ADDENDUM TO THE CPSD STAFF REPORT, SECTION IX I.12-01-007

I. PG&E's Long-term Incentive Plan

PG&E's Long-term Incentive Plan (LTIP) provides an incentive that links employee financial rewards to shareholder return. All employees at the Officer and Director and Senior Director level are eligible to receive an award each year. Below this level, 25% of senior level individual contributors and Managers are eligible to receive an award.

Supervisors determine whether an employee receives an award and the amount. The total value of the award is determined on a dollar basis, and converted into a number of shares based on the PG&E share price on the date of the award. They are awarded as: 50% Restricted Stock Units which are hypothetical shares of PG&E stock that vests over a 4-year period, and 50% Performance Shares that vest at the end of a 3-year performance period.

The value of the Performance Shares is determined by shareholder return. If shareholder return is in the highest rank of a comparative group of companies, the greater the award.

Upon the vesting date, PG&E Corporation's total shareholder return is compared to the total shareholder return of the twelve other companies in PG&E's comparator group. If PG&E's total shareholder return falls below the 25th percentile of the comparator group, the settlement percentage for the Performance Shares will be 0%. If PG&E's total shareholder return is at the 75th percentile, the settlement percentage will be 100%; and if PG&E's total shareholder return is in the top rank, the settlement percentage will be 200%. According to PG&E, "The greater our TSR [total shareholder return] at the end of the three-year period compared to our corporate performance comparator group, the greater the award."[1]

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[1] DR_CPUC_198-11Attch02, p. 2.

For example, the guidelines provide Directors with a base salary of $200,000 and above to be eligible to receive a maximum of $200,000 (although most Senior Vice Presidents received $400,000 or above). In most cases, half of the value is comprised of Performance Shares. After vesting, if PG&E's total shareholder return is the highest of the comparative companies, the $200,000 award could increase to $300,000 ($100,000 in Restricted Stock Units, and $200,000 in Performance Shares). If PG&E's shareholder return is in the lowest 25th percentile, the employee's $200,000 award is reduced to just $100,000 for the Restricted Stock Units. The employee does not receive any Performance Shares.

In 2006, the "Chairman, CEO, and President" (one position) received a $7 million LTIP award, equally split between Restricted Stock Units and Performance Shares. If PG&E's shareholder return is in the top rank of its comparative group, that person could receive the full award of up to $10.5 million ($3.5 million Restricted Stock Units and $7 million Performance Shares). The Chief Executive Officer (assume of PG&E Utility) received a $3 million award, also equally split, which could render a full award of up to $4.5 million bonus ($1.5 million in Restricted Stock Units and $3 million in Performance Shares) in 2006.[2]

II. PG&E's Short-term Incentive Plan

The Short-term Incentive Plan (STIP) provides a cash award to employees who are employed in non-bargaining unit positions and some selected bargaining-unit positions. The award uses earnings on operations as a significant portion of the award criteria. The STIP award is based on the employee's earnings, target participation rate for that job classification,[3] the individual employee's performance, and the "final company score."

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[2] PG&E documents show that the Chairman, CEO, and President was first elected on January 1, 2006 and resigned May 31, 2007.

[3] The target participation rate of the employee's job classification varies; from 6% for individual contributors to up to 30% for Senior Directors.

Fifty percent of the multiplier that determines the final company score is based on earnings from operations.

In a message from a Sr. Vice President, "Our Short-Term Incentive Plan (STIP) is designed to promote and reinforce our Vision and Values…." According to a PG&E Annual Rewards Process Overview, the "STIP rewards annual results and impact on the business as measured by company financial and operational results…."[4]

A multi-step formula determines the individual award. For example, if an employee earns $70,000 during the calendar year and the target participation rate for his classification or pay band is 10%, the target award would be $7,000. If the employee performed adequately, the performance score would be 100%,[5] which would leave the $7,000 whole.

The $7,000 is then multiplied by the "final company score," of which 50% is made up by earnings from operations. The other 50% is allocated between a "Brand Health Index," reliable energy delivery, a safety index (employee safety), a survey employee index, and an environmental index. Gas system integrity work is 30% of the reliable energy delivery criterion which is 15% of the final company score. Therefore, gas system integrity work is 4.5% of the final company score.

In 2009, the Earnings from Operations score were 1.574,[6] which means that earnings from operations exceeded its target earnings by about 57%. If all other company score elements met the goals at 100%, the STIP multiplier would be 1.29 (50% of the increase over 100%), which would increase the $7,000 award to $9,030.

According to PG&E, the 2010 Earnings from Operations targets are not publically reported; however, they are consistent with PG&E Corporation's publically disclosed guidance range. In 2010, PG&E applied a range of earnings per share from operations of $3.35 to $3.50. During the first half of 2010, PG&E actual earnings were falling slightly

[4] CPUC_198-32Atch01, p 3.

[5] The guidelines provide performance modifiers that range from 0% to up to 150% depending on the competency of the employee.

short of the target earnings (actual was $1.33 billion). As a result, the earnings-from-operations multiplier was less than 1, or 0.944. If all other company score elements met the goals at 100%, the $7,000 bonus would decrease to $6,608.[7]

In its mid-year progress report, PG&E directs its employees to, "Continue to focus on productivity and efficiency to meet our budget and profitability target. To maximize the value for money we spend to operate, use our precious financial resources as carefully as we would our own personal funds."[8]

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[6] CPUC_198-32Atch05, p 5.

[7] Some elements were higher and some were lower; which resulted in an actual STIP final company score of 0.864. The Gas System Integrity Work was 1.501; which means that PG&E completed all planned gas leak surveys required to achieve a 1.0 score, and exceeded its gas leak survey quality maximum threshold score by nearly 33%.

[8] CPUC_198-32Atch06, p. 5.