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PCG - Q4 2012 PG&E Corporation Earnings Conference Call

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OVERVIEW:

Management discussed 4Q12 and 2012 results, reporting EPS of $0.59 and $3.22 for the respective periods. Guidance was for 2013 EPS from operations of $2.55-2.75.

CORPORATE PARTICIPANTS

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PRESENTATION

Operator

Good morning and welcome to the PG&E Corporation fourth-quarter earnings conference call. All lines will be muted during the presentation portion of the call, with an opportunity for questions and answers at the end.

At this time I would like to introduce your host, Gabe Togneri with PG&E. Thank you and enjoy your conference. You may proceed, Mr. Togneri.

Gabe Togneri - PG&E Corporation - VP IR

Thank you, Jackie, and good morning, everyone. Thanks for joining us today.

Before you hear from Tony Earley, Chris Johns, and Kent Harvey, let me give you the usual reminders, and that being the discussion will include forward-looking statements that are based on assumptions and expectations reflecting information currently available to management. Some of the important factors that could affect the Company's results are described in Exhibit 1, located in the Appendix for today's slides. We also encourage you to review the discussion of risk factors that appears in the 2012 annual report and in the Form 10-K, both of which will be filed with the SEC later today.

With that, I'll hand it over to Tony.

Tony Earley - PG&E Corporation - Chairman, CEO, President

Good morning, and thanks for joining us today. We have a lot to cover this morning, starting with our results over the past year, and then we will discuss our outlook for 2013 and beyond. I'll begin, and then turn it over to Chris and Kent.

Our focus continues to be on the areas outlined at the beginning of last year -- resolving gas issues; positioning the Company for long-term success; and rebuilding relationships and partnering effectively with stakeholders. We've made significant progress in all of these areas in the last year.

As you know, we have been working diligently to resolve the outstanding gas issues. Unfortunately, we reached an impasse in settlement discussions with the other parties in the investigations, and we are now moving forward with the scheduled regulatory proceedings. We're committed to bringing this to a conclusion that is fair to all the parties involved, including our shareholders.

You know, since the San Bruno accident we've spent $1.4 billion in shareholder dollars on unrecovered pipeline-related expenses and capital investment. And the total cost is $1.9 billion when we add the charge we've taken related to potential penalties, the contribution we made to the City of San Bruno, and the incremental work we've done to improve our performance across the utility.

While the investigations remain undecided, we are well on the path to resolving many of the other issues. The decision on the Pipeline Safety Enhancement Plan was an important step forward in closing out some of the cost uncertainties. While the result was not what we originally had in mind, it was an improvement over the proposed decision.

We've also continued to make substantial progress on third-party liabilities. We've settled all of the most serious cases, and we're now focused on resolving the remaining cases.

As a result of the settlements, the judge in the case recently took the trial off the court's calendar and encouraged the parties to continue settlement discussions on the remaining cases. And we continue to receive insurance payments.

As we've reported to you each quarter, we've also made substantial progress on gas operational issues. One area where our assessment is not complete is the encroachment issue on our gas pipeline rights-of-way; but we are including a range of costs in our guidance today, and Kent will get to that later.

We continue to be focused on that issue, as well as resolving the CPUC and criminal investigations.

We are starting to transition from the uncertainties of the past couple of years, and we have taken steps to position the Company for long-term success. As I've mentioned before, we've adopted a more rigorous multi-year planning process, which has put us on a positive trajectory towards operational and financial success.

As part of our planning process, we established key operating metric targets at the beginning of last year, and we closed the year with strong performance against those metrics. Our continuous improvement program is up and running.

And we filed our 2014 General Rate Case application, which is intended to re-baseline the Company's distribution and generation operations. Our objective is to execute well on the programs outlined in the GRC, enabling us to earn our authorized return in 2014, with the exception of the gas transmission business.

As I've said since arriving at PG&E, we can't rebuild our Company without also rebuilding relationships and being a trusted partner. The first step has been meeting our operational commitments.

In 2012, for the second year in a row, we executed an unprecedented level of gas work, and we've gotten much better at communicating with our stakeholders about the work that we're doing. We've been collaborating with public officials in Sacramento on important policy issues such as residential electric rates and greenhouse gas emissions. We're also improving our relationships with the cities and towns across our service territory.

Last year, we piloted an initiative to strengthen our local PG&E presence. And we're so pleased with the results that we're expanding those pilots across our system. In addition, the customer outreach and education effort that we launched in 2012 is delivering results. We're seeing strong momentum in our Customer Satisfaction Survey scores, and our brand favorability numbers have moved up sharply.

But we recognize that relationships with our customers are still fragile. To continue to earn back their trust, we simply have to keep our focus on improving the safety and reliability of our system and our service. We believe that delivering strong operational results for our customers will lead to strong financial results over time.

So now I'm going to turn things over to Chris, who will cover regulatory and operational items in a little more detail. Chris?

Chris Johns - Pacific Gas and Electric Company - President

Thanks Tony. First, I'll start with our regulatory activity. In December of 2012, we saw resolution of several significant cases at the CPUC.

First, the Commission voted out the cost of capital case, resulting in a 10.4% return on equity for 2013 and a capital structure of 52% equity. In addition, last month the parties filed a settlement that would essentially extend the previous adjustment mechanism through the end of 2015.

The CPUC also approved our application for the Oakley Generating Station, a 586 megawatt high-efficiency gas plant to be built in Contra Costa County. We expect to take ownership of the facility from the developer sometime in 2016 or 2017.

Also in December the CPUC awarded us $21 million in energy efficiency incentive revenues associated with the successful results of our 2010 customer energy efficiency programs.

As you know, the PUC also voted out our Pipeline Safety Enhancement Plan, or PSEP. Although the vote provides certainty on how the Plan will be implemented, the punitive disallowance is disappointing. The PSEP decision and the current Gas Transmission rate case remain in effect through the end of 2014, and we'll incorporate future pipeline spending in the 2015 Gas Transmission rate case.

