~~;~~.

~~d. The brokerage or commissions paid on each sale;~~

~~e. The consideration realized in money on each sale, or the cash value of labor or property, if any.~~

4. The total bonds or other evidences of indebtedness issued under the order of the Commission and outstanding at the end of the quarter, which shall show the principal amount of such bonds or other evidences of indebtedness issued.~~:~~

~~a. The total number of such bonds or other evidences of indebtedness issued;~~

~~b. The total face value thereof;~~

~~c. The total brokerage or commissions paid thereon to date;~~

~~d. The total consideration which has been received in money from the sale thereof, and the total cash value of labor or property, if any.~~

B. DISBURSEMENTS

Each utility authorized to issue stock, bonds or other evidences of indebtedness shall file quarterly reports showing the purposes for which it expended the proceeds realized from the sale of said stock, bonds or other evidences of indebtedness. The expenditures shall be set forth in such manner as will enable the Commission to ascertain their compliance with Section 817 of the Public Utilities Code and with the related authorizing decision.

C. ~~PLACED IN SPECIAL BANK ACCOUNT~~MAINTENANCE OF RECORDS

Utilities shall maintain records and accounts consistent with current accounting and internal control standards in a manner that demonstrates the appropriate use of funds in compliance with Section 817 of the Public Utilities Code and any related financing authorization. Utilities shall make these records available to Commission Staff upon written request.~~A separate bank account shall be opened with a state or national bank, to which shall be charged or credited all receipts and disbursements of money derived from the sale of stocks, bonds or other evidences of indebtedness authorized to be issued by this Commission. A statement of this account shall be furnished the Commission each quarter showing the balance in cash on hand to the credit of the fund at the end of the preceeding quarter.~~

D. INCORPORATION BY REFERENCE

Any of the information required by Sections A, B, or C above may be incorporated by reference to offering documents provided to investors in connection with the relevant securities issuance.

APPENDIX B

Competitive Bidding Workshop, R.11-03-007

January 9, 2012

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