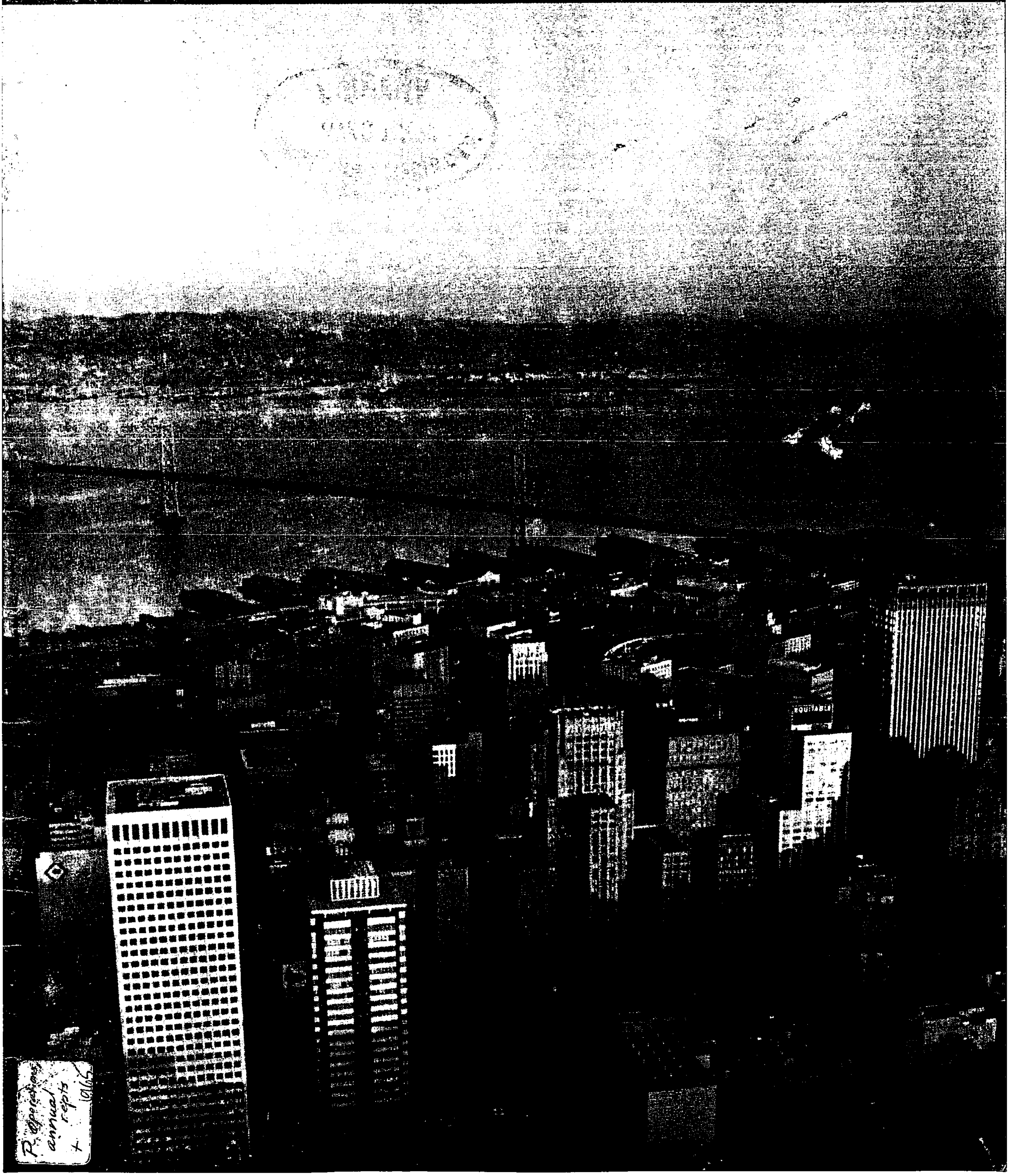
PACIFIC GAS AND ELECTRIC COMPANY ANNUAL REPORT 1965



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With profound respect and affection for James Byers Black, the directors of Pacific Gas and Electric Company dedicate this 1965 Annual Report to his memory.

JAMES BYERS BLACK
1890 - 1965

On March 20, 1965, death ended the distinguished public service career of James B. Black. He was the principal architect of the mergers in 1930 which gave Pacific Gas and Electric Company essentially its present service area. For almost 30 years since 1935 Mr. Black played an important role in guiding the destinies of the Company, first as President and later as Chairman of the Board.

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Cover: San Francisco's changing skyline.

BOARD OF DIRECTORS

ROBERT H. GERDES*, *San Francisco*
Chairman of the Board
K. C. CHRISTENSEN, *San Francisco*
RANSOM M. COOK, *San Francisco*
JAMES F. CRAFTS*, *San Francisco*
PAUL L. DAVIES, *San Jose*
CHARLES DE BRETTEVILLE, *San Francisco*
RUSSELL GIFFEN, *Fresno*
WALTER A. HAAS*, *San Francisco*
REED O. HUNT†, *San Francisco*
ELLIOTT MCALLISTER*, *San Francisco*
DAVID PACKARD, *Palo Alto*
PORTER SESNON, *San Francisco*
S. L. SIBLEY*, *San Francisco*
EMMETT G. SOLOMON, *San Francisco*
CARL F. WENTE*, *San Francisco*

*Member Executive Committee
†Elected April 21, 1965 to succeed James B. Black, deceased.

EXECUTIVE OFFICERS

ROBERT H. GERDES, *Chairman of the Board and Chief Executive Officer*
S. L. SIBLEY, *President and Chief Operating Officer*
K. C. CHRISTENSEN, *Senior Vice President*
JOHN F. BONNER, *Senior Vice President*
R. L. HAYDEN, *Senior Vice President*
RICHARD H. PETERSON, *Senior Vice President and General Counsel*
H. P. BRAUN, *Vice President — Electric Operations*
E. H. FISHER, *Vice President — Gas Operations*
ROBERT R. GROS, *Vice President — Public Relations*
E. J. LAGE, *Vice President — Rates and Valuation*
FREDERICK W. MIELKE, JR., *Vice President and Assistant to Chairman*
V. C. REDMAN, *Vice President — Commercial Operations*
C. H. SEDAM, *Vice President — General Construction*
JOHN G. SMITH, *Vice President — Personnel and General Services*
C. C. WHELCHEL, *Vice President — Engineering*
D. L. BELL, *Treasurer*
L. W. COUGHLAN, *Comptroller*
EDMOND E. MANHARD, *Secretary*
FREDERICK T. SEARLS, *General Attorney*

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A. H. CATHERALL, *Assistant Secretary and Assistant Treasurer*
A. J. DUFFY, *Assistant Treasurer*
J. N. GEHRE, *Assistant Secretary*
JOHN F. TAYLOR, *Assistant Secretary*

HIGHLIGHTS OF OPERATION

	1965	1964
Operating Revenues and Other Income	$ 853,660,000	$ 817,446,000
Natural Gas Purchased	$ 223,615,000	$ 222,316,000
Taxes and Franchise Payments	$ 170,741,000	$ 163,451,000
Operating Payroll	$ 102,787,000	$ 99,112,000
Other Expenses and Charges	$ 216,244,000	$ 206,731,000
Net Income	$ 140,273,000	$ 125,836,000
Earned Per Common Share (on end-of-period shares)	$2.08	$1.83
Total Assets	$3,277,887,000	$3,090,387,000
Construction Expenditures	$ 286,708,000	$ 240,071,000
Sales of Electricity to Customers (KWH)	31,683,319,000	30,592,261,000
Sales of Gas to Customers (MCF)	537,297,000	487,423,000
Total Customers	4,346,462	4,212,548
Number of Employees	21,004	19,846
Number of Stockholders	260,280	258,272

ROBERT H. GERDES
Chairman and Chief Executive Officer

SHERMER L. SIBLEY
President and Chief Operating Officer

REPORT OF THE DIRECTORS OF PACIFIC GAS AND ELECTRIC COMPANY

San Francisco, California, February 25, 1966

TO OUR STOCKHOLDERS:

The year 1965 was one of vigorous growth for the Company and the territory it serves. New record levels for sales and revenues, earnings and dividends, and construction expenditures were attained.

Net earnings available for the common stock were $2.08 a share compared with $1.83 a share in 1964, both based on the number of shares outstanding at the respective year-ends. The increase of 25¢ per share, or 14%, is attributable to our increased business, greater operating efficiencies, invested earnings, and an excellent water year which produced increased hydroelectric generation with resultant savings in fuel costs.

In March the dividend on the common stock was increased from $1.10 to $1.20 on an annual basis. This was the fourth dividend increase in the last five years.

Operating revenues reached $851 million, an increase of $36 million over the previous year. This substantial gain in revenues was achieved notwithstanding a rate reduction amounting to $10 million annually which became effective in mid-1964, and below normal electric sales for agricultural pumping and resale because of heavy precipitation.

CUSTOMER GROWTH

133,914 new customers were connected to our lines in 1965, as compared with 146,725 in the previous year. This 9% decline was the result of some overbuilding of new dwelling units, particularly multifamily dwellings, as occurred nationwide during 1963 and 1964. There is now evidence that the backlog of unoccupied dwelling units in our service territory is being fairly well absorbed.

Among new customers last year was a Sacramento family who, in December, became the two millionth customer on our gas system. It took ninety-eight years to gain the first million gas customers and only fifteen years for the second million. At the year-end the Company was serving 4,346,462 customers in all branches of its operations.

COMMERCIAL AND INDUSTRIAL ACTIVITY

The rapid population growth in our service area has been accompanied by an even greater increase in commercial and industrial activity, a few highlights of which are featured in subsequent pages of this report. New commercial and industrial business, both gas and electric, connected last year exceeded that of any previous year, and we expect an even greater volume of new business in these categories this year.

One of the significant features of the industrial development in our service area has been its extraordinary diversity. An unusually large number of industrial classifications are represented. They are widely dispersed geographically throughout the area, although the main concentration is around the San Francisco Bay. The diversity is evidenced by the fact that last year no single type of industry accounted for more than 3% of our revenues and no single industrial customer contributed as much as 1% to our revenues.

CONSTRUCTION EXPENDITURES

To keep pace with the rapid growth the Company in 1965 spent $287 million on new construction, by far the largest of any year in our history. We expect to spend approximately the same amount in 1966 to continue our expansion. A 210,000 kilowatt steam-electric generating unit, located in and designed primarily to serve the City of San Francisco, was dedicated in December at our Potrero Power Plant. The 330,000 kilowatt McCloud-Pit hydroelectric project was substantially completed by year-end. Construction continues on two 750,000 kilowatt steam-electric generating units at our Moss Landing Power Plant. The first unit will be placed in service in 1967 and the second in the following year.

Work continued on our $185 million program to build 500,000 volt transmission lines which will serve as a link in the Pacific Northwest-Southwest Intertie. These lines will transmit surplus Northwest power into California, and also will serve to transmit large amounts of power between various points on the Company's system and among members of the California Power Pool. The first 89-mile portion of this system was placed in operation in December, transmitting power from our McCloud-Pit hydro system at 230,000 volts, initially. Operation at 500,000 volts over this and other parts of the system is scheduled to begin in 1967.

Throughout the year the Company continued its search for new sites for future steam-electric generating plants—conventional and nuclear. Several advantageous new sites have been purchased. During this year we expect to select the site for, and to order, a large nuclear plant for operation in the early 1970's. We believe that after 1970 the major proportion of the Company's new electric generating facilities will be nuclear.

ADDITIONAL GAS SUPPLY

Steps are proceeding to secure an additional long-term supply of natural gas. Authorization has already been granted by governmental authorities in Canada to increase the average daily deliveries of gas to the Company through the Alberta-California pipeline from 415 million cubic feet to 615 million cubic feet. On February 17, 1966, an Examiner of the Federal Power Commission, subject to the approval of the full Commission, granted our subsidiary, Pacific Gas Transmission Company, the necessary authorization to import the additional gas and transport it to California. The Commission's decision is expected shortly. The incremental delivered cost to the Company of this additional gas would be relatively low, because only added compressors are needed to expand the capacity of the line. These can be installed at a relatively modest capital cost.

INCREASED ATTENTION TO ESTHETICS

Increasingly, the public is giving attention to matters of esthetics and the need to preserve and improve the attractiveness of our surroundings. This has resulted in more public awareness of highways and structures of various kinds, including overhead electric lines. Convinced that utility structures can be attractive as well as functional, the Company's engineers and designers and its landscape consultants are placing strong emphasis on esthetics in all new planning. This is reflected in our new substations, service centers, offices and other facilities.

For some time the Company has been conducting extensive research and working with manufacturers to develop methods to reduce the cost of underground electric distribution lines and to improve the appearance of overhead lines. An attractive streamlined system has been developed which has gained wide acceptance. Much progress has been made in reducing the cost of underground distribution lines, and they have been installed in many new subdivisions. The Company also has asked the California Public Utilities Commission to authorize a stepped-up program for converting existing overhead distribution lines to underground in certain designated areas. Such conversions must take place gradually, however, because the cost of attempting a changeover within a short time would be prohibitive to both ratepayers and the

Company. Research is also being carried on with respect to underground high voltage transmission lines, but no economic solution has yet been found except in highly developed metropolitan areas.