Looking at significant regulatory items in 2013, as Tony mentioned, we filed our $1.28 billion application for the 2014 General Rate Case in December. The Administrative Law Judge on that case has approved a schedule that, if followed, would allow the case to be resolved by the end of this year. As part of this rate case, we are participating in a new CPUC process where a third party performs an independent safety overview of our filing.

We also filed our Transmission Owner case, or TO14, with the FERC, and re-filed the application at the end of the year under order from FERC staff to use a much lower return on equity. We have filed a request for rehearing, as we believe the resulting ROE is insufficient to attract capital.

Moving on to operations. 2012 was a very busy year across the entire Company as we executed on our plans to enhance the safety and reliability of our system.

In the gas business, in 2012 we completed pressure tests on 175 miles of pipeline. This level of strength testing in a single year on pipes already in service exceeds anything any other utility has done before.

We also replaced 40 miles of pipe and installed 46 remote or automatic shutoff valves across the system. This year we will complete our comprehensive validation of the maximum allowable operating pressure on all of our gas transmission pipelines.

As you know, we have brought in an experienced gas leadership team and tasked them with ensuring that we have a safe and reliable system. As part of their evaluation, they've identified additional work related to integrity management requirements and maintaining pipeline rights-of-way across our system, both of which we've discussed with you in the past.

On the integrity management side, we've made some changes to our risk assessment methodology to better align with leading practices. So for example, we've strengthened our procedures associated with identifying manufacturing and construction defects and internal corrosion on our pipes. We're now incorporating assessment and testing for these and other potential challenges into our integrity management program, where we'll also use the information for asset management and investment planning.

Much of this work was not included in our last Gas Transmission rate case. The costs for the work we do this year and next will not be recovered, but we do plan to include this enhanced integrity management approach in our request for the next Gas Transmission case starting in 2015.

With regard to the encroachment on our rights-of-way and the necessary mitigation we'll have to undertake, we're conducting a detailed survey to ascertain the exact coordinates of the pipeline within the rights-of-way across our entire service area. We expect to complete this survey later this year.

Meanwhile, we've relied on aerial photography and other inputs to develop preliminary cost estimates. Our information thus far confirms that the encroachments are numerous and significant. And because this issue arises from our ineffective patrolling in the past, we will not be able to recover these costs in rates.

We expect the total cost for this right-of-way work to be on the order of $500 million over the next five years. Obviously this is a significant cost, but it's work we're committed to get done and to get done effectively and efficiently.

Shifting gears, we're really pleased with the work being done to provide reliable customer service in electric operations and in energy supply. For example, in electric operations, installing SmartGrid technology such as intelligent switches on more than 100 distribution circuits helped us reach record reliability for PG&E for the fourth year in a row.

While we're not yet at the first-quartile level we aspire to be, our consistent improvements give me confidence that we're making good progress in that direction.

At Diablo Canyon, we had another year of strong performance on safety and operations, and ended the year with a 90% capacity factor overall. Earlier this month, we began a regularly scheduled refueling outage on Unit 2.

Finally, we continue to progress on the renewables area and are on target to meet our commitment of having 33% renewable power by 2020. However, as part of that process we have decided not to continue with our utility-owned solar PV program after this year, as we are getting better pricing for our customers through competitive bidding.

We're seeing the results of our focus on operations and planned incremental spending and capital investments, all of which continue in 2013. This year, the additional capital spending will support things like consolidating our electric and gas distribution control centers and installing more SCADA technology.

We believe it makes sense to continue these efforts going into the next General Rate Case, given our progress in improving our operations across the board. Our customers are responding to these efforts. Last year, our Customer Satisfaction Survey results were the highest they've been since 2009. This reflects our customers' appreciation for our team's commitment to restoring power quickly and safely.

With that, I'll turn things over to Kent.

Kent Harvey - PG&E Corporation - SVP, CFO

Thanks Chris. Good morning. I plan to briefly go through Q4 and 2012 results, and then spend most of my time on guidance going forward.

Slide 4 summarizes the results for the quarter and the full year. Earnings from operations were $0.59 for the quarter and $3.22 for the year. GAAP results are also shown here and reflect the items impacting comparability for natural gas matters and for environmental-related costs. The natural gas item is laid out in pre-tax dollars in the table at the bottom.

Pipeline-related costs came in at $106 million pre-tax for the quarter and $477 million for the year, well within our guidance range of $450 million to $550 million. We had been trending toward the upper end of the range during much of the year, but some of our expected legal costs were pushed into 2013 given delays in the pipeline investigations while settlement discussions were underway.

Importantly, during the quarter we took a pre-tax charge of $353 million for the capital that was disallowed in connection with our Pipeline Safety Enhancement Plan. Going forward, we don't expect additional capital write-offs unless our costs trend higher than our current assumptions.

During Q4, we accrued an additional $17 million for possible penalties related to the gas matters. Our original accrual of $200 million done in Q4 of 2011 included potential fines for missing maps in our gas leak survey program. Since those fines have been paid, we took an additional accrual in Q4 in order to restore the total accrual to $200 million.

We continue to believe that this represents the low end of the range for possible penalties. During the quarter there were no additional accruals for third-party liability claims, but we did book additional insurance recoveries of $50 million, which you see near the bottom. That brings total insurance recoveries to $185 million during 2012 and $284 million since the accident.

In terms of the item impacting comparability for environmental-related costs, which is back in the top part of the slide, we accrued an additional charge of about $0.02 per share in Q4, reflecting updated cost estimates related to property purchases and whole-house water replacement.

Slide 5 shows the quarter-over-quarter comparison for earnings from operations, including the main drivers that take us from $0.89 in Q4 2011 to $0.59 in Q4 2012. Most of these drivers are consistent with items we've seen in past quarters.

Planned incremental work across the utility totaled $0.11 negative. And employee incentive compensation accounted for a $0.09 difference, since the annual incentive in the prior year was well below target.

In addition, increased shares outstanding drove a $0.05 decline; storm costs and litigation costs were each $0.02 negative; and we had various other items that totaled $0.06 negative. A few of these items include somewhat lower awards for our energy efficiency programs when compared to the prior year, and then lower tax settlements. These factors were partially offset by a $0.05 increase in rate base earnings compared to a year ago.

In terms of our equity issuance, we issued a total of $775 million of common stock during the year, bringing our year-end share count to 431 million shares.

That's it for 2012 results, and I'd like to now move on to our outlook going forward. I plan to walk through our guidance for 2013 and then I'll also provide some thoughts about 2014 and beyond.

As we've discussed before, 2013 is going to be a down year for us due to the impact of our lower authorized return, the additional dilution from share issuance year-over-year, and our continued incremental spend across the utility prior to a reset in our 2014 General Rate Case.

Let's start by going through some of the key assumptions in our guidance, which are shown on slide 6. First, we're assuming capital expenditures for the year of a little over $5 billion, somewhat higher than last year's level. You can see the key components of the planned CapEx on the left.

We're also assuming an average authorized rate base of about $26 billion in 2013. This reflects past regulatory decisions, like our 2011 General Rate Case, as well as pending proceedings, such as our current electric transmission case with the FERC.

The authorized return on equity for most of our rate base other than electric transmission is assumed to be the 10.4% that we recently received from the California PUC. However, we are assuming an ROE of only 9.1% on the electric transmission business for guidance purposes, given where we currently are with the FERC on that issue. Our authorized equity ratio continues to be 52% across the board.

We assume that we'll continue to incur about $250 million of expenses across the utility in excess of levels authorized in recent rate cases, in order to enhance the level of service we're providing customers. We've requested recovery of most of these costs starting in 2014 in our next General Rate Case. There is roughly about $50 million of the total that relates to gas transmission, and that's expected to be incorporated in our next Gas Transmission case in 2015.

Because the CapEx program described above will exceed levels authorized in our last General Rate Case and other proceedings by about $1 billion this year, we expect to incur some additional financing and depreciation expense that won't be recovered in 2013. We do anticipate truing up rate base in our upcoming General Rate Case to include recovery of most of these investments beginning in 2014.

As we've previously discussed, we expect our below-the-line costs in 2013 to fully offset CWIP earnings. So that's another assumption underlying our guidance.

And, as has been the case for the past couple years, we continue to experience lower revenues for our gas storage business due to market conditions being less favorable than was assumed in our last Gas Transmission case. Roughly offsetting this last item is the assumption that we earn an incentive award for our customer energy efficiency programs this year that approximates the one we earned late in 2012.

Turning to slide 7, you'll see that these assumptions lead us to provide a guidance range for earnings from operations in 2013 of $2.55 to $2.75 per share. The primary drivers year-over-year are the reduction in authorized ROE for both the PUC and FERC jurisdictional assets; the additional dilution due to share issuance year-over-year; the impact of below-the-line costs, which are expected to fully offset CWIP earnings as compared to partially offset in 2012; and then planned CapEx in excess of authorized levels. These factors are partially offset by the growth in authorized rate base.

Moving on to slide 8, you can see our guidance for the item impacting comparability for gas matters in 2013. We're providing guidance for pipeline-related costs that we expect to incur but not recover during 2013 of $400 to $500 million pre-tax. Let's go through each of those components.

In terms of the Pipeline Safety Enhancement Plan, we wrote off the capital that was disallowed by the CPUC in Q4. So our guidance in 2013 includes the expenses that we expect to incur but not recover through rates. Our pre-tax guidance range for this component is $150 to $200 million.

In terms of the emerging work, we're looking at the costs to survey and begin clearing our pipeline rights-of-way and the higher level of activity we've undertaken on our integrity management program. Our pre-tax guidance for these emerging work categories is $175 to $225 million.

We expect the right-of way work to represent more than half of this spend in 2013, and as Chris indicated, to be carried out over a five-year period. We do not expect to recover these costs through rates. We'll continue to refine our estimates once we've completed the centerline survey late in the year.

We expect the integrity management work to represent less than half of the spend in 2013 and to continue in future years. However, we plan to seek recovery of these ongoing costs beginning in 2015 in the next Gas Transmission case.

Finally, we're showing a range of $50 million to $100 million for legal and other costs, since some costs we planned in 2012 were pushed out with the delayed proceedings at the CPUC. We would expect these costs to decline significantly after this year.

You'll notice also that the guidance range we're using for total pipeline-related costs is somewhat narrower than just the sum of the ranges for each piece. At the bottom of the slide are the other categories we've been tracking related to gas matters.

As we've done in the past, we're not providing guidance for additional penalties coming out of the investigations; and the range we show for third-party liabilities continues to reflect the difference between what we've accrued to date -- $455 million – and then the upper end of the estimate we've disclosed, which is $600 million. We're also not providing guidance for insurance recoveries, but anticipate those to continue to follow from the resolution of the third-party claims.

On slide 9, you can see our estimated equity issuance of $1 to $1.2 billion for 2013. This range is consistent with our guidance assumptions and does not reflect any equity issuance that would result from fines greater than the $200 million we've already accrued.

Key factors driving our equity issuance in 2013 compared to 2012 are lower earnings from operations in 2013, somewhat higher CapEx, and the PSEP capital charge at the end of last year. We'll continue to utilize various ways to raise equity efficiently and effectively, including our Dividend Reinvestment 401(k) programs, and our dribble program.

Slide 10 summarizes 2013 guidance, including earnings from operations and the gas matters item. As you can see, we're also including a modest guidance range for environmental-related costs in connection with the Hinkley clean-up.

The range here reflects some true-ups we may experience on our whole-house water program during the year as well as habitat protection activities we may undertake. You'll remember, we've already accrued the expected costs associated with our proposed final remedy to clean up the groundwater. Our guidance does not include additional costs in the event a more onerous final remedy is ordered.

I know many of you recognize that 2013 is an unusual year for us, and you are interested in getting a read on what things might look like in 2014 and beyond. So while we're not providing earnings guidance beyond 2013 at this point, I do want to share with you our current view of our CapEx and our rate base going forward.