The Company is also playing an increasingly important role in another area that has been occupying public attention, that of recreation. The Company has long had its reservoirs and watershed lands open for public enjoyment and in recent years has developed a number of camping and picnic sites in the Sierra and Cascade mountains. More will be opened this year. They have proved popular with the public and have resulted in a resolution by the California State Senate commending the Company for its recreation policies.

SYSTEM RELIABILITY

In the wake of the power blackout in the Northeast on November 9, we issued a statement reassuring our customers that such a massive power failure would be highly unlikely on our system. This opinion is based in part upon the wide dispersion of our generating facilities, including hydro, and the reserves maintained; the built-in ability of our system to isolate areas of trouble; and the extensive use of underfrequency relays to disconnect loads temporarily. Nevertheless, PG&E and other major California utilities created a task force of high level operating executives with directions to restudy intensively the reliability of our interconnected power systems in view of the Northeastern experience.

NEW COMPUTER USES

It was over ten years ago that we began the first studies for the application of electronic data processing to our operations. Since that time much has been accomplished. We now apply computer systems increasingly to many important areas of the Company's activities. This has enabled us to handle a greatly increased volume of business with much greater efficiency and economy.

However, a new era in electronic data processing equipment and the related systems technology is now emerging. These developments make it feasible to build more comprehensive systems than heretofore—systems commonly referred to as "total management information systems." These new systems span all aspects of the Company's operations and permit the most advanced techniques of management information, planning and control, and provide new approaches to management decision making. After a comprehensive study which broadly defined our requirements, a task force was activated to install such a system. The benefits we expect include increased capacity needed to handle an increasing volume of business efficiently and at reasonable cost, improved customer service, better controls, and elimination of repetitive routine decision making, so that managers and supervisors may function more effectively.

ORGANIZATION

On April 7, 1965 the Board of Directors elected the undersigned to their present positions, and shortly thereafter a number of changes were made in the organizational structure of the Company, which are described on page 21.

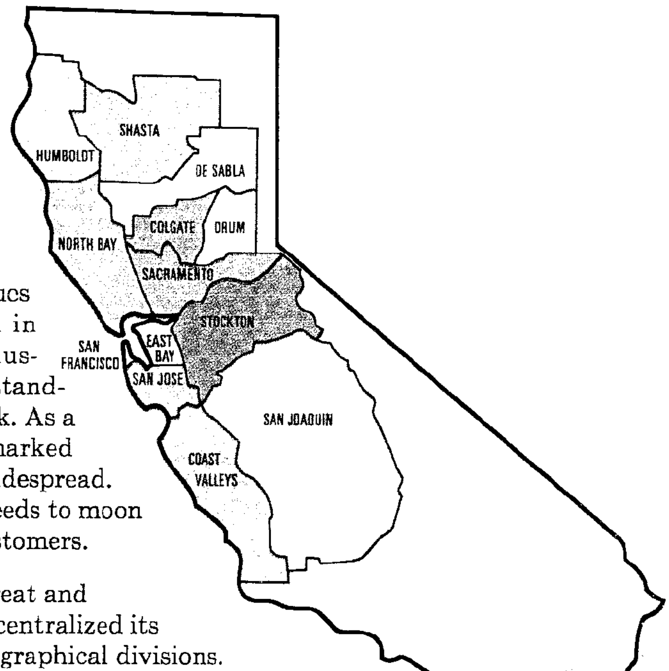
Public opinion surveys have shown that the phrase "courteous and friendly employees" is the term most frequently used by our customers to describe PG&E. The importance of the goodwill created by our employees, on and off the job, cannot be overemphasized. This is only one of the many reasons why we take this opportunity every year to acknowledge gratefully the splendid performance of our employees.

The pages that follow contain a more detailed review of our operations during the past year. Financial statements, together with the opinion of our independent certified public accountants, are set forth beginning on page 26.

Robert H. Gerdes *For the Board of Directors* S L Sibley

PG&E, PURVEYOR OF ENERGY FOR AN ABUNDANT LAND

FROM THE ice-carved summits of the Sierra Nevada to the sandy shores of the Pacific, from the redwood forests of Humboldt to the Mojave Desert – this is the area of California served by PG&E. Measure this service territory by its longest dimension and it will equal the distance between Washington, D.C. and St. Louis, Mo. All of New York and Pennsylvania could fit into its 94,000 square miles.



Within the 47 counties in which PG&E provides service reside an estimated 8.8 million people. There will be another quarter million by the end of 1966. It is an area exceeded in population by only six of the fifty states.

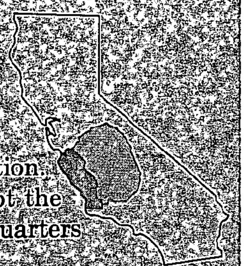
The great migration that began with the Gold Rush in 1849 continues to this day. But it is the arrival in increasing numbers of big new industries and businesses that is the outstanding feature of today's westward trek. As a result, the diversity that has long marked this area's economy is even more widespread. Products ranging from sunflower seeds to moon rockets are produced by PG&E customers.

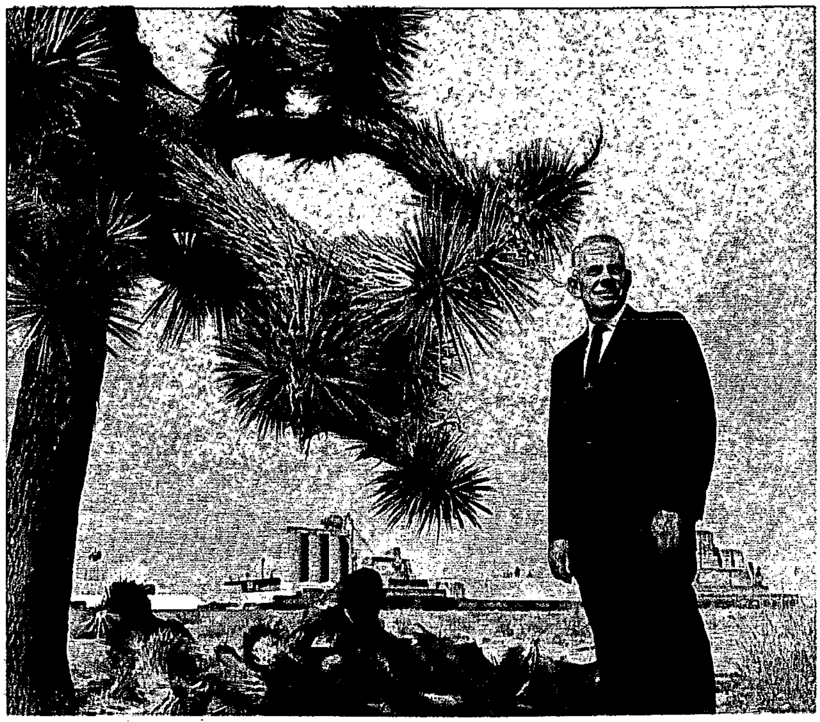
To meet the energy needs of this great and growing land, the Company has decentralized its daily operations throughout 13 geographical divisions. In this Annual Report, these divisions and the men who manage them are featured. Together they form a cross section of PG&E, and of Northern and Central California.

COAST VALLEYS AND SAN JOAQUIN

MAKING UP the southern third of the PG&E system are the Coast Valleys and San Joaquin divisions. Much of Coast Valleys consists of the Salinas Valley, transformed by irrigation to farms which yield three and sometimes four crops a year. Lettuce, artichokes, strawberries, sugar beets are just a few of the products of the valley. At the northern end of the division, Manager Leigh H. Smith stands amid a field of zinnias grown near San Juan Bautista by one of the nation's largest seed producers. At the southern end of the division are cattle, oil and Vandenberg Air Force Base and Missile Test Center. Headquarters of the division are in Salinas. Nearby is the beautiful Monterey Peninsula, with its world-famous golf courses and other recreational facilities.

SAN JOAQUIN DIVISION borders Los Angeles County on the south and covers most of the San Joaquin Valley from the crest of the Coast Range to the summit of the Sierra Nevada. It also extends into the Mojave Desert, a storehouse of mineral wealth. Division Manager Earl E. Foley, beside a Joshua tree, stands before a plant that processes the world's largest deposit of borax, one of the many extractive industries there which consume great quantities of natural gas. The division includes the nation's two leading cotton-producing counties, Fresno and Kern. The latter is also one of the country's major oil-producing counties. For 19 years California has ranked first in farm income, and the San Joaquin Valley is the hub of the state's "agribusiness" activities. The peaks of the Sierra Nevada to the east provide water, hydro power and summer and winter recreation. Factories of many types dot the valley floor. Division headquarters are in Fresno.





THE 1965 FINANCIAL STORY

REVENUES Revenues increased 4½% in 1965 to reach an all-time high of $851,399,000. We continued to have the largest operating revenues of any gas and electric utility in the nation.

Revenues in 1965 would have been considerably greater had it not been for weather conditions which restricted revenue growth in both the Electric and Gas Departments.

In the Electric Department satisfactory gains were recorded in the residential, commercial and industrial categories, our principal classes of business. Revenues from industrial power sales showed a gratifying gain of 7.2%. However, revenues from agricultural power and resale fell substantially below those of the previous year, both attributable to the weather. The above-normal precipitation resulted in a reduced demand for pumping of water for irrigation, and also, in the resale category, certain public agencies did not purchase their normal amounts of supplementary power from the Company.

In the Gas Department only nominal gains in revenue occurred in the residential and commercial classifications. This was because temperatures in 1965 were slightly above normal whereas in the previous year they were well below normal. On the other hand, revenues from industrial sales, which are not affected by temperatures, showed a very satisfactory gain of 7%. Resale revenues were almost double those of the previous year, reflecting increased sales of gas to the Pacific Lighting group of companies, which distribute gas in Southern California.

EXPENSES There was a relatively small increase in the cost of conducting our expanded operations in 1965. Operating expenses, exclusive of taxes and depreciation, amounted to $406,831,000. This was an increase of less than 3% over 1964 and was the smallest increase in recent years.

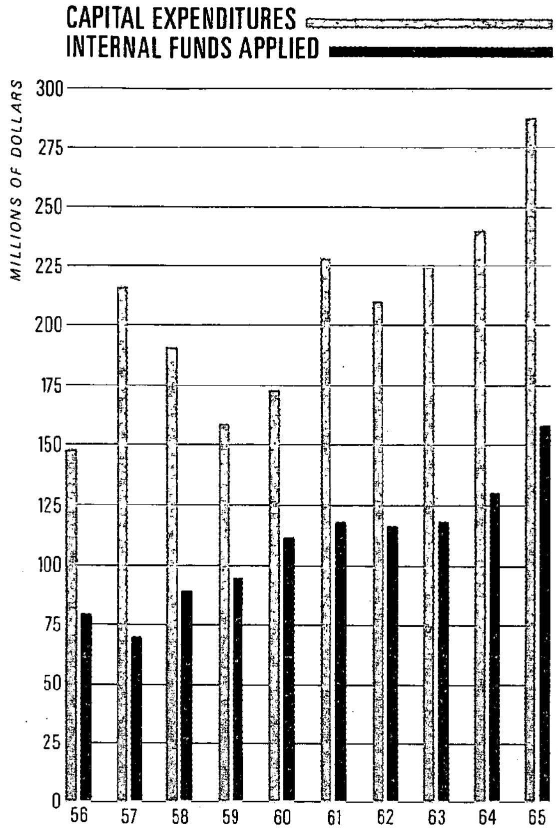
The exceptionally favorable water year for hydro generation, which substantially reduced the fuel requirements in our steam-electric generating plants, and the continued introduction of operating economies contributed to this result.

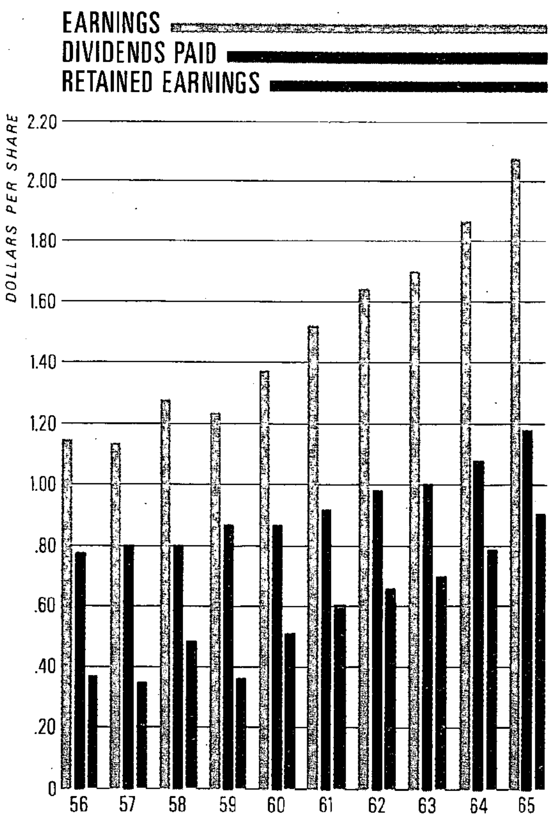
The purchase of natural gas for sale to our customers and for fueling steam-electric generating plants now accounts for more than half of our operating expenses. The average cost of gas purchased is, therefore, of major importance in the cost of conducting our business. Ten years ago the average cost of gas purchased was 25.7¢ per MCF. Thereafter, our gas suppliers made successive price increases with the result that our average cost reached a peak of 33.5¢ in 1962. In subsequent years, however, the average cost of gas purchased has declined, reaching an average of 30.5¢ in 1965. The significance of these figures is indicated by the fact that each 1/10th of a cent reduction in the average cost of gas reduces operating costs by three quarters of a million dollars annually. If we are successful in obtaining permits to import additional gas from Canada, a further decrease in the average cost of gas will occur.