Slide 11 shows a range of estimated CapEx for 2014 through 2016. The upper end of the range provided for each year reflects the CapEx level included in our 2014 General Rate Case and attrition requests. It also represents our current views of future regulatory requests for electric transmission and gas transmission.

The lower end of the ranges reflects current spending levels across the utility, with some adjustment for known changes, such as the end of the Cornerstone program and the utility photovoltaic program.

I should also point out that we've excluded the recently approved Oakley Generating project from the 2016 CapEx numbers shown here, just in the interest of being conservative. Our turnkey purchase of that plant will occur when it's ready to go operational, and that could be as early as 2016.

The level of CapEx I've described would provide for significant growth over the next few years. And as you'd expect, we'd continue to issue a meaningful amount of equity to support this growth.

Slide 12 shows ranges for our authorized rate base consistent with the CapEx numbers. Under these assumptions, average authorized rate base for 2014 ranges from $28.5 billion to $29 billion and would grow to between $32 and $35 billion in 2016. The compound growth rate over this period ranges from 6% to 10%, excluding the Oakley Plant.

These numbers reflect our intent in the 2014 General Rate Case to true up our rate base in order to reflect the higher CapEx we're undertaking this year. In addition, we hope to true up our revenues to recover most of the incremental expenses we've been incurring across the utility to improve service both last year and this year. As a result, our objective is to earn our authorized return for the non-pipeline segments of our business starting in 2014.

Slide 13 just addresses the fact that in future years we still expect to incur some costs for gas pipeline work that will not be recovered. You already know that the PSEP decision did not sufficiently fund our planned expense work, and that affects us through the end of 2014.

After that, we anticipate incorporating our ongoing pipeline safety work into our 2015 Gas Transmission case. By then, there will be even more data to demonstrate the true cost of doing this work.

In terms of the emerging work, Chris mentioned that our current estimate for the right-of-way activities is roughly $500 million over five years, so we expect those unrecovered costs to continue through 2017. We also expect our enhanced integrity management program to continue next year and beyond. Though we won't recover those costs in 2014, we do plan to incorporate them into our 2015 Gas Transmission case.

Finally, we expect our legal costs to decline significantly in 2014. On this slide, we have not included things like third-party liabilities, insurance, and penalties, and our objective is to resolve those as much as possible this year.

Obviously, there may be some things that don't get fully wrapped up. We plan to continue to break out these costs so you can keep track of the impact that they have on our GAAP results.

I'm going to stop here. I know I've covered a lot. Hopefully, the information that we covered today will be helpful to you in assessing our financial prospects going forward. Tony?

Tony Earley - PG&E Corporation - Chairman, CEO, President

Thanks Kent. Let me just reiterate some of the points from this morning's call.

We weren't able to resolve all of the San Bruno-related issues last year, as we had hoped to do. But we have resolved many of them, including the Pipeline Safety Enhancement Plan and much of the third-party liability, and I'm pleased with that.

Operationally, 2012 was a very productive year for us. We accomplished the work we set out to do, and I'm proud of the employees who have been working hard toward our goal of becoming a safer, high-performing Company.

Though challenges remain, our recovery is clearly underway, and our progress will continue in 2013. We have a good team in place, a solid fundamental operating plan, and some successes under our belt. We're committed to becoming a high-performing gas and electric utility that our customers, regulators, and shareholders deserve.

So with that, let me open the floor for your questions.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) Angie Storozynski, Macquarie.

Angie Storozynski - Macquarie Research - Analyst

Thank you very much. I might have missed the statements about how much you have accrued for the potential penalty versus the $1 to $1.2 billion equity guidance. Your slide 9 says that does not include potential penalties above the accrued level. So what is the accrued level?

Kent Harvey - PG&E Corporation - SVP, CFO

The accrued level is $200 million.

Angie Storozynski - Macquarie Research - Analyst

Wow. So you are assuming that that issue is largely a function of basically unrecoverable expenses?

Kent Harvey - PG&E Corporation - SVP, CFO

And our capital expenditure program.

Angie Storozynski - Macquarie Research - Analyst

Okay. Now if you -- I'm basically a little bit stunned that this is how much equity you would need in 2013. I would have assumed that this is partly a function of the penalty, well in excess of the $200 million that you have already accrued for. But that's fine.

Now can you talk a little bit more about the FERC transmission ROE? It seems extremely low.

Kent Harvey - PG&E Corporation - SVP, CFO

Yes, we were served a -- received a FERC staff order in our Transmission Owner case that essentially ordered us to file with a 9.1% return on equity. It's obviously something we don't think is adequate to attract capital.

We think it is a very narrow way to actually consider what our true cost of equity is, and we hope to be able to resolve it through settlement discussions or else through the legal process. But that's going to take us a while to actually resolve. So we have assumed the 9.1% return on equity for the electric transmission component of our business in our 2013 guidance.

Angie Storozynski - Macquarie Research - Analyst

Okay. Then lastly, the pipeline-related expenses, if I look beyond 2014 where you have your legal expenses significantly down, is it fair to assume that the only unrecoverable expense that I should assume is the right-of-way payment of roughly $100 million, say '15, 16, 17?

Kent Harvey - PG&E Corporation - SVP, CFO

Yes, if you look at slide 13, it really lays out the natural gas matters beyond 2013. You can see most of those items we would be either completing the expenditures on or pursuing them through our normal pipeline rate case. So it really is the right-of-way encroachment that is the multiyear item that we do not intend to pursue recovery of.

Angie Storozynski - Macquarie Research - Analyst

Okay, thank you.

Operator

Leslie Rich, JPMorgan.

Leslie Rich - JPMorgan - Analyst

Good morning. Just a couple quick questions. Can you remind me the purchase price for Oakley, when you do have to pay for it and it goes into rates?

Chris Johns - Pacific Gas and Electric Company - President

Hey, Leslie, this is Chris. We have not put out the price for Oakley. It is under a confidentiality agreement; and we still have to negotiate some of the pieces of getting the contract completed.

But what I can tell you is it is 586 megawatts. It is a modern facility. It is dry cooled, and it is in California with all our related regulatory costs that go with that.