Expenses in other areas of our operations have been kept under close control because of our continued emphasis on cost reduction practices, and the wider use of computers and other automatic equipment. Computers have not only taken over routine chores in accounting, but they have been applied to system planning, engineering and research. In 1965 we purchased automatic load dispatching equipment to bring 17 additional generating units producing 981,000 kilowatts of power under computer control. We plan to bring five more units producing 424,000 kilowatts under automatic dispatching this year. Computer operation automatically selects the most economical combinations of generating plants to meet varying load conditions.

An optical scanner that automatically transcribes data from meter reading documents directly to magnetic tape for electronic data processing has been ordered. A pilot operation using the new system will be started immediately. If successful, we expect to convert entirely to this method during 1966.

TAXES Taxes of all types totalled $180,657,000 in 1965, a new peak. This amount was equal to 21 per cent of our operating revenues; in other words, out of every dollar of a customer's bill, 21 cents was for taxes.


CAPITAL EXPENDITURES
INTERNAL FUNDS APPLIED
MILLIONS OF DOLLARS
300
275
250
225
200
175
150
125
100
75
50
25
0
56
57
58
59
60
61
62
63
64
65


EARNINGS
DIVIDENDS PAID
RETAINED EARNINGS
DOLLARS PER SHARE
2.20
2.00
1.80
1.60
1.40
1.20
1.00
.80
.60
.40
.20
0
56
57
58
59
60
61
62
63
64
65

The magnitude of the Company's role as tax collector is illustrated by the fact that the amount of taxes we paid last year is almost equal to the electric revenues collected from all residential customers in our entire service territory. This indicates the extent to which taxes affect the level of our rates. When Federal income taxes were reduced by the Revenue Act of 1964 from 52% to 48% in two annual steps, PG&E made a $9,800,000 annual rate reduction in order to pass the entire benefit to our customers.

With the tax burdens steadily mounting, particularly on the state and local levels, the sweeping tax exemptions that are accorded government-owned electric systems should be seriously reviewed by our citizens. Presently tax-sheltered and often tax-subsidized commercial operations of governmental agencies should bear their full share of the costs of government. This would also permit their efficiency and usefulness to be judged by the same yardstick that is applied to investor-owned businesses.

A table showing taxes by classes and a comparison with the previous year appears on page 12 of this report.

EARNINGS AND DIVIDENDS

Net income for the year amounted to $140,273,000, an increase of $14,437,000 over 1964. After $18,336,000 in dividends was paid to holders of preferred stock, there remained $121,937,000 for the common stock, or $2.08 a share.

On March 17, 1965, the Board of Directors increased the quarterly dividend on common stock from 27½ to 30 cents, equivalent to an increase from $1.10 to $1.20 per share on an annual basis. The first dividend at the new rate was paid to common stockholders on April 15, 1965.

The total dividends declared on the common stock during the year amounted to $70,484,000. The balance not paid out as dividends ($51,453,000) was reinvested in the business, thereby adding to the equity of common stockholders.

To comply with the requirements of the U. S. Internal Revenue Code, all dividend payments in 1965 to holders of PG&E stock, both common and preferred, have been reported to the Internal Revenue Service. Each shareholder for whom a report was submitted was mailed a copy in mid-December, 1965.

In the same mailing all common stockholders were advised that none of the common stock dividend payments in 1965 was excludable from their taxable income for Federal income tax purposes.

FINANCING

To assist in financing the Company's $287 million construction program in 1965, we sold at competitive bidding in July $75 million of our First and Refunding Mortgage Bonds, 4⅝%, Series LL, due June 1, 1997.

At year-end we had $46 million in short term bank loans outstanding. In January we received $25 million from the State of California for the sale of our Big Bend Powerhouse which will be flooded by waters behind the big Oroville Dam of the California Water Project. Proceeds from this sale were applied to reduce the amount of the outstanding bank loans.

We expect that the Company's new money require ments in 1966 will be obtained entirely from the sale of bonds. Initially we plan the sale, at competitive bidding, of $75 million of our First and Refunding Mortgage Bonds with bids to be received on March 15, 1966.

At the close of 1965 the Company's total capitalization was $2,900 million, consisting of 50.6% mortgage bonds, 12.1% preferred stock, and 37.3% common stock equity.

ANTITRUST SETTLEMENTS

Reference has been made in previous reports to the filing by the Company of 18 damage actions under the antitrust laws against various manufacturers of electrical equipment. Settlements have now been reached in all of these actions aggregating $8.7 million, of which the Company has received $7.0 million to date, the balance to be received in installment payments. These sums have been or will be credited to the appropriate plant accounts.

STOCK OWNERSHIP

At the end of 1965, the Company had 260,280 stockholders, a gain of 2,008 for the year. Of the total, 184,295 owned common stock and 75,985 preferred stock. The Company continues to be the most widely-owned electric and gas utility in the nation and ranks eighth in number of stockholders among all corporations in the country.

Many of our employees share in the ownership of the Company through their membership in the Employees' Savings Fund Plan. More than 1,500,000 shares of common stock have been purchased by the trustee for the accounts of employees since the Plan's inception. At year's end about 14,500 employees, or 93% of those eligible, were participating in this stock purchase plan which is designed to supplement retirement income.

On April 1, 1965 the Savings Fund Plan completed its sixth year of operation. In those six years, 1,480 P G &E employees retired as Plan members, each receiving an average of almost $3,000 in PG&E stock, U.S. Savings Bonds, or cash. Significantly, seven chose to receive stock for every one who chose cash upon leaving the Plan.

The distribution of PG&E stock ownership is indicated in the accompanying table. It should be noted, however, that although the majority of our outstanding stock is held by individuals, a large amount is held by institutional investors, such as insurance companies, investment companies and pension funds. The millions of people represented by these institutional investors have an indirect but nonetheless vital interest in the financial well-being of our Company. When their numbers are added to the 260,280 stockholders of record, the magnitude of the public's ownership of PG&E becomes very great indeed.

DISTRIBUTION OF STOCK OWNERSHIP

by Class of Investor, December 31, 1965

	Number of Stockholders	*Number of Shares Owned*
Women	100,028	18,084,164
Joint and other tenancies	70,546	10,272,552
Men	56,715	10,645,310
Trustees, guardians and other fiduciaries	23,247	3,746,812
Nominees	3,116	16,610,443
Corporations, partnerships and proprietorships	2,568	2,366,077
Charitable and fraternal organizations and foundations	1,297	489,138
Banks, investment companies and security dealers	1,086	4,321,786
Insurance companies	709	5,715,610
Religious institutions	575	151,637
Educational institutions	360	319,811
Labor organizations	33	23,079
Total	260,280	72,746,419

FIVE YEARS IN BRIEF

PACIFIC GAS AND ELECTRIC COMPANY

	1965	1964	1963	1962	1961
SOURCE OF INCOME:					
Electric revenues	$538,271,000	$518,903,000	$488,265,000	$463,405,000	$446,154,000
Gas revenues	310,762,000	293,728,000	271,428,000	263,608,000	246,432,000
Other operating revenues	2,366,000	2,328,000	2,157,000	2,412,000	3,122,000
Other income	2,261,000	2,487,000	2,388,000	2,247,000	1,694,000
Total	$853,660,000	$817,446,000	$764,238,000	$731,672,000	$697,402,000
DISPOSITION OF INCOME:					
Wages and salaries	$102,787,000	$ 99,112,000	$ 93,451,000	$ 88,489,000	$ 83,244,000
Power purchased	14,115,000	10,373,000	10,991,000	5,033,000	4,048,000
Natural gas purchased	223,615,000	222,316,000	203,568,000	196,145,000	185,776,000
Oil and other fuel	8,693,000	8,305,000	9,413,000	11,718,000	18,464,000
Other operating expenses	52,010,000	51,195,000	43,483,000	42,747,000	38,216,000
Insurance, injuries and damages, etc.	5,611,000	4,734,000	5,170,000	6,000,000	5,700,000
Depreciation	92,774,000	89,707,000	83,250,000	71,682,000	66,862,000
Taxes—current	168,408,000	160,964,000	147,300,000	152,225,000	148,587,000
Taxes—deferred	* 2,909,000	* 2,407,000	3,838,000	4,801,000	6,509,000
Bond interest and other income deductions	48,283,000	47,311,000	49,672,000	42,140,000	37,755,000
Dividends declared on preferred stock	18,336,000	18,336,000	18,336,000	18,336,000	18,336,000
Dividends declared on common stock	70,484,000	63,369,000	56,477,000	56,477,000	51,457,000
Balance retained in the business	51,453,000	44,131,000	39,289,000	35,879,000	32,448,000
Total	$853,660,000	$817,446,000	$764,238,000	$731,672,000	$697,402,000
NUMBER OF SHARES OF COMMON STOCK OUTSTANDING:					
Average for the year	58,736,429	57,606,878	56,477,326	56,477,326	55,229,907
End of year	58,736,429	58,736,429	56,477,326	56,477,326	56,477,325
EARNINGS PER SHARE OF COMMON STOCK:					
On average shares outstanding	$2.08	$1.87	$1.70	$1.64	$1.52
On end-of-year shares outstanding	2.08	1.83	1.70	1.64	1.49
DIVIDENDS PER SHARE OF COMMON STOCK:					
Declared basis	$1.20	$1.10	$1.00	$1.00	$ .93
Paid basis	1.18	1.08	1.00	.98	.92

*Denotes red figure.

SOURCE AND APPLICATION OF FUNDS

PACIFIC GAS AND ELECTRIC COMPANY

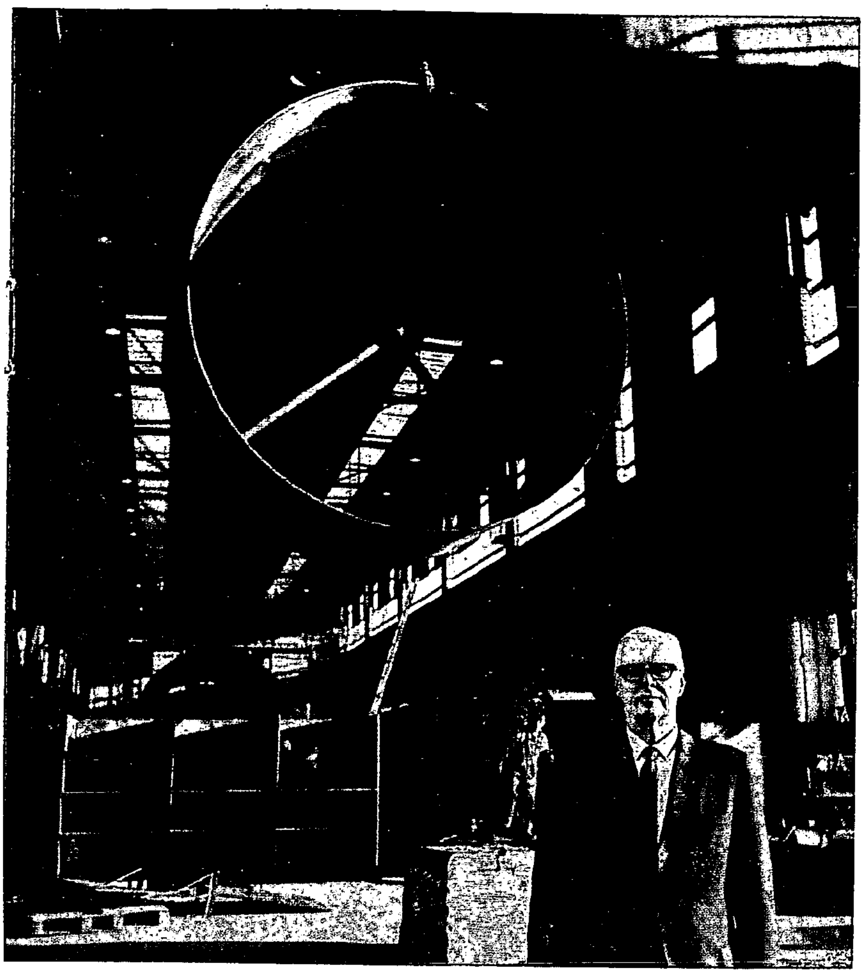
	1965	1964
SOURCE OF FUNDS:		
Net income	$140,273,000	$125,836,000
Depreciation (incl. charges to other accounts)	96,981,000	92,944,000
Mortgage bonds sold	74,853,000	64,493,000
Common stock sold	–	63,179,000
Bank borrowings	46,000,000	–
Sales and salvage of utility plant, and reimbursements	19,998,000	15,689,000
Decrease in working capital	12,858,000	–
TOTAL	$390,963,000	$362,141,000
APPLICATION OF FUNDS:		
Construction expenditures	$286,708,000	$240,071,000
Mortgage bonds retired	15,436,000	12,936,000
Dividends—preferred and common stock	88,819,000	81,704,000
Increase in working capital	–	27,430,000
TOTAL	$390,963,000	$362,141,000

TAXES AND FRANCHISE PAYMENTS

PACIFIC GAS AND ELECTRIC COMPANY

	1965	1964	*Increase*
LOCAL TAXES AND FRANCHISE PAYMENTS:			
Ad valorem property taxes	$ 89,163,000	$ 83,919,000	$ 5,244,000
Franchise payments	5,242,000	4,894,000	348,000
Total	94,405,000	88,813,000	5,592,000
STATE TAXES:			
Corporation franchise: current	8,515,000	7,714,000	801,000
Corporation franchise: deferred (net)	* 230,000	433,000	* 663,000
Unemployment insurance	2,155,000	2,064,000	91,000
Other	831,000	723,000	108,000
Total	11,271,000	10,934,000	337,000
CITY AND STATE TAXES:			
Sales and use	5,015,000	3,585,000	1,430,000
FEDERAL TAXES:			
Corporation income: current	68,419,000	64,145,000	4,274,000
Corporation income: deferred (net)	* 2,679,000	* 2,840,000	161,000
Unemployment insurance	274,000	472,000	* 198,000
Insurance contributions	3,797,000	3,597,000	200,000
Other	143,000	187,000	* 44,000
Total	69,954,000	65,561,000	4,393,000
CANADIAN TAXES	12,000	31,000	* 19,000
TOTAL TAXES AND FRANCHISE PAYMENTS	$180,657,000	$168,924,000	$11,733,000
CHARGED TO:			
Expense as taxes	$165,499,000	$158,557,000	$ 6,942,000
Expense as franchise payments	5,242,000	4,894,000	348,000
Utility plant and other accounts	9,916,000	5,473,000	4,443,000
TOTAL TAXES AND FRANCHISE PAYMENTS	$180,657,000	$168,924,000	$11,733,000

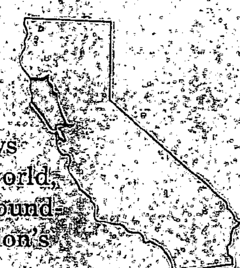
*Denotes red figure.