Leslie Rich - JPMorgan - Analyst

Okay. Then on your comment on solar, you said that you would not continue with utility-owned solar investments beyond this year. I recall you had a solar program for X number of megawatts over a multiyear period. Was that scheduled to finish this year, or are you building less than you had originally thought?

Chris Johns - Pacific Gas and Electric Company - President

Leslie, we completed the first three years of a five-year program; so basically we are not completing the last two years. And as I said in my prepared remarks, we are just seeing prices that are much better through the contracting process.

Leslie Rich - JPMorgan - Analyst

Okay, thank you.

Operator

Dan Eggers, Credit Suisse.

Dan Eggers - Credit Suisse - Analyst

Hey, good morning, guys. Say, Tony, just on the OII proceedings and the outlook given the fact that the settlement talks fell apart a little while ago, is this something from your perspective that is going to have to go through the full regulatory process to come to conclusion? Or do you think there is leeway or interest in finding a workable solution for all the parties, given what you guys have been through so far?

Tony Earley - PG&E Corporation - Chairman, CEO, President

Yes, we made it clear that we are open to settlement. As I have said time and again, we need to get these proceedings behind us.

That said, we have got to get the other parties to the same position. I was disappointed toward the end of last year; we thought we were getting very close, and it became apparent that we weren't as close as we had hoped.

But we made it clear to everyone we are ready to sit down. But what I don't want to do is go into expanded settlement discussions and defer resolution of the proceedings.

As we saw from the PSEP proceeding, while the result wasn't what we had wanted, it is a result. We know where we are; we had the plan approved; and we can now move forward and deal with it.

So it is almost more important to us to keep the proceedings moving, to get them done. But that said, these settlements can occur very quickly if in fact we get all the parties agreeing that is what we want to do.

Dan Eggers - Credit Suisse - Analyst

Okay, got it. Then I guess on the encroachment issue, how did you guys come to the $500 million number based on what you have surveyed so far? How high is your confidence that is going to be the ultimate cost?

Chris Johns - Pacific Gas and Electric Company - President

Dan, this is Chris again. What we did is that, as I said, we are going to go through a detailed centerline project, but that project is going to take us through the end of this year to get completed. So we wanted to be able to provide some overview of what we think the numbers would be.

So we used a lot of our aerial photography capability to look over the lines. Then we also used some inputs from testing that we have been doing over the last year, including some pilots that we had in place.

So what we tried to do is estimate based on what we have seen in the past how many -- how much vegetation is out there around our lines, how many structures might be in and around them, and then estimate what those costs would look like in doing that. So as you can imagine, the large part of that $500 million is construction-type cost and vegetation management-type costs that are associated with that.

So we feel like we have done a lot of due diligence around it. Obviously, we will have to tweak it as we physically get out and walk the line to make sure. But we think we have a pretty good estimate there.

Dan Eggers - Credit Suisse - Analyst

Okay. I guess one last one, Kent. When you look at the range of CapEx, the high end to base case, can you just maybe help bucket a little bit more that span? How much of that is going to be pipeline-related versus electric transmission-related versus other stuff? Just so we can try and gauge the potential for the high versus low.

Kent Harvey - PG&E Corporation - SVP, CFO

Dan, I think on the slide we kind of -- at least for 2013 show our pipeline spend broken out in the assumptions page which was, I think, slide 6. So you get a sense of our electric transmission CapEx for this year is about $800 million. Excuse me, are you saying electric or gas? I'm sorry.

Dan Eggers - Credit Suisse - Analyst

Both, actually.

Kent Harvey - PG&E Corporation - SVP, CFO

Okay. Yes, that slide shows you how much is electric transmission; it shows about $850 million. Then you see the gas transmission, which is in the $350 million range.

So those are kind of -- then you want to add the PSEP down below, which is $450 million. So there are comparable sizes to those two parts of our business.

Dan Eggers - Credit Suisse - Analyst

So you expect to continue at that rate, and just the sensitivity due to that spending is going to affect the range?

Kent Harvey - PG&E Corporation - SVP, CFO

Well, you know, it is not exactly the same number in future years. But you will see overall we are increasing, and those would be some part of those increases.

Dan Eggers - Credit Suisse - Analyst

Okay. Thank you, guys.

Operator

Jonathan Arnold, Deutsche Bank.

Jonathan Arnold - Deutsche Bank - Analyst

Good morning, guys. I am just curious. I think Tony made the comment at the beginning that in 2014 you targeted earning the allowed return everywhere except the gas transmission business. Given that a lot of these emerging work costs and other stuff here, if I am understanding you right, they are excluded from operating earnings, will you comment on the GAAP results? Or are there other things that are causing you not to earn that allowed return in '14?

Kent Harvey - PG&E Corporation - SVP, CFO

Jonathan, this is Kent. In 2014, it is just that the gas pipeline profile is what it is. We are spending dollars in a lot of areas that weren't in our last gas transmission case.

Our intent is in 2015 to be able to true that up for the items other than the right-of-way work. So that is really why 2015 is a really important year for us on the gas transmission business.

The other lines of business we would be addressing through our General Rate Case in 2014, and then our Transmission Owner case for electric transmission which we tend to do just about annually.

Jonathan Arnold - Deutsche Bank - Analyst

Okay, so it is really the integrity management and other work? Or is that below the line?

Kent Harvey - PG&E Corporation - SVP, CFO

Well, the integrity management, you are right, we have been breaking out as a big new category where we are spending a lot. But even within the gas transmission business, notwithstanding the item impacting comparability, I indicated that of our incremental spend across the utility of $250 million this year and last year, about $50 million of that is in the gas transmission business. So that piece of the $250 million also wouldn't be trued up until 2015.

Jonathan Arnold - Deutsche Bank - Analyst

Okay. Understood. Thank you.

Then on the equity, Kent, you have listed out the various, DRIP, 401(k), dribble. Can you just remind me what's a reasonable expectation for how much you could raise through those programs collectively, and at what level you would be looking to step outside of those plans?