NORTH BAY AND SAN FRANCISCO

WORLD-FAMOUS table wines are produced in quality vineyards in the North Bay Division. So are atomic submarines (at Mare Island Naval Shipyard) and steel products from a Napa fabricating plant where Division Manager Elias S. Day stands. The division, with headquarters in San Rafael, extends northward from the Golden Gate Bridge and includes the booming residential areas of North Bay counties. It also embraces about 200 miles of rugged and scenic coastline, a flourishing lumbering industry, commercial and sport fishing, orchards, recreation centers and The Geysers Power Plant, where PG&E produces electricity using natural steam from the depths of the earth.

BIRTHPLACE and headquarters of PG&E is San Francisco. In 1852 the San Francisco Gas Company was founded, and there, in 1879, the California Electric Light Co. offered the first public electric service in the nation from a central station. From these and other predecessors, PG&E was formed in 1905. San Francisco is a bustling division headed by Harry A. Lee, shown at the Pacific Coast Stock Exchange. Financial center of the West, San Francisco is a city with an ever-changing profile. Great new office and apartment buildings are rising above its busy streets. A bold new rapid transit system is being built to whisk commuters and shoppers throughout the area. A vital city that draws tourists from all over the world, San Francisco and its surrounding Bay Area form the nation's gateway to the Pacific.



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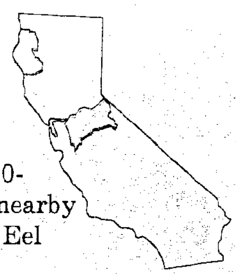
STOCKTON AND HUMBOLDT

IN THE HEART of the great central valley of California is Stockton Division, the geographic center of population of the three Pacific Coast states. The city of Stockton, division headquarters, is a deep water port about 80 miles inland. The division includes the fertile peatlands at the confluence of the San Joaquin and Sacramento rivers and stretches eastward to the summit of the Sierra. In it lies part of the fabled Mother Lode country, an attraction to tourists. A growing number of national companies have located in the division, among them a large chocolate manufacturer, a major producer of glass and this air products plant beside which stands Division Manager Walter D. Skinner. The area is a big producer of dairy products, vegetables, fruits, lumber and fertilizer. It is also a food processing center. With many miles of waterways, the Stockton area is noted for its boating opportunities.

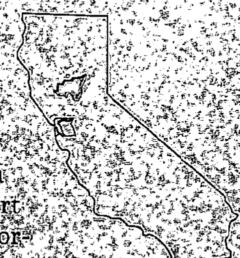
THE MAJESTIC coast redwoods are a main feature of the Humboldt Division, headquartered in Eureka. These giant trees support an important tourist industry and, together with other types of timber, make the area a center for lumber and forest products. Miles of coastline cut by many rivers provide important sport and commercial fishing. Division Manager Victor C. Novarino stands beside Humboldt Bay, famous for its shellfish. In the background is one of two big new pulp mills, the first ones designed to utilize redwood chips. Situated at Eureka is PG&E's Humboldt Bay Power Plant with its 52,000-kilowatt nuclear unit and nearby is the dairy country of the Eel River meadows.

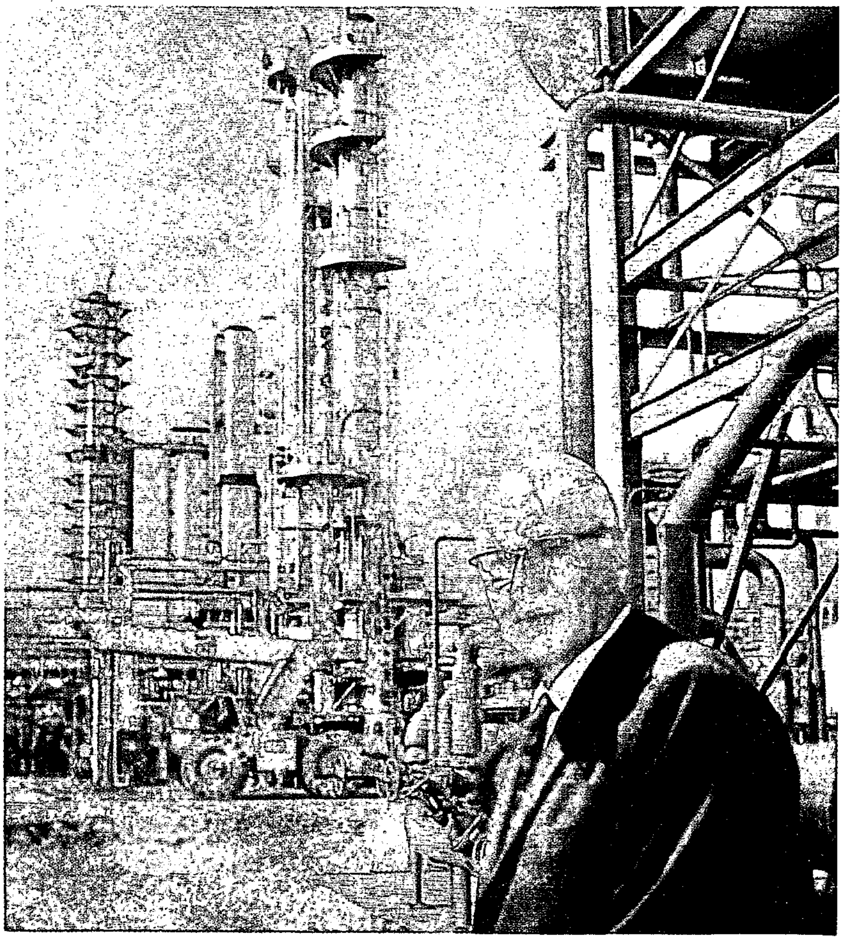


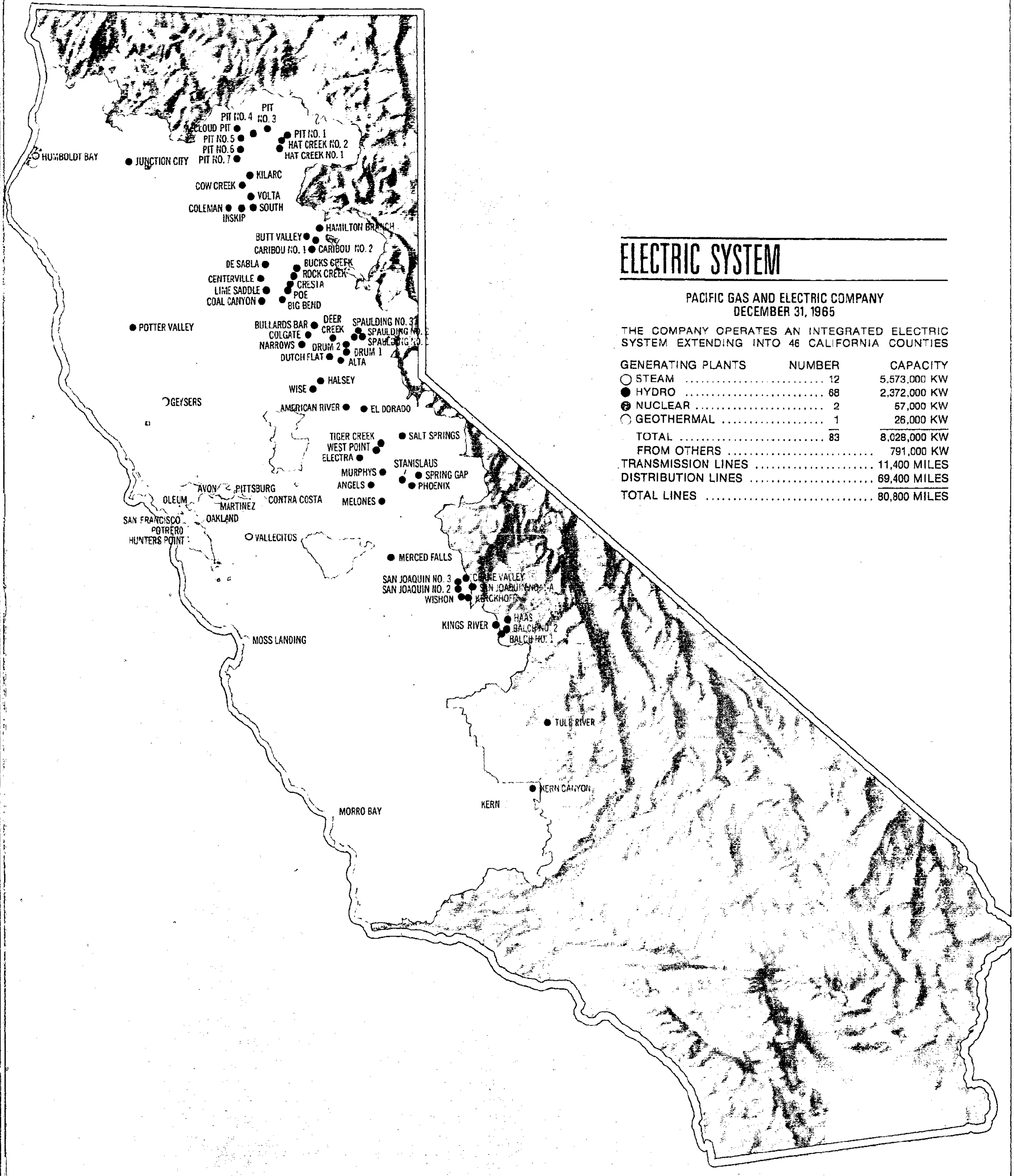
COLGATE AND EAST BAY

WATER is the key to Colgate Division, a rich agricultural land in the center of the Sacramento Valley. Here the monumental Oroville Dam, to be completed in 1968, will impound 3.5 million acre-feet of water for eventual transfer for agricultural, industrial and domestic uses in the San Joaquin Valley and Southern California. The division is the largest rice producing area in the state and has some of the finest waterfowl hunting in the nation. The world's largest walnut grove is in Colgate, and it also claims the title of "Peach Bowl of the World." Here Division Manager Willard L. Murray (at left in top picture) discusses the peach harvest with a local grower. Industries of many types are within the division, which has its headquarters in Marysville.

AN $80 MILLION expansion of a major oil refinery to include a hydrocracking plant three times the size of the largest yet built is typical of the industrial boom in the East Bay Division. Oil refineries, one of which is partly visible behind Division Manager Harold F. Carr, have made the area a principal petroleum and petrochemical center. Here, too, are located some of PG&E's largest steam-electric generating plants. Mills of two national steel firms are being expanded and new industrial parks are developing rapidly. The division is the home of the University of California at Berkeley and a center for nuclear research. The area of Oakland, division headquarters, is a heavily populated residential, industrial and business center. The division includes a number of excellent port facilities and is an important transportation center.







ELECTRIC SYSTEM

PACIFIC GAS AND ELECTRIC COMPANY
DECEMBER 31, 1965

THE COMPANY OPERATES AN INTEGRATED ELECTRIC SYSTEM EXTENDING INTO 46 CALIFORNIA COUNTIES

GENERATING PLANTS	NUMBER	CAPACITY
○ STEAM	12	5,573,000 KW
● HYDRO	68	2,372,000 KW
NUCLEAR	2	57,000 KW
GEOTHERMAL	1	26,000 KW
TOTAL	83	8,028,000 KW
FROM OTHERS		791,000 KW
TRANSMISSION LINES		11,400 MILES
DISTRIBUTION LINES		69,400 MILES
TOTAL LINES		80,800 MILES

OPERATIONS AND ADMINISTRATION

ELECTRIC OPERATIONS

Despite the good water year in 1965, which caused a reduction in sales for irrigation pumping and resale, system electric output reached 39.2 billion kilowatt hours. This is an increase of 4% over 1964. Because of the favorable water conditions, hydroelectric generation accounted for 34% of the total output, a substantial increase over the normal expectation. Company steam-electric generating plants produced 51%, and the remaining 15% was obtained from other producers.