Kent Harvey - PG&E Corporation - SVP, CFO

Well, if you look at our 2012 equity issuance, for example, which was $775 million, we did those in three fairly equal pieces. So we got about a third of that through our internal programs, our DRIP and our 401(k). We got about a third of that through our dribble program. And then the remaining third, about $250 million, we did through a block transaction early last year.

So that is not to put a cap on how much you could do, for example, through the dribble program. That is just how much we did last year.

And we are going to continue to evaluate the options that make sense for us, given our profile and the timing and so forth in 2013. Obviously, one factor will be when and how the pipeline matters get additionally resolved.

Jonathan Arnold - Deutsche Bank - Analyst

Sure. But does it seem -- is there a scenario where you could do the number you have put out? I guess the number is likely to be bigger whatever. But would you use those base assumptions from last year? About two-thirds of last year's number through the programs and the rest as a block, is that a good working assumption?

Kent Harvey - PG&E Corporation - SVP, CFO

Jonathan, I think the key will be we will probably get up to about $300 million through our internal programs. And we would want to optimize the rest of our issuance.

Jonathan Arnold - Deutsche Bank - Analyst

Okay.

Kent Harvey - PG&E Corporation - SVP, CFO

So undoubtedly the dribble will be a significant component of that, but we are going to really use the various options that we have in the way that makes the most sense, so that we can have issuance that is both efficient and effective.

Jonathan Arnold - Deutsche Bank - Analyst

Fair, all right. Thank you.

Operator

Hugh Wynne, Sanford Bernstein.

Hugh Wynne - Sanford C. Bernstein & Co. - Analyst

Hi. Tony, as you know, the normal utility business model is you provide safe and reliable service; you get to invest a lot of capital doing it; you earn a nice return on that; and then you pass through the operating cost to the customer. On the gas side, PG&E seems to be running kind of an anti-utility, where the service isn't safe and reliable; you spend a lot of capital trying to catch up on the safety and incur a lot of integrity management costs; and then you just write it off. It is kind of like burning $100 bills.

How confident are you that this is over now? Or do you fear that there could be other items like the right-of-way clearance that are still looming ahead and might limit your ability to recover capital and operating costs in future?

Tony Earley - PG&E Corporation - Chairman, CEO, President

Well, we are clearly playing catch-up in investing in the system. But I think we are starting to see certainty emerge.

So for example the Pipeline Safety Enhancement Plan, as we said, went through the proceeding. We had proposed that we recover about 85% of the plan. Some of the interveners in the case said -- no, you ought to recover nothing. We ended up in the 60% range or so, which is less than we wanted, but it gives us some certainty about what we are going to recover going forward in the future.

In terms of what other expectations -- one of the other things that we have done is we have reviewed and are in the process of reviewing every single aspect of our gas business. Kind of divided the system into asset classes -- so gas transmission, rights-of-way, gas storage. And we prioritized based upon where we thought the largest risks might be.

We are comfortable that we think we have identified all of the large risks. We are not through all of the asset classes yet, but the ones that we are working through and we want to be through are top to bottom reviews, certainly by the end of 2013. But since they are lower-risk areas, we don't expect numbers to emerge that would be anywhere near what we are seeing from the right-of-way clearance numbers.

Hugh Wynne - Sanford C. Bernstein & Co. - Analyst

Great. And Kent if you have already said this, I apologize, but can you remind me what FERC ROE is assumed in the earnings guidance for '13?

Kent Harvey - PG&E Corporation - SVP, CFO

Yes, Hugh. We are assuming the 9.1% which was what we were ordered to refile with the FERC. So that is assumed for 2013.

Hugh Wynne - Sanford C. Bernstein & Co. - Analyst

Great. Thank you very much.

Operator

Brian Chin, Citi.

Brian Chin - Citigroup - Analyst

Asked and answered, actually. Thank you very much.

Operator

Ashar Khan, Visium.

Ashar Khan - Visium Asset Management - Analyst

Hi, good morning. Kent can I just ask, what -- I might have missed this in your presentations, I apologize, running. What is the average shares outstanding in the '13 guidance?

Kent Harvey - PG&E Corporation - SVP, CFO

I actually didn't provide a share count for the '13 guidance. But we have indicated that the year-end count was 431 million shares and that our guidance, based on the assumptions we provided, is to issue equity of between $1 billion and $1.2 billion during 2013.

That all is based on our current accrual for the fine. So if the fine ends up being an incremental amount above that, then you would want to adjust those estimates accordingly.

Ashar Khan - Visium Asset Management - Analyst

Okay. If I can then ask another related question, where did that book value per share end up for the Corporation at the end of the year?

Kent Harvey - PG&E Corporation - SVP, CFO

I don't have that with me, Ashar, but that will be available when we get our 10-K out later today.

Ashar Khan - Visium Asset Management - Analyst

Okay, okay. Fair enough. Thank you, sir.

Operator

Michael Lapides, Goldman Sachs.

Michael Lapides - Goldman Sachs - Analyst

Hey, guys. A couple questions, looking at both page 6 and page 8, the guidance on the natural gas matters. First question, I completely understand the moving all the PSEP and all the San Bruno items into the IIC.

But just curious; what went behind the decision to move things like the right-of-way work? Doing work for the next five years strikes me as a recurring item a little bit. That is the first question.

Second, can you clarify that second bullet point on financing and depreciation costs? Are you saying that is $1 billion and therefore you would apply whatever depreciation rate to that to get to what the earnings drag from that would be?

Kent Harvey - PG&E Corporation - SVP, CFO

Yes, this is Kent. Let's take your second question first. You are interpreting the bullet on slide 6 correctly.

We expect our CapEx to be roughly $1 billion over what was authorized in our last GRC and other proceedings. So during this year we will incur the associated financing and depreciation costs on that; and then that is what we would true up in the 2014 General Rate Case. So that is the correct interpretation.

Your other question about the natural gas matters is – you are correct that the right-of-way work is for a long period of time. What we've tried to do with all the gas matters is give you the full picture of them because every – all of this really relates to the recovery following the accident at San Bruno. So what we are trying to do is give you as much transparency as possible so that you can understand what is in there, as compared to just have it all blended into our overall GAAP results.