The peak demand on our system, which occurred on December 20, amounted to 6,836,000 kilowatts.

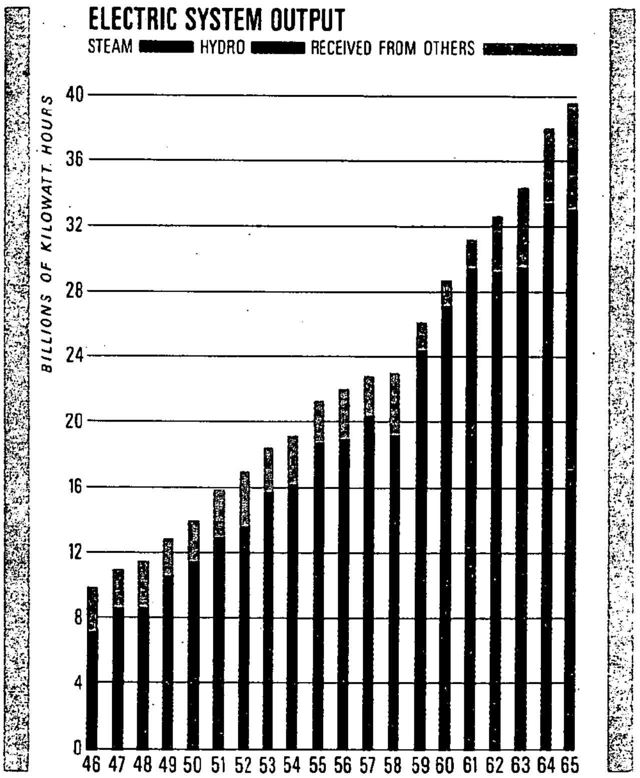
Placed in operation in 1965 were three new powerhouses at the McCloud-Pit hydro development, adding 252,500 kilowatts of capacity. Also completed were the 45,000 kilowatt expansion of Drum Powerhouse and, in San Francisco, the 210,000 kilowatt Potrero Power Plant Unit 3.

Further advances in nuclear power generation were made last year at the Company's two atomic plants. At Vallecitos, steam from an advanced superheat reactor developed by General Electric Company and a group of utilities is being used to generate power. It replaces the boiling water reactor retired late in 1963 after its developmental job had been accomplished.

Our nuclear unit at Humboldt Bay Power Plant is back on the line after a scheduled shutdown for its first refueling after more than two years of continuous operation. One quarter of the initial core was replaced with a new fuel which is clad in a zirconium alloy, an advanced sheathing which promises lower fuel costs.

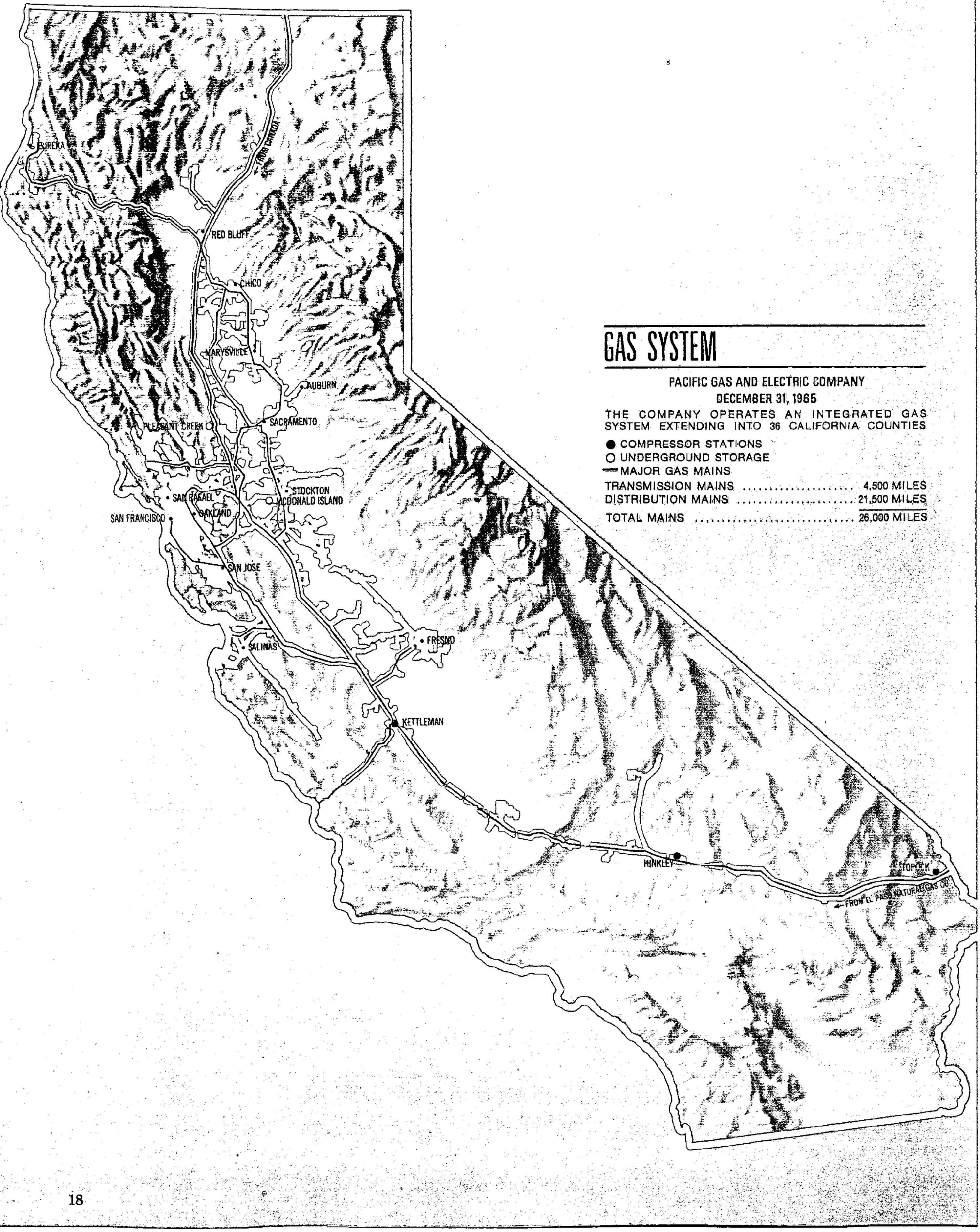
Using helicopters, cranes with giant 150-foot booms and 65 different kinds of vehicles, Company crews are building more than a thousand miles of extra high voltage lines. The lines will carry power at 500,000 volts from the Company's big new thermal plants and will also be part of the Pacific Northwest-Southwest Intertie.

Further progress was made on the nation's largest relighting program: PG&E's four-year project to replace 110,000 Company-owned incandescent street lights with mercury vapor units. The new units increase street lighting levels by about 100 per cent, yet cost less to operate and maintain. The availability of these new units has encouraged many municipalities to expand greatly the number of street lights.



At year-end the Company had 1,605,000 kilowatts of generating capacity under construction as follows:

Completion Date		*Estimated Capacity (KW)*
1966	McCloud-Pit No. 1 (hydro)	77,500
1966	Geysers No. 3 (geothermal)	27,500
1967	Moss Landing No. 6 (conventional steam)	750,000
1968	Moss Landing No. 7 (conventional steam)	750,000



GAS SYSTEM

PACIFIC GAS AND ELECTRIC COMPANY

DECEMBER 31, 1965

THE COMPANY OPERATES AN INTEGRATED GAS SYSTEM EXTENDING INTO 36 CALIFORNIA COUNTIES

● COMPRESSOR STATIONS
○ UNDERGROUND STORAGE
═ MAJOR GAS MAINS

TRANSMISSION MAINS	4,500 MILES
DISTRIBUTION MAINS	21,500 MILES
TOTAL MAINS	26,000 MILES

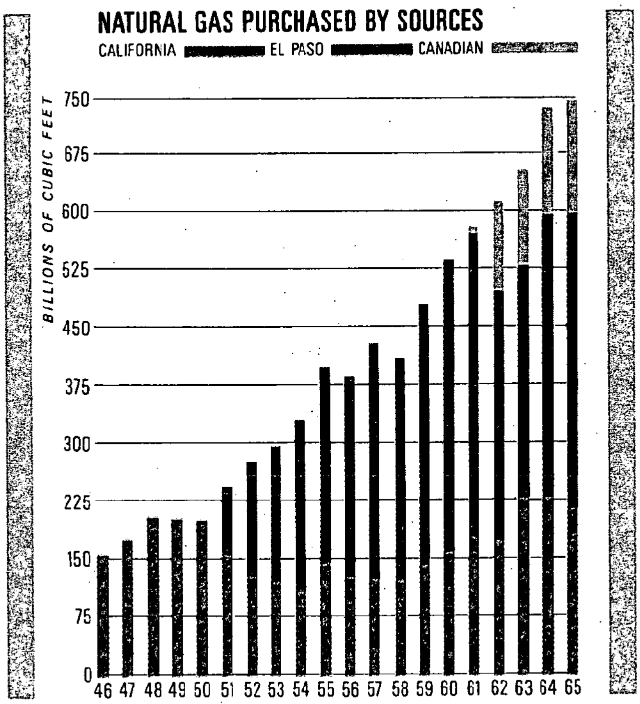
GAS OPERATIONS

While our natural gas customers doubled in number in the past 15 years, their total gas consumption tripled. As mentioned in the opening letter, to keep ahead of this rising demand the Company is proposing to increase its imports of Canadian gas by about one half. Also, important new discoveries of natural gas continue to be made in California. The Company, for instance, last year completed a pipeline from the Dutch Slough field near Antioch which will add up to one hundred million cubic feet a day to the system supply.

Gas system sendout reached an all-time peak on December 17 when consumption reached 3,112 million cubic feet. To meet these peak demands our underground gas storage fields, particularly McDonald Island, are especially helpful.

As is shown on the chart on this page, the sources of gas purchased by PG&E have been subject to major changes in the past two decades. Prior to 1950 gas produced in California was the sole source of the Company's supply. Throughout the 1950's gas obtained through the El Paso Natural Gas Company system from the southwestern states became increasingly important and represented over 70% of total purchases by 1960. Completion of the Alberta-California pipeline in 1961 enabled the Company to tap a third major source of gas in western Canada. In 1965 about 51% of our supply came from the El Paso system, 29% from California and 20% from Canada. It is expected that reserves of gas from these three areas will provide an adequate supply for many years.

Major additions to the Company's gas transmission system were completed in 1965. Natural gas is being brought into presently unserved areas as quickly as it is economically feasible. Rights of way are being obtained to extend a 12-inch main 64 miles to serve the homes and industries in Ukiah and Cloverdale. These are now served by propane-air systems which the Company has purchased from the City of Ukiah and from a private owner in Cloverdale.



BUSINESS DEVELOPMENT

The dynamic growth of the Western market in general and of California in particular has resulted in a wave of new industrial plants and plant expansions in PG&E's service area.

The past year was marked by announcements of, or start of construction on, giant industrial plants such as a fully-integrated steel mill, four new oil refineries and an $80 million addition to a fifth, a major glass factory, a large building materials plant and a number of big food processing and chemical plants.

In the ten years 1956-65, inclusive, more than five billion dollars were invested by major firms in new industrial plants, plant expansions and new businesses in our area. These capital investments created jobs for almost 160,000 people and increased payrolls by at least $1.2 billion annually.

The Company's Area Development Department co-

CUSTOMERS	1965	1964	Increase during 1965
Electric Department	2,323,896	2,254,267	69,629
Gas Department	2,008,623	1,944,503	64,120
Water Department	13,416	13,243	173
Steam Department	527	535	* 8
Total	4,346,462	4,212,548	133,914

*Denotes red figure.

operates with other agencies in promoting the location of new industries in our service territory. The department advises communities on how to attract new industries and businesses as well as residents. Last year it assisted in the organization of several "Congresses for Community Progress." In these town hall type meetings civic leaders and interested citizens take stock of their community's needs and draft civic betterment programs.

California is the leading agricultural state in the nation and the progress of agriculture in our territory is of direct concern to the Company. The ending of Public Law 78 (the Bracero program) affected crop production and some commodity prices and is hastening the development of more automatic harvesters and of crop varieties that will lend themselves to automated picking. Electric energy has long played an important role on farms in the Company's territory. PG&E holds on-site demonstrations of new power-using farm machinery to aid the farmers.

Other load-building activities include coordinated sales and advertising programs to promote sales of appliances. One indication of the success of these programs is the fact that average annual use of electricity by our residential customers reached 4,454 kilowatt-hours in 1965, an increase of 205 kilowatt-hours over 1964, and almost one third more than the 3,451 kilowatt-hours used by the average household in 1960.

EMPLOYEES

There were 21,004 men and women on the Company payroll at the end of 1965, an increase of 1,158 employees over the previous year. Most of the increase represents employees engaged in construction of the Company's big extra high voltage transmission system.