Michael Lapides - Goldman Sachs - Analyst

Got it. When we look at your rate base guidance slides through 2016, I think it is slide 12, does that include or exclude the CWIP balance? And can you just give us an update on what that CWIP balance is?

Kent Harvey - PG&E Corporation - SVP, CFO

It did not include the CWIP balance, and I have indicated in our guidance that we would expect our below-the-line costs that we normally incur to largely offset our equity AFUDC. So we have not included that on the slide.

In terms of what CWIP has usually run for us, I would say over the last two years it's probably averaged in the $1.5 billion range, something like that. So you could probably use that as a ballpark estimate.

Michael Lapides - Goldman Sachs - Analyst

Got it. I guess one final question, just when you think about financing and over the next 12 to 24 months, really the next several years. Would you ever consider using anything other than just straight common? Meaning converts or something like that. We have seen some other companies in the industry use that to help finance when they have got a multiyear high-growth and CapEx plan. Or from a regulatory standpoint does that make it harder to use instruments like that?

Kent Harvey - PG&E Corporation - SVP, CFO

No, I would say those are instruments that we are definitely considering in the future. We have a lot of different alternatives, and we are really trying to figure out which ones make the most sense for us given our profile, the timing and nature of our needs. But those are definitely on the radar screen.

Michael Lapides - Goldman Sachs - Analyst

Got it. Thanks, guys. Much appreciated.

Operator

Anthony Crowdell, Jefferies.

Anthony Crowdell - Jefferies & Company - Analyst

Good morning, guys. I just want to know, when I look at the midpoint of your 2013 guidance, and I look at your forecasted rate base, I calculate an earned ROE of somewhere like 5.0%, 5.1%. Can you break out what you think the earned ROEs will be in '13 for your electric and gas business?

And going forward in '14 and '15, any comments on where you expect those ROEs to be?

Kent Harvey - PG&E Corporation - SVP, CFO

This is Kent. I don't intend to break out earned ROE that specifically, but I would point you again to slide 6, which essentially shows you what our authorized returns are. And then in the lower right-hand corner we have what we label as EPS factors. Those are the key items that will affect our ability to earn the authorized returns.

We have been telling you for a while about our incremental spend across the utility, and that includes both the gas and the electric parts of our business, of $250 million. We just spoke briefly about the impact of higher CapEx for 2013. We talked about the fact that we are expecting our below-the-line costs to essentially offset our CWIP earnings this year.

And then we have continued to have a little bit lower gas storage revenues than was assumed in our gas pipeline case. And that is comparable to last year, but it has been a bit of a drag compared to an authorized return.

Then the offset to that is that we do assume that we get energy efficiency incentive as we got late last year.

Anthony Crowdell - Jefferies & Company - Analyst

Okay. If I look then, I guess, past '14 -- and I just want to make sure I have heard the correct statements. I think Tony had said earlier in the call that in '14 you expect to earn your allowed return in electric. Is that correct?

And possibly in '15 when you file your gas case, is it reasonable to assume that you earn your allowed return? Or I guess the only cost that you are not putting in there would be the right-of-way encroachment; is that accurate?

Kent Harvey - PG&E Corporation - SVP, CFO

Yes, I think that's right. When you say gas, in this case what we're talking about is the gas pipeline part of our Company. Gas distribution will be addressed in our General Rate Case in 2014.

Anthony Crowdell - Jefferies & Company - Analyst

Okay, and it's reasonable to say that '14 you guys earn the allowed return in, I guess, gas distribution and electric. And '15 you hope to have all the gas pipeline costs except right-of-way in that rate case for new rates January 1 of '15.

Kent Harvey - PG&E Corporation - SVP, CFO

That is what our objective is.

Anthony Crowdell - Jefferies & Company - Analyst

Great. Thank you, guys.

Operator

Jon Cohen, ISI Group.

Jon Cohen - ISI Group - Analyst

Hey, good morning. I just had a question about the timing of the equity issuance. So if we are standing at the end of 2013 and you would have issued the $1 to $1.2 billion, can we assume that all of the unrecovered costs through '13 are now going to be incorporated in your capital structure and you're going to be sitting at a 52% equity ratio? And really beyond 2013, the only equity that you will have to issue other than normal course of business, CapEx, and the fine, is going to be for the integrity management, the PSEP, O&M in '14, and the integrity -- and sorry, the encroachment beyond 2013.

Kent Harvey - PG&E Corporation - SVP, CFO

This is Kent. I think you are thinking about it the right way. We don't really necessarily manage to be at exactly our authorized equity ratio, say, December 31 of 2013. But we do have to manage our capital structure over a period of time such that it averages to that level.

So sometimes we are slightly below, sometimes we are slightly above. But the intent of your statement is correct, which is that we try to keep up with our equity needs over time. And I think the way you articulated some of the costs beyond 2013 that we would need to fund with incremental equity sounds appropriate to me.

Jon Cohen - ISI Group - Analyst

Okay. Then can you just let us know, in that $1 to $1.2 billion, do you assume any incremental insurance recoveries above what has already been received?

Kent Harvey - PG&E Corporation - SVP, CFO

We have not provided in our guidance any assumptions about insurance. When we do our internal forecasting and determine some of the ranges of what financing needs we have, we usually try to come up with some assumptions about insurance proceeds. But we are not disclosing what those are, baked into our equity assumptions.

Jon Cohen - ISI Group - Analyst

Okay, thanks, and then the last question is, do you have some flexibility over when you issue the equity? So if you think that you might get closer to a settlement between now and year-end, could you put off the equity issuance and sort of lean on short-term debt or the parent revolver and do one big equity issuance later in the year?

Kent Harvey - PG&E Corporation - SVP, CFO

Yes, we do have flexibility about the timing, although we do need to maintain our capital structure over time. So we wouldn't want to get too far off on that issue.

But we do have some flexibility there, and we do intend to issue it in a way that is efficient and to not be -- to not have to be rushed to issue equity in a way that wouldn't make sense for our Company and our shareholders. So we would try to manage that. And I would anticipate if we needed to manage the timing of an issuance that we could do some short-term measures to give us that flexibility, such as you describe.