As tasks grow more complex and tools and equipment become more specialized, formal training programs for our employees are being stepped up. Last year one employee in five was selected to attend some type of formal Company training. The courses cover managerial as well as technical skills. All executive officers, division managers and department heads have participated in professional management seminars conducted by a management consultant firm.

In 1965 our employees established the best safety record in the Company's history. As compared with 1964, there was a reduction of 9% in the number of lost-time injuries, and a reduction of 13% in the frequency rate of such injuries. Our injury frequency rate continues to be substantially below the average for the electric utility industry.

Wages and salaries amounted to $174,828,000 in 1965, of which $102,787,000 was paid to operating employees and charged against income. The balance was paid to employees engaged in construction activities and was charged to capital accounts.

At midyear, basic wage rates were increased by 3.25% under the terms of a three-year contract negotiated in 1963 with the International Brotherhood of Electrical Workers (IBEW) and the Engineers and Scientists of California (ESC). In addition, Company contributions to the medical plans of the Pacific Service Employees Benefit Association were increased at midyear as provided by the IBEW and ESC contracts.

During 1965 the Company again took part in a number of local and state programs designed to encourage young men and women to complete their education and so prepare themselves for useful careers. Teachers and students regularly visit our offices and facilities to learn more about the business and technical world. These tours provide the Company with an opportunity to stress the fact that we are an equal opportunity employer and that hiring and promotion are based on merit alone and without regard to racial, religious or other considerations.

DIRECTORS AND OFFICERS

Following the death of James B. Black, who had provided outstanding executive leadership for almost 30 years, the Board of Directors on April 7, 1965 elected Robert H. Gerdes Chairman of the Board and Chief Executive Officer. Shermer L. Sibley was elected President and Chief Operating Officer.

Mr. Gerdes had been President and Chief Executive Officer since 1963 and prior thereto had been Executive Vice President since 1954. Mr. Sibley had been Vice President and General Manager since 1958.

On April 21, 1965, Reed O. Hunt was elected to the Board to fill the vacancy caused by Mr. Black's death. Mr. Hunt is Chairman of the Board and Chief Executive Officer of Crown Zellerbach Corporation.

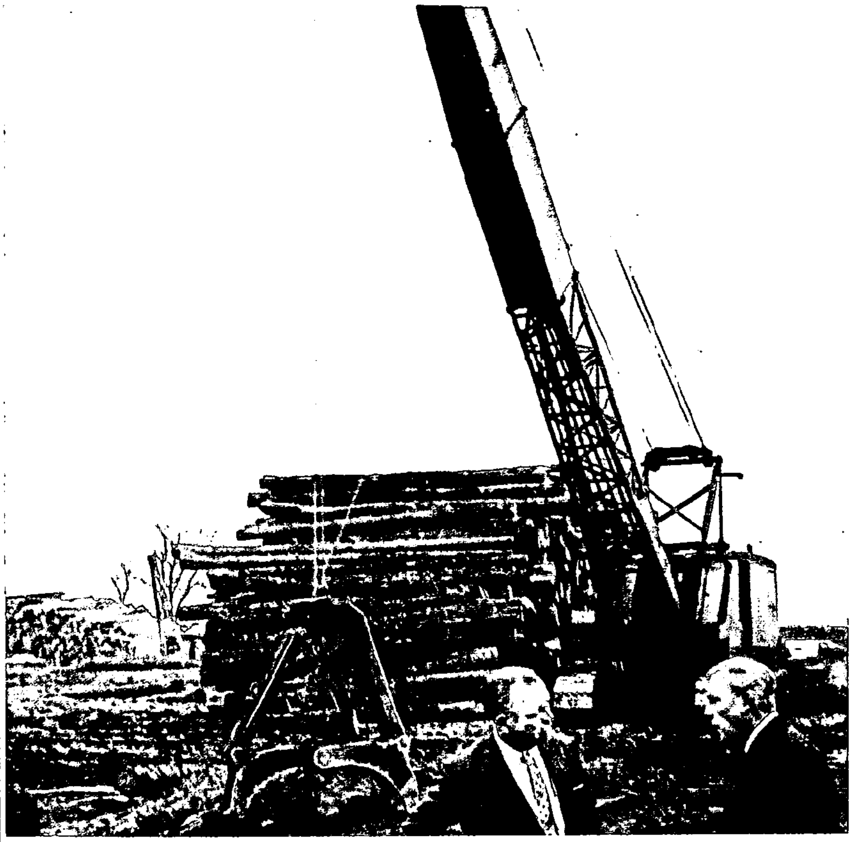
On May 1 a change was made in the organizational structure of the Company. The then vacant office of Vice President and General Manager was eliminated and four positions of Senior Vice President were established. The new Senior Vice Presidents named were John F. Bonner and R. W. Joyce, with primary reporting responsibility to Mr. Sibley, and K. C. Christensen and Richard H. Peterson, with primary reporting responsibility to Mr. Gerdes. Each Senior Vice President has reporting to him vice presidents, other executive officers, and managers representing the various areas of Company operation.

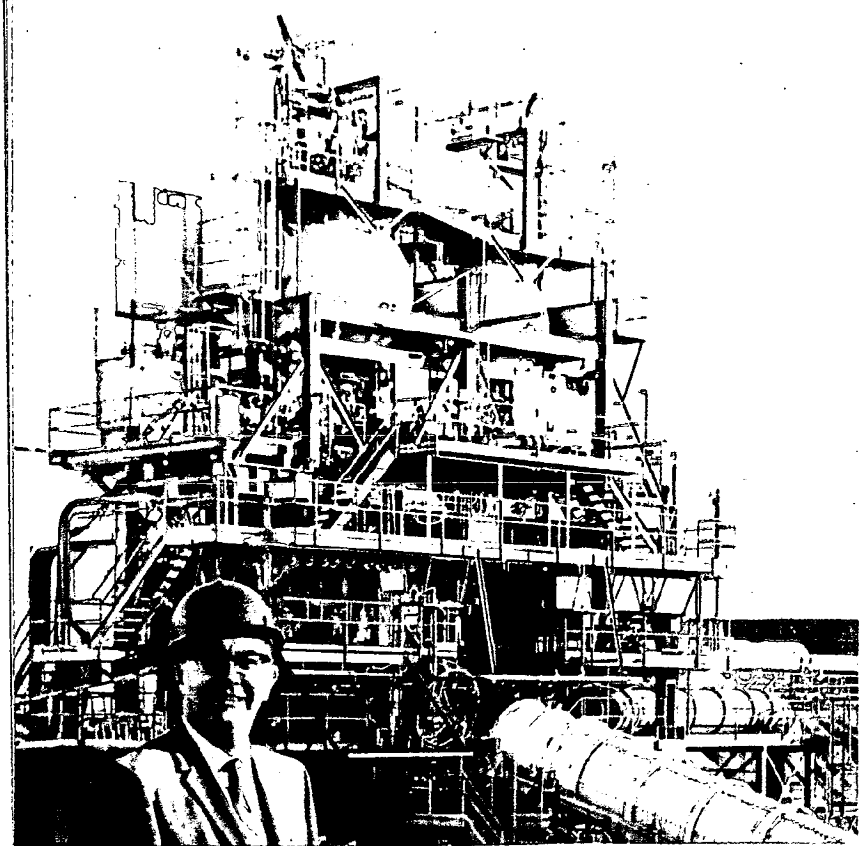
This new executive structure relieves some of the burdens that had been placed upon the Chairman of the Board and the President by the growth of the Company. It also permits additional delegation of authority, should serve to develop top officers and allows a greater degree of management flexibility.

Vern C. Redman, manager of the San Joaquin Division, was appointed Vice President—Commercial Operations on June 1. At the same time Frederick W. Mielke, Jr. was appointed Vice President and Assistant to the Chairman. Mr. Mielke had been assistant to Mr. Gerdes when the latter was President.

On November 18 Mr. Joyce died after a brief illness. He had been a valued and respected executive of the Company for 18 years, the last four as Vice President and then Senior Vice President. Following Mr. Joyce's untimely death, Richard L. Hayden, Vice President—Personnel and General Services, was elected Senior Vice President on November 30. On December 1, John G. Smith, manager of Purchasing and Stores, was elected Vice President—Personnel and General Services.

(The Management will solicit proxies for the annual meeting to be held at the office of the Company, 245 Market Street, San Francisco, California, on Tuesday, April 26, 1966. In connection with such solicitation, it is expected that the proxy statement and form of proxy will be mailed to stockholders on or about March 18, 1966.)





SHASTA AND SACRAMENTO

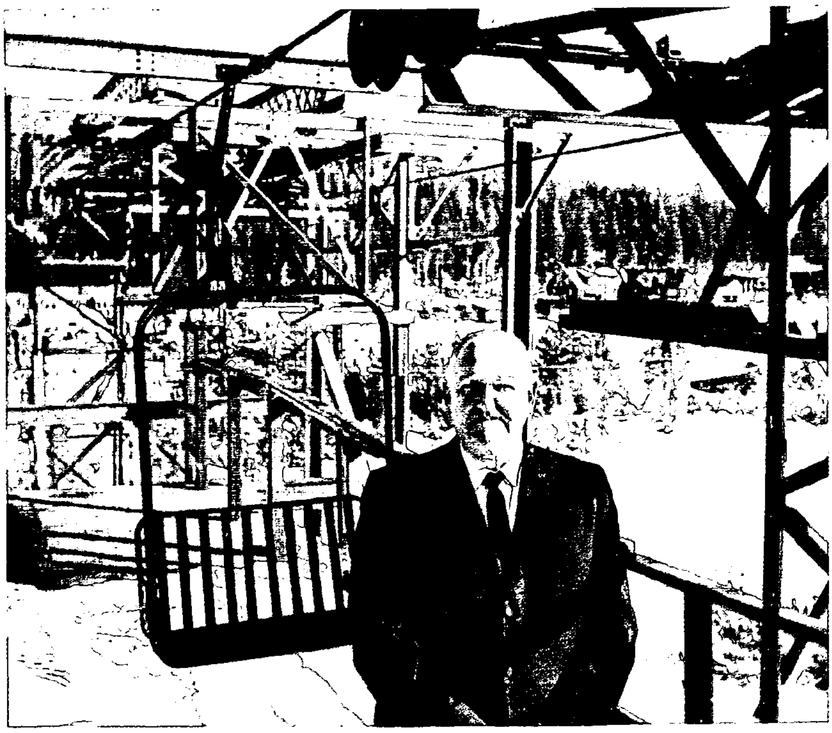
A LAND of mountains, farmlands, forests and rushing rivers is Shasta Division. Lumber, plywood and paper are produced by modern new plants. At one of these plants, Division Manager Lee W. Brillhart, at left, inspects the log storage area with a plant executive. The McCloud and Pit rivers produce more power (725,000 kilowatts) than any other river system on the Company's electric network. A major new cement plant consumes large quantities of natural gas from the 1,400-mile Canadian gas line. A growing area noted for its recreational opportunities, Shasta Division, with headquarters in Red Bluff, includes the olive center of Corning, Lassen Volcanic National Park and Shasta Lake Recreation Area. It also contains numerous cattle ranches and, in the Trinity Mountains, wilderness areas accessible only to experienced outdoorsmen.

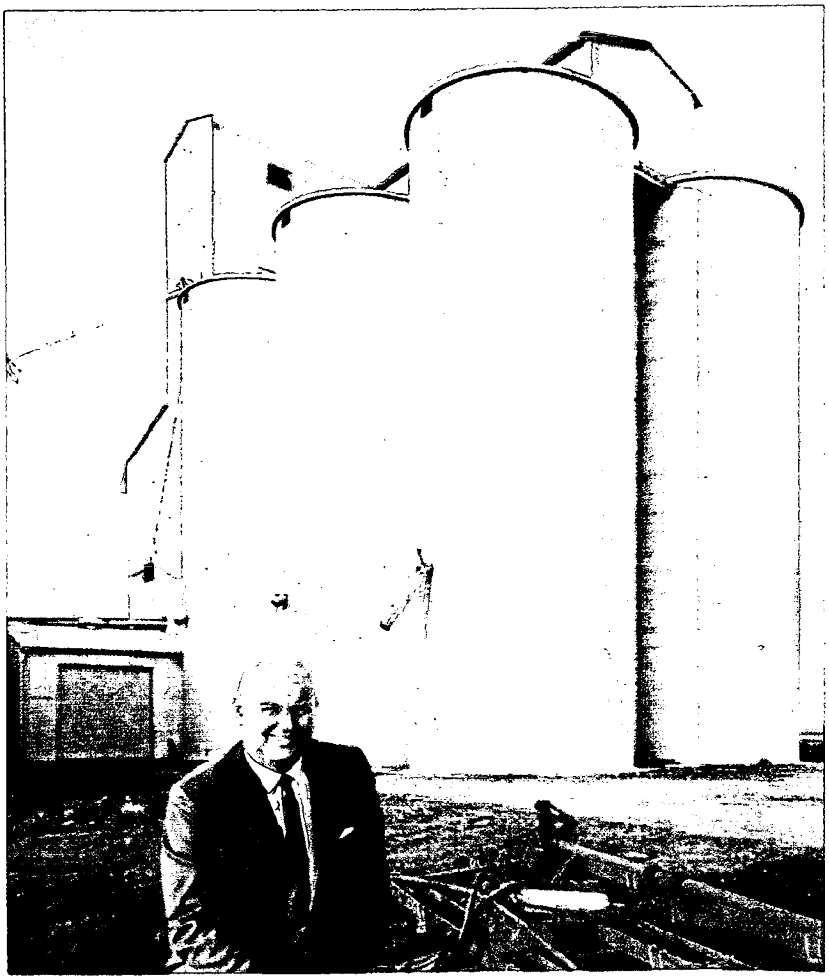
HEADQUARTERS of Sacramento Division is California's capital, Sacramento, one of the inland deep water ports from which produce of the valley, particularly rice, is shipped. The diversity of the entire PG&E system is typified in this division. Engines and fuel for rockets are produced by plants not far from where John Sutter built his pioneer fort. Division Manager Kenneth C. Porter stands beside a huge stand on which the engines for the Gemini rockets were tested. Rich natural gas fields are in the division, as are the timbered mountains of the Sierra. It is an area of summer homes and recreation, strategically located industrial parks and productive farmlands, big Air Force bases and the University of California's Davis campus.

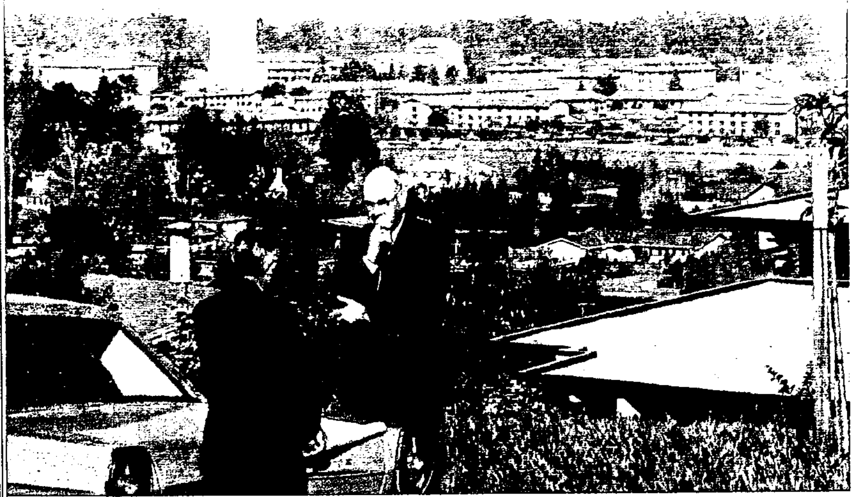
DRUM AND DE SABLA

SOME of the oldest gold mining communities in the state, including the division headquarters city of Auburn, are in Drum Division. The division also includes some of the newest industries, such as a $15 million building products plant rising in the midst of ranch lands on the Sacramento Valley floor. From there, Drum Division rises in a succession of wooded hills to the summit of the Sierra Nevada. Modern freeways and rail lines cross the Sierra, making Drum Division a heavily-travelled gateway to California. Lumber, pears, almonds and minerals are among its products. So is recreation – summer and winter – and Manager William D. Laughlin considers the red steel framework of a ski slope chairlift high in the Sierra almost a symbol of Drum Division.

FROM THE GREAT ranches of the Sacramento Valley to the tall pine country of the Sierra, DeSabla Division covers a variety of resources and scenery. Its geographic backbone is the spectacular Feather River canyon, with its "stairway of power" developed by PG&E. The division produces natural gas as well as electric power and is a center for sugar beets, nuts, cattle, and dairy products. Another major crop, rice, is stored in the silos behind Division Manager Ellis B. Langley. Food processing plants and agricultural equipment firms abound. In the mountains that cover much of the division are the big PG&E reservoirs of Almanor and Bucks Lake which provide water for power and recreation for thousands. Division headquarters are in Chico, an educational and commercial center for the growing area.



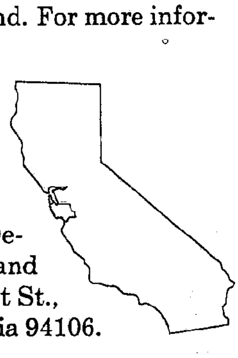




SAN JOSE

YOUTH, vitality and a preoccupation with the future mark San Jose Division. Covering most of the San Francisco Peninsula, the fertile plain south of the bay and oceanside resort areas, the division is the fastest growing area of the PG&E system. Almost one fourth of Northern and Central California's population increase since 1958 has occurred in San Jose Division. Stimulating this growth are the great educational institutions which have attracted aerospace and electronic industries in growing numbers. These schools include San Jose State, Santa Clara University, the new University of California at Santa Cruz and Stanford University, shown here with Division Manager L. J. Brundige in the foreground. Succeeding Brundige, who retired on December 31, is C. Elliot Ginochio, pictured at a Santa Clara County electronics plant. Despite its vast residential areas, its great auto assembly and food machinery factories and its many other industries, the division also produces an abundance of agricultural products including cherries, field crops and $10 million worth of cut flowers annually.

LIKE a glimpse in a kaleidoscope, any summary of PG&E's service territory can offer only an impression of the form and color of this vigorous land. For more information about business opportunities in Northern and Central California or for specific assistance in locating a plant or business here, write: Manager, Area Development, Pacific Gas and Electric Co., 245 Market St., San Francisco, California 94106.



REVENUES AND SALES

ELECTRIC AND GAS DEPARTMENTS BY CLASSES OF SERVICE

ELECTRIC DEPARTMENT	1965	1964	Increase Amount	Increase Per Cent
REVENUES:				
Residential	$ 193,219,065	$ 183,108,666	$ 10,110,399	5.5%
Commercial	190,277,116	181,371,401	8,905,715	4.9
Industrial (1000 kw demand or over)	70,645,968	65,908,285	4,737,683	7.2
Agricultural Power	50,572,841	54,930,675	* 4,357,834	* 7.9
Public Street and Highway Lighting	8,653,119	8,208,620	444,499	5.4
Other Electric Utilities	14,551,062	16,658,193	* 2,107,131	*12.6
Miscellaneous	10,352,005	8,717,438	1,634,567	18.8
TOTAL	$ 538,271,176	$ 518,903,278	$ 19,367,898	3.7%
SALES—Kilowatt Hours:				
Residential	8,543,621,421	7,850,728,715	692,892,706	8.8%
Commercial	9,598,447,112	8,960,017,039	638,430,073	7.1
Industrial (1000 kw demand or over)	7,589,860,973	6,914,438,780	675,422,193	9.8
Agricultural Power	3,628,496,328	4,069,702,328	* 441,206,000	*10.8
Public Street and Highway Lighting	259,665,248	244,760,230	14,905,018	6.1
Other Electric Utilities	2,063,228,193	2,552,613,619	* 489,385,426	*19.2
Total Sales to Customers	31,683,319,275	30,592,260,711	1,091,058,564	3.6
Delivered for the Account of Others	2,386,056,830	1,662,579,115	723,477,715	43.5
TOTAL	34,069,376,105	32,254,839,826	1,814,536,279	5.6%

GAS DEPARTMENT	1965	1964	Increase Amount	Increase Per Cent
REVENUES:				
Residential	$ 163,143,142	$ 160,420,278	$ 2,722,864	1.7%
Commercial	40,221,605	39,731,486	490,119	1.2
Industrial	91,235,162	85,275,367	5,959,795	7.0
Other Gas Utilities	15,776,822	7,931,967	7,844,855	98.9
Miscellaneous	385,031	368,728	16,303	4.4
TOTAL	$ 310,761,762	$ 293,727,826	$ 17,033,936	5.8%
SALES—Thousands of Cubic Feet:				
Residential	202,600,838	200,326,514	2,274,324	1.1%
Commercial	60,782,777	60,178,943	603,834	1.0
Industrial	218,803,490	202,326,759	16,476,731	8.1
Other Gas Utilities	55,109,865	24,590,614	30,519,251	124.1
Total Sales to Customers	537,296,970	487,422,830	49,874,140	10.2
Company Use (Steam plants)	174,954,248	216,714,600	* 41,760,352	*19.3
TOTAL	712,251,218	704,137,430	8,113,788	1.2%

*Denotes red figure.

[redacted]

STATEMENT OF EARNED SURPLUS

PACIFIC GAS AND ELECTRIC COMPANY
FOR THE YEARS ENDED DECEMBER 31, 1965 AND 1964

	1965	1964
BALANCE, JANUARY 1	$275,040,672	$224,529,036
NET INCOME	140,272,450	125,836,100
SPECIAL CREDIT—Investment tax credit for 1963 and 1962		7,469,279
OTHER ADDITIONS (DEDUCTIONS)—Net	1,813,445	(1,089,228)
Total	417,126,567	356,745,187
DIVIDENDS DECLARED—Cash:		
First preferred stock	18,335,609	18,335,619
Common stock (1965—$1.20, 1964—$1.10 a share)	70,483,715	63,368,896
Total	88,819,324	81,704,515
BALANCE, DECEMBER 31	$328,307,243	$275,040,672

The accompanying notes to financial statements are an integral part of this statement.

ACCOUNTANTS' OPINION

HASKINS & SELLS
CERTIFIED PUBLIC ACCOUNTANTS

120 MONTGOMERY STREET
SAN FRANCISCO 94104

February 17, 1966

The Shareholders and the Board of Directors of
Pacific Gas and Electric Company:

We have examined the financial statements and schedules of Pacific Gas and Electric Company for the year ended December 31, 1965. Our examination was made in accordance with generally accepted auditing standards, and accordingly included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances.

In our opinion, the accompanying balance sheet and schedules of capital stock and mortgage bonds and the statements of income and earned surplus present fairly the financial position of the Company at December 31, 1965 and the results of its operations for the year then ended, in conformity with generally accepted accounting principles applied on a basis consistent with that of the preceding year.

Haskins & Sells

STATEMENT OF INCOME

PACIFIC GAS AND ELECTRIC COMPANY
FOR THE YEARS ENDED DECEMBER 31, 1965 AND 1964

	1965	1964
OPERATING REVENUES:		
Electric	$538,271,176	$518,903,278
Gas	310,761,762	293,727,826
Other	2,366,005	2,328,206
Total	851,398,943	814,959,310
OPERATING EXPENSES:		
Power purchased	14,114,816	10,372,949
Natural gas purchased	223,614,742	222,316,099
Oil and other fuel	8,692,972	8,304,970
Other production	13,179,274	12,692,139
Transmission	7,647,669	7,633,516
Distribution	35,148,039	33,296,368
Maintenance	36,709,025	37,007,152
Customer accounts	27,056,674	26,224,594
Sales promotion	7,801,498	7,418,385
Administrative and general	32,867,066	30,768,914
Depreciation (Note 4)	92,774,439	89,706,911
Taxes (Note 4):		
Federal income—current	68,630,000	66,307,000
Federal income—deferred—net (credit)	(2,679,510)	(2,840,244)
Other	99,548,286	95,089,884
Total	665,104,990	644,298,637
OPERATING INCOME	186,293,953	170,660,673
OTHER INCOME	2,261,447	2,486,785
Total	188,555,400	173,147,458
INCOME DEDUCTIONS:		
Interest on mortgage bonds	53,258,954	49,655,626
Interest charged to construction (credit)	(8,677,988)	(5,671,368)
Other	3,701,984	3,327,100
Total	48,282,950	47,311,358
NET INCOME	$140,272,450	$125,836,100

The accompanying notes to financial statements are an integral part of this statement.

BALANCE SHEET

PACIFIC GAS AND ELECTRIC COMPANY
DECEMBER 31, 1965 AND 1964

ASSETS

	1965	1964
UTILITY PLANT—At original cost	$3,957,153,885	$3,697,637,986
Accumulated depreciation (Note 4)	922,953,845	847,121,238
Utility plant—net	3,034,200,040	2,850,516,748
INVESTMENTS—At cost:		
Subsidiaries (Notes 1 and 3)	22,956,545	25,828,601
Nonutility property and other	3,721,359	3,398,523
Total investments	26,677,904	29,227,124
CURRENT ASSETS:		
Cash	25,559,508	25,183,111
Temporary cash investments		9,023,946
Accounts receivable (less allowance for uncollectible accounts: 1965, $1,813,780; 1964, $1,788,605)	73,414,820	67,897,111
Materials and supplies—at average cost	26,994,208	24,485,377
Gas stored underground—at average cost	22,626,655	19,236,052
Prepayments	60,930,289	55,565,999
Total current assets	209,525,480	201,391,596
DEFERRED DEBITS:		
Unamortized bond discount and expense—net	6,800,595	7,131,744
Other	682,547	2,120,154
Total deferred debits	7,483,142	9,251,898
TOTAL	$3,277,886,566	$3,090,387,366

The accompanying notes to financial statements are an integral part of this statement.