Jon Cohen - ISI Group - Analyst

Okay, great. Thanks a lot.

Operator

Travis Miller, Morningstar.

Travis Miller - Morningstar - Analyst

Good morning. Thanks. Wonder if you could quantify the difference in the drop from 2012 EPS to 2013 midpoint guidance that came from that cut in the allowed ROE? And then also perhaps the cash flow impact from that.

Kent Harvey - PG&E Corporation - SVP, CFO

Well, that is the biggest item, Travis, there is no doubt about it. I think you can pretty much just get there by taking the rate base amounts, which we have broken up by line of business.

So you can take electric transmission, for example, and you could go from what was implicitly in our guidance before for last year of 11.35% and take it down to 9.1%, 52% of that rate base. And then you could do the same calculation for the other lines of business going from 11.35% to our new assumption of 10.4% based on the PUC's decision. And I think you'll pretty much land with what we landed with.

Travis Miller - Morningstar - Analyst

Okay, great. Then real quick, how much incremental debt do you expect to issue in 2013? Obviously we've heard about equity but what about debt?

Kent Harvey - PG&E Corporation - SVP, CFO

You know, we have been -- if you look over the last several years we have been issuing long-term debt annually. That probably averages about $1 billion; and I wouldn't expect a significant difference in that in terms of an order of magnitude change or anything. So somewhere in that very rough range would probably be a reasonable expectation for 2013.

Travis Miller - Morningstar - Analyst

Okay, great. Thanks a lot.

Operator

Kevin Fallon, SIR Capital Management.

Kevin Fallon - SIR Capital Management - Analyst

Good morning. Just a question. Do your financing plans and your rate base guidance include the impact of bonus depreciation?

Kent Harvey - PG&E Corporation - SVP, CFO

You know, they do for this most recent bonus depreciation. But the reality of our situation is, given the pancaking we have had from the last several years of bonus depreciation, even before 2013 bonus was approved we already were expecting to be in a net operating loss position for 2013.

So it is really not going to be providing us any financing benefit incrementally in 2013. And we will probably see that benefit actually next year, just given our current situation.

Kevin Fallon - SIR Capital Management - Analyst

Okay. Just to clarify, on slide 12, the rate base slide. Those are average rate bases or year-end rate bases for the shown years?

Kent Harvey - PG&E Corporation - SVP, CFO

Those are average rate bases.

Kevin Fallon - SIR Capital Management - Analyst

Okay. Finally, just if you could give some color on the FERC rate case process. As you go through the settlement talks, when you ultimately come to the end point, however it turns out, is the ROE adjusted for the change in the 10-year Treasury? So if interest rates move higher, do they make adjustment? Or are you stuck at that base 8.6% for this proceeding no matter what?

Tom Bottorff - Pacific Gas and Electric Company - SVP Regulatory Affairs

This is Tom Bottorff, Senior Vice President of Regulatory Affairs. The rate of return is yet to be determined in that proceeding. But if we settle the case the rate of return is sort of implicit. It is not explicitly adopted as part of the settlement.

So as in prior rate cases, there really is no adopted rate of return. That would only happen in the event of going to litigation and having a decision.

Kevin Fallon - SIR Capital Management - Analyst

But that is what I mean. They gave you a point estimate to change rates on under the current 8.6% base ROE. And that is what I am asking. That was an administrative determination by the FERC.

Is there an administrative process, ex something in a settlement, that changes that? Or is that 8.6% the base unless you reach a different number in the settlement?

Tom Bottorff - Pacific Gas and Electric Company - SVP Regulatory Affairs

If we reach a different number in the settlement, then the rates will be based on that adopted settlement figure.

Kevin Fallon - SIR Capital Management - Analyst

But if the case is litigated and rates move higher, is it adjusted upward or is it stuck at that 8.6%?

Kent Harvey - PG&E Corporation - SVP, CFO

Right now the issue is we had to submit our application with the 9.1%; it has the 8.6% plus a 50 basis point adder for the California ISO. And that is based on data that was available when we did the filing. It essentially looks at a number of comparable utilities.

And it is prescriptive in that we are required to use the DCF model, which of course is particularly disadvantageous in this current economic environment and we don't think representative of our true cost of equity. So we would have to litigate that. And unless the FERC ended up with something that was more reasonable, then we would have to seek legal review of that decision.

Kevin Fallon - SIR Capital Management - Analyst

Okay. Thank you very much.

Gabe Togneri - PG&E Corporation - VP IR

Jackie, this is Gabe. We have reached the one-hour point and we have some time constraints on this end. Is there one more question that is in the queue?

Operator

Ashar Khan.

Gabe Togneri - PG&E Corporation - VP IR

Let's go ahead and take that one.

Ashar Khan - Visium Asset Management - Analyst

Kent, I just went back and looked at your 10-K from the third quarter. So I guess you were around $30; and then I've got the GAAP earnings and the dividend. Am I -- tell me if I am doing my utility math wrong or right.

GAAP earnings you are showing this year $1.66 to $2.00. The dividend is around that level. So assuming we come out or book value does not increase, it remains at $30 or so, then is it fair to look at it that if the Company earns around a 10% by the end of '13 that the earning power is more like $3 a share or something like that?

Kent Harvey - PG&E Corporation - SVP, CFO

I don't know; I can't follow your logic over the phone. So if you want to follow-up with our IR team about your question, maybe we can handle it that way, Ashar.

Ashar Khan - Visium Asset Management - Analyst

Okay. Thank you.

Gabe Togneri - PG&E Corporation - VP IR

All right, I apologize for breaking in and if there are any questions remaining, but we do have some constraints on this end. Please call the Investor Relations line if you have any follow-up questions.

And we will wish you a great day, and talk to you the next time. Thank you.

Operator

Ladies and gentlemen, thank you for attending the PG&E Corporation fourth-quarter earnings conference call. This now concludes the conference. Enjoy the rest of your day.