BALANCE SHEET

PACIFIC GAS AND ELECTRIC COMPANY
DECEMBER 31, 1965 AND 1964

LIABILITIES

	1965	1964
CAPITALIZATION:		
Capital stock (Schedule 1):		
First preferred stock	$ 350,249,775	$ 350,249,775
Common stock	587,366,620	587,366,620
Excess of premiums over discount and expense on outstanding shares	167,636,008	167,636,008
Total capital stock	1,105,252,403	1,105,252,403
Earned surplus	328,307,243	275,040,672
Total capital stock and surplus	1,433,559,646	1,380,293,075
Mortgage bonds (Note 3) (Schedule 2)	1,466,416,000	1,407,897,000
Total capitalization	2,899,975,646	2,788,190,075
CURRENT LIABILITIES:		
Notes payable to banks	46,000,000	
Accounts payable	59,277,413	43,020,073
Customer deposits	5,510,939	5,212,094
Taxes accrued (Note 4)	100,937,080	101,443,904
Interest accrued	5,126,063	5,015,877
Dividends payable	17,621,674	16,153,519
Mortgage bonds—current portion (Note 3) (Schedule 2)	7,782,000	7,957,000
Total current liabilities	242,255,169	178,802,467
CUSTOMER ADVANCES FOR CONSTRUCTION	9,180,748	7,973,846
DEFERRED CREDITS	4,929,213	2,223,360
RESERVES FOR INSURANCE AND CASUALTIES	8,709,291	7,994,595
CONTRIBUTIONS IN AID OF CONSTRUCTION	42,958,226	32,415,580
ACCUMULATED DEFERRED TAXES ON INCOME (Note 4)	69,878,273	72,787,443
TOTAL	$3,277,886,566	$3,090,387,366

The accompanying notes to financial statements are an integral part of this statement.

CAPITAL STOCK—SCHEDULE 1

DECEMBER 31, 1965

Description	*Shares Authorized*	*Outstanding—Held by Public* *Shares*	*Amount*
FIRST PREFERRED, CUMULATIVE, PAR VALUE $25 PER SHARE (Note 2):			
6% (see Note)	4,211,662	4,211,662	$ 105,291,550
5½%	1,173,163	1,173,163	29,329,075
5%	400,000	400,000	10,000,000
5% redeemable	2,860,977	2,860,977	71,524,425
5% redeemable—Series A	1,750,000	1,719,388	42,984,700
4.80% redeemable	1,517,375	1,517,375	37,934,375
4.50% redeemable	1,127,426	1,127,426	28,185,650
4.36% redeemable	1,000,000	1,000,000	25,000,000
Redeemable (unclassified in series)	5,959,397		
TOTAL	20,000,000	14,009,991	350,249,775
COMMON, PAR VALUE $10 PER SHARE (see Note)	75,000,000	58,736,662	587,366,620
TOTAL			937,616,395
EXCESS OF PREMIUMS OVER DISCOUNT AND EXPENSE ON OUTSTANDING SHARES			167,636,008
TOTAL CAPITAL STOCK			$1,105,252,403

NOTE: Capital stock outstanding includes warrants for the issuance of one share of 6% first preferred stock and 233 shares of common stock.

MORTGAGE BONDS—First and Refunding—SCHEDULE 2

DECEMBER 31, 1965

Series	*Interest Rate %*	*Maturity*	*Outstanding—Held by Public*	*Held in Treasury*
I	3½	June 1, 1966	$ 927,000	
J	3	Dec. 1, 1970	18,324,000	
K	3	June 1, 1971	23,789,000	
L	3	June 1, 1974	109,101,000	
M	3	Dec. 1, 1979	77,376,000	
N	3	Dec. 1, 1977	47,962,000	
O	3	Dec. 1, 1975	4,100,000	$ 300,000
P	2¾	June 1, 1981	22,686,000	50,000
Q	2⅞	Dec. 1, 1980	60,365,000	
R	3⅛	June 1, 1982	67,878,000	73,000
S	3	June 1, 1983	69,801,000	53,000
T	2⅞	June 1, 1976	71,119,000	1,217,000
U	3⅜	Dec. 1, 1985	42,823,000	
W	3⅛	Dec. 1, 1984	52,765,000	162,000
X	3⅛	June 1, 1984	59,459,000	
Y	3⅜	Dec. 1, 1987	41,930,000	
Z	3⅜	Dec. 1, 1988	17,282,000	1,000,000
AA	4½	Dec. 1, 1986	30,969,000	
BB	5	June 1, 1989	58,000,000	
CC	3¾	Dec. 1, 1978	64,927,000	699,000
DD	4½	June 1, 1990	53,723,000	164,000
EE	5	June 1, 1991	60,025,000	
FF	4⅝	June 1, 1992	54,135,000	
GG	4½	June 1, 1993	56,757,000	
HH	4⅜	June 1, 1994	58,437,000	
II	4¼	June 1, 1995	52,788,000	132,000
JJ	4½	June 1, 1996	63,750,000	117,000
KK	4½	Dec. 1, 1996	62,000,000	
LL	4⅝	June 1, 1997	71,000,000	4,000,000
TOTAL			1,474,198,000	$7,967,000
Mortgage Bonds Included in Current Liabilities (Note 3)			7,782,000	
Mortgage Bonds Included in Capitalization			$1,466,416,000	

NOTE: The amount of First and Refunding Mortgage Bonds currently authorized ($2,000,000,000) may be increased from time to time by the Board of Directors. Additional bonds, of other series, may be issued subject to provisions of the related bond indenture.

The accompanying notes to financial statements are an integral part of these schedules.

NOTES TO FINANCIAL STATEMENTS

PACIFIC GAS AND ELECTRIC COMPANY
DECEMBER 31, 1965 AND 1964

NOTE 1 SUBSIDIARIES:

The financial statements relate to the Company only because the assets and revenues of the subsidiaries were not significant in relation to those of the Company. The Company's equity in the net assets of the subsidiaries as of December 31, 1965 was $21,716,195 ($1,240,350 less than its investment) and in the results of operations for the year ended December 31, 1965 and 1964 was $1,520,597 and $1,520,693. Dividend income was $1,130,370 and $1,166,545 for the years 1965 and 1964, respectively.

NOTE 2 PREFERRED STOCK:

Preferred stock outstanding at December 31, 1965 included 8,225,166 shares subject to redemption, at the option of the Company, at par value ($25) per share plus a premium of $.75 to $2.25, depending upon the series and date fixed for redemption.

NOTE 3 MORTGAGE BONDS:

The Company is required, according to provisions of the First and Refunding Mortgage Bond indenture, to make semi-annual sinking-fund payments for the retirement of the bonds. Such payments due during the years ending December 31, 1966 and 1965 are included, net of treasury bonds, in current liabilities.

All real properties and substantially all personal properties are subject to the lien of the mortgage. Securities representing investments in subsidiaries are pledged as collateral for the bonds.

NOTE 4 DEPRECIATION AND TAXES ON INCOME:

For financial statement purposes depreciation on utility plant has been computed on a straight-line remaining life basis at rates based on the estimated useful lives of plant properties. For Federal income tax purposes amortization on utility plant completed under certificates of necessity and depreciation on substantially all other plant additions have been computed, as permitted by the Treasury Department, by liberalized methods and guideline lives. The Company is normalizing the tax effect of accelerated amortization on plant completed under certificates of necessity.

With respect to income tax reductions arising from use of liberalized depreciation the California Public Utilities Commission issued an order in 1960 that it will not allow as an operating expense for rate-making purposes any amount for income taxes which is in excess of the amount of taxes assessed and paid. Income tax reductions arising from the use of liberalized depreciation for tax purposes, and from the investment tax credit (1965—$5,861,000; 1964—$5,294,000), have been taken into income.

NOTE 5 COMMITMENTS:

Utility plant construction expenditures for the year 1966 are estimated at $279,000,000.

The Company provides retirement and savings fund plans for eligible employees. Provisions for such plans (including amounts charged to construction) for the year 1965 were $12,692,000. At December 31, 1965 the unfunded liability, as computed by actuaries, was approximately $9,755,000.

Most of the Company's hydroelectric developments are subject to Federal Power Commission licenses which provide that the United States government shall have the right, upon the expiration of the license, to take over the project upon payment of "net investment" in project plus severance damages, determined in accordance with the Federal law under which the license was issued. The Federal Power Commission has under consideration the promulgation of regulations with respect to determination of the "net investment" in such projects. The effect of such regulations as may be adopted is not presently determinable.

DEPARTMENTAL ORGANIZATION

ELECTRIC OPERATIONS
C. R. Machen, *Assistant to Vice President – Electric Operations*
MANAGERS:
Elmer F. Kaprielian, *Power Control*
Paul Matthew, *Steam Generation*
J. N. Spaulding, *Water Systems*
H. R. Daniels, *Hydro Generation*
R. F. Stuart, *Substations*
H. J. Stefanetti, *Transmission and Distribution*
R. L. Brinton, *Communications*
F. D. Beardsley, *System Protection*

GAS OPERATIONS
MANAGERS:
R. D. Smith, *Gas System Design*
M. A. Richford, *Gas Utilization*
R. T. Peterson, *Gas Control*
K. B. Anderson, *Pipe Line Operations*
E. F. Sibley, *Gas Distribution*
S. A. Haavik, *Natural Gas Production*
J. J. Pugh, *Gas System Planning*
N. H. Neel, *Gas Purchase Department*

ENGINEERING
J. D. Worthington, *Assistant to Vice President – Engineering*
W. R. Johnson, *Chief Electric Generation and Transmission Engineer*
Thomas A. Bettersworth, *Chief Electric Distribution Engineer*
E. V. Noe, *Chief Engineering Services*
William O. Cheney, *Chief Engineering Research*
W. M. Pickslay, *Chief Computer Application Engineer*
B. W. Shackelford, *Chief Civil Engineer*
D. V. Kelly, *Chief Mechanical Engineer*
H. R. Perry, *Chief Planning Engineer*

RATES AND VALUATION
MANAGERS:
Edward C. Ritchie, *Valuation Department*
John F. Roberts, *Rate Department*
John R. Kleespies, *Economics and Statistics Department*

COMPTROLLER
ASSISTANT COMPTROLLERS:
John Brass, Jr.
Granger F. Hill
MANAGERS:
Richard B. Luce, *Plant Accounting*
Dexter Stoner, *Accounting Methods and Procedures*
George Kestner, *Customer Accounting*
L. D. Coughran, *General Accounting*
Frank A. Peter, *Assistant to the Comptroller*

TREASURER
MANAGERS:
E. C. Paddock, *Credit and Collections Department*
J. A. Crockwell, *Insurance Department*

PERSONNEL DEPARTMENT
MANAGERS:
Harry M. McKnight, *Personnel Relations*
V. J. Thompson, *Industrial Relations*

GENERAL CONSTRUCTION
MANAGERS:
Joe Pirtz, Jr., *Civil and Hydro Construction*
C. R. Martin, *Station Construction*
Myron A. Kirsch, *Line Construction*
M. H. Chandler, *Gas Construction*
R. B. Thompson, *Field Office Operations and Personnel*
V. Hugo Irons, *General Construction Services*

COMMERCIAL OPERATIONS
MANAGERS:
Walter D. Howell, *General Sales*
Albert B. Cook, *Commercial Department*
J. G. Foster, *Residential Sales*
R. I. Mendes, *Market Research and Sales Control*
J. S. Walsh, *Area Development*
F. G. Rothganger, *Commercial, Industrial and Agricultural Sales*
Allen D. Owen, *Customer Services*

LAND DEPARTMENT
S. B. Barton, *Manager*

TAX DEPARTMENT
Francis J. Carr, *Manager*

INTERNAL AUDITING DEPARTMENT
Frank P. Lallement, *Manager*

LAW DEPARTMENT
SENIOR ATTORNEYS:
William B. Kuder
William E. Johns
Malcolm H. Furbush
John A. Sproul
John C. Morrissey
Richard A. Raftery
Charles T. VanDeusen
Malcolm A. MacKillop

CLAIMS AND SAFETY DEPARTMENT
R. W. White, *Manager*

AUTOMOTIVE DEPARTMENT
Gerald P. Larson, *Manager*

PURCHASING AND STORES DEPARTMENT
F. F. Mautz, *Manager*

ADVERTISING AND PUBLICITY DEPARTMENT
A. J. McCollum, *Manager*
W. A. Hynes, *Manager Public Activities*

DIVISION MANAGERS

COAST VALLEYS: Leigh H. Smith, Salinas
COLGATE: W. L. Murray, Marysville
DE SABLA: Ellis B. Langley, Chico
DRUM: William D. Laughlin, Auburn
EAST BAY: Harold F. Carr, Oakland
HUMBOLDT: V. C. Novarino, Eureka
NORTH BAY: E. S. Day, San Rafael
SACRAMENTO: K. C. Porter, Sacramento
SAN FRANCISCO: H. A. Lee, San Francisco
SAN JOAQUIN: Earl E. Foley, Fresno
SAN JOSE: L. J. Brundige,* San Jose
SHASTA: Lee W. Brillhart, Red Bluff
STOCKTON: Walter D. Skinner, Stockton

*Retired December 31, 1965, succeeded by C. E. Ginochio

STOCKHOLDERS' CALENDAR

SCHEDULE OF DIVIDEND PAYMENTS

Common Stock		First Preferred Stock	
Record Date	Date Payable	Record Date	Date Payable
March 25	April 15, 1966	January 28	February 15, 1966
June 24	July 15, 1966	April 29	May 16, 1966
September 23	October 15, 1966	July 29	August 15, 1966
December 23	January 16, 1967	October 28	November 15, 1966

STOCK TRANSFER AGENCIES

OFFICE OF THE COMPANY (E. F. Hall, Transfer Agent), San Francisco; BANKERS TRUST COMPANY, New York

REGISTRARS OF STOCK

WELLS FARGO BANK, San Francisco;
CHEMICAL BANK NEW YORK TRUST COMPANY, New York